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BNP RESIDENTIAL PROPERTIES INC  
Form 10-K  
March 09, 2006

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2005  
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OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 1-9496

BNP RESIDENTIAL PROPERTIES, INC.  
(Exact name of registrant as specified in its charter)

Maryland 56-1574675  
-----  
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

301 S. College St., Suite 3850, Charlotte, NC 28202-6024  
-----  
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code 704/944-0100  
-----

Securities registered pursuant to Section 12(b) of the Act:

| Title of each class<br>-----            | Name of each exchange<br>on which registered:<br>----- |
|---|--|
| Common Stock, par value \$.01 per share | American Stock Exchange                                |

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.  Yes  No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.  Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405

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of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of the Form 10-K or any amendment to this Form 10-K. [ ]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer:

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).  Yes  No

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The aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of June 30, 2005 (the last business day of the registrant's most recently completed second fiscal quarter) was approximately \$145.2 million.

The number of shares of the registrant's common stock outstanding on February 28, 2006 (the latest practicable date) was 10,402,448.

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### CAUTION REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report contains forward-looking statements. You can identify such statements by the use of forward-looking terminology, such as "may," "will," "expect," "anticipate," "estimate," "continue" or other similar words. These statements discuss future expectations, contain projections of results of operations or of financial condition or state other "forward-looking" information.

Although we believe that our plans, intentions and expectations reflected in or suggested by these forward-looking statements are reasonable, we cannot assure you that we will achieve our plans, intentions or expectations. When you consider such forward-looking statements, you should keep in mind the following important factors that could cause our actual results to differ materially from those contained in any forward-looking statement:

- o our markets could suffer unexpected increases in the development of apartments or other rental or competitive housing alternatives;
- o our markets could suffer unexpected declines in economic growth or an increase in unemployment rates;
- o general economic conditions could cause the financial condition of a large number of our tenants to deteriorate;
- o we may be unable to lease or re-lease apartments quickly or on as favorable terms as under existing leases;
- o a decline in revenues from, or a sale of, our restaurant properties could adversely affect our financial condition and results of operations;
- o we may have incorrectly assessed the environmental condition of our properties;
- o an unexpected increase in interest rates could cause our debt service costs to exceed our expectations;
- o we may be unable to meet our long-term liquidity requirements on favorable terms; and
- o we could lose key executive officers.

Given these uncertainties, we caution you not to place undue reliance on forward-looking statements. We undertake no obligation to revise these forward-looking statements if future events or circumstances render them inaccurate.

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## PART I

### ITEM 1. BUSINESS

#### Company Profile

BNP Residential Properties, Inc. is a self-administered and self-managed real estate investment trust ("REIT") with operations in North Carolina, South Carolina and Virginia. Our primary activity is the ownership and operation of apartment communities. We currently own and manage 30 apartment communities containing 7,946 apartment units. We also serve as general partner of limited partnerships that own three properties with 713 apartment units, which we also manage. In addition to our apartment communities, we own 40 properties that we lease on a triple-net basis to a restaurant operator under a master lease.

BNP Residential Properties, Inc. is structured as an UpREIT, or "umbrella partnership real estate investment trust." We are the sole general partner and own a controlling interest in BNP Residential Properties Limited Partnership, through which we conduct all of our operations. We refer to this partnership as the operating partnership. We refer to the limited partners of the operating partnership as "minority common unitholders" or "minority interest." We currently own 80% of the outstanding operating partnership common units.

As of February 28, 2006, we have 10,402,448 shares of common stock outstanding. We have 1,230 shareholders of record, and we estimate that there are approximately 2,900 beneficial owners of our common stock. Our shares are listed on the American Stock Exchange, trading under the symbol "BNP." The operating partnership has an additional 2,534,619 operating partnership minority common units outstanding.

We have 240 employees, including management, accounting, legal, acquisitions, development, property management, leasing, maintenance and administrative personnel. Our executive offices are located at 301 South College Street, Suite 3850, Charlotte, North Carolina 28202-6024, and our telephone number is 704/944-0100.

In addition to this Annual Report, we file quarterly and special reports, proxy statements and other information with the SEC. All documents that we file with the SEC are available free of charge on our corporate website, which is [www.bnp-residential.com](http://www.bnp-residential.com). You may also read and copy any document that we file at the public reference facilities of the SEC at 450 Fifth Street NW, Washington, D.C. 20549. Please call the SEC at (800) SEC-0330 for further information about the public reference facilities. These documents also may be accessed through the SEC's electronic data gathering, analysis and retrieval system ("EDGAR") via electronic means, including the SEC's home page on the Internet (<http://www.sec.gov>). In addition, since some of our securities are listed on the American Stock Exchange, you can read our SEC filings at the offices of the American Stock Exchange, 86 Trinity Place, New York, New York 10006.

#### History and Development of BNP Residential Properties, Inc.

The company was originally incorporated in the state of Delaware in 1987. Beginning in 1987, we elected to be taxed as a REIT under the Internal Revenue Code. As such, we generally are not, and will not be, subject to federal or state income taxes on net income. As a REIT, we are subject to a number of organizational and operational requirements, including a requirement that we

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currently distribute at least 90% of our REIT taxable income as dividends.

In 1987, we purchased 47 existing restaurant properties located in North Carolina and Virginia for an aggregate purchase price of \$43.2 million. From 1987 through 1992, our assets consisted primarily of these 47 restaurant properties. During this period we operated as an externally administered and

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externally managed REIT. We leased the restaurants on a triple-net basis to Boddie-Noell Enterprises, Inc., a restaurant operator, under a master lease. A master lease is a single lease that covers multiple properties, while a triple-net lease is one where the lessee pays all operating expenses, maintenance, property insurance and real estate taxes.

In 1993, we began to change our focus from restaurant properties to apartment communities, with the objective of increasing funds from operations and enhancing shareholder value. In 1994 we acquired BT Venture Corporation, an integrated real estate company specializing in the management, development and acquisition of apartment properties, and we began operating as a self-administered and self-managed REIT.

In 1997, we reincorporated in the state of Maryland and reorganized to our present UpREIT structure. Through our UpREIT structure, we can acquire properties in exchange for operating partnership units and trigger no immediate tax obligation for certain sellers. We believe that our conversion to an UpREIT enables us to acquire properties not otherwise available or at lower prices because of the tax advantages to certain property sellers of receiving limited partnership interests instead of cash as consideration. Minority unitholders will generally be able to redeem their units for cash or, at our option as general partner, for shares of common stock of the company on a one-for-one basis. Distributions of cash from the operating partnership are allocated between the REIT and the minority unitholders based on their respective unit ownership.

In December 2001, our Board of Directors authorized the issuance of Series B Cumulative Convertible Preferred Stock. Between 2001 and 2003, we issued a total of 909,090 shares of this preferred stock for proceeds of \$10 million. During 2004, we raised \$30 million of new equity through the issuance of 2.6 million shares of common stock to a number of institutional investors and mutual funds.

From 1993 through 2004, we acquired 26 apartment properties through a combination of cash purchases, assumption of long-term debt, and issuance of operating partnership units. In several cases, we combined two properties to operate as single apartment communities.

To date we have sold seven restaurant properties to Boddie-Noell Enterprises, the lessee, under an agreement that allowed the lessee to close up to seven restaurants and buy them back for no less than net carrying value.

### Recent Developments

In January 2005, we acquired Boddie Investment Company through a merger. As a result of this acquisition, we have assumed the role of general partner and acquired certain economic interests in three limited partnerships (a 50% interest in Marina Shores Associates One, Limited Partnership, 1% interest in The Villages of Chapel Hill Limited Partnership, and 1% interest in The Villages of Chapel Hill - Phase 5 Limited Partnership). Prior to this acquisition, we managed the apartment communities owned by these partnerships on a contract basis; we will continue to manage these properties. We now include

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these limited partnerships in our consolidated financial statements.

During 2005, we continued to add to and improve our portfolio of apartment properties with eight acquisitions. We made four of these acquisitions through issuance of operating partnership units, and another four acquisitions through direct purchases. Also during 2005 and for the first time in our history, we sold one apartment community.

In November 2005, the company redeemed all 909,090 shares of our Series B Cumulative Convertible Preferred Stock on a one-for-one basis through issuance of 909,090 shares of our common stock.

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### Business Strategy

Our principal investment objective is to provide our shareholders with a combination of current income and long-term appreciation in the value of the company's common stock. We focus on increasing long-term growth in funds from operations and funds available for distribution per share, and on increasing the value of our portfolio through effective management, growth, financing and investment strategies. We expect to implement our strategies primarily through the acquisition, operation, leasing and management of apartment communities.

We seek to acquire apartment properties in the southeastern United States. We focus on markets that exhibit substantial economic growth and an expanding job base that provide opportunities for us to quickly build a significant market presence. Through our UpREIT structure, we have the ability to acquire apartment communities by issuing operating partnership units in tax-deferred exchanges with owners of such properties. We expect that we will finance future acquisitions of apartment communities with operating partnership units as well as loans and funds from additional offerings of common stock, preferred stock or joint venture arrangements.

We will selectively consider opportunities to add additional units to existing communities, to acquire and rehabilitate older apartment communities, and to develop new apartment communities. Members of our management team have directed over \$116 million of development or redevelopment projects, including 15 apartment communities containing over 2,900 apartment units. This development and redevelopment experience will enable us to build additional apartment communities and to rehabilitate existing communities when economic conditions and available capital make such opportunities attractive.

We strongly emphasize on-site property management. We seek opportunities and have developed internal programs to increase average occupancy rates, reduce resident turnover, raise rents and control costs. On-site community managers report directly to regional managers who are locally based. This flat organization provides for efficient staffing levels, reduces overhead expenses, and enables us to respond to the needs of residents and on-site employees. In an effort to reduce long-term operating costs, we regularly review each apartment community and promptly attend to maintenance and recurring capital needs. Our employees supervise all renovation and repair activities, which are generally completed by outside contractors.

We continue to seek additional sources of revenue at our existing apartment communities. These include water submetering and marketing of cable television, high-speed Internet service and telephone services.

### ITEM 1A. RISK FACTORS

An investment in our securities involves various risks, including those

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described below. You should consider carefully these risk factors together with all of the other information included in this Annual Report before deciding to purchase or sell our securities.

Some of the information in this discussion of risk factors may contain forward-looking statements. Please review our Caution Regarding Forward-Looking Statements at the beginning of this Annual Report. When considering such forward-looking statements, you should keep in mind the risk factors and other cautionary statements in this Annual Report. The risk factors noted in this section and other factors noted throughout this Annual Report, including certain risks and uncertainties, could cause our actual results to differ materially from those contained in any forward-looking statement.

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Geographic concentration of our properties makes our business vulnerable to economic downturns in North Carolina, South Carolina or Virginia.

All of our properties are located in North Carolina, South Carolina and Virginia. Adverse economic developments in these states could adversely impact the operations of our properties and therefore our profitability. The concentration of properties in a limited number of markets may expose us to risks of adverse economic developments that are greater than the risks of owning properties in many markets. Our revenues and the value of our properties may be affected by a number of factors, including the local economic climate (which may be adversely impacted by business layoffs, downsizing or industry slow downs), changing demographics and other factors.

Our apartment communities are subject to multiple operating risks.

Our apartment communities are subject to operating risks common to apartment communities in general. Such risks include:

- o competition from other apartment communities;
- o alternative housing, including home ownership, especially during times of low mortgage interest rates;
- o new construction of comparable properties or adverse economic conditions in the areas in which our apartment communities are located, either of which might adversely affect apartment occupancy or rental rates;
- o increases in operating costs (including insurance and real estate taxes), which may not necessarily be offset by increased rents; and
- o the inability or unwillingness of residents to pay rent increases.

The local rental market may limit the extent to which we may increase rents in response to operating expense increases without decreasing occupancy rates. Any of the above events could adversely affect our ability to make distributions.

A decline in revenues from, or a sale of, our restaurant properties could adversely affect our financial condition and results of operations.

We own 40 restaurant properties that we lease on a triple-net basis to Boddie-Noell Enterprises, Inc. The master lease for our restaurant properties requires Boddie-Noell Enterprises to pay us annual rent equal to the greater of

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a specified minimum rent or 9.875% of food sales. If Boddie-Noell Enterprises renews the master lease, after December 2007, it has the right to terminate the lease on up to five restaurants per year by offering to purchase them under specified terms.

The original lease was for 47 restaurant properties. Since 1999, we have sold seven restaurant properties deemed non-economic to Boddie-Noell Enterprises under an agreement that allowed the lessee to close up to seven restaurants and buy them back for no less than net carrying value. As a result of these sales, we received total proceeds of \$4.4 million, which equaled the net carrying value of the properties.

Of the 40 restaurant properties we currently own, 39 are operated as Hardee's and one is operated as a B-B-Q & Ribs. The minimum rent on the 40 restaurants is \$3.8 million per year.

As a result of favorable sales, our restaurant rental income peaked in 1992 at \$5.3 million, which was substantially above the then-current minimum rent. However, from 1992 through 2002, restaurant sales declined each year. In 2003, Hardee's, the concept at the majority of our restaurant properties,

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introduced the "Thick-Burger" product line and began seeing significant sales increases; and same-store sales at our restaurant properties increased by 2.4%. These increases continued into 2004, with same-store sales for 2004 improving by 8.5% over 2003 levels; however, in 2005 same-store sales declined by 5.9% compared to 2004. Even with the recent same-store sales increases, from 1996 through 2005 the revenues of our restaurant properties were below the level requiring payments in excess of the minimum rent. For us to receive percentage rent in 2006, same-store sales would have to increase by 7.1% from 2005 levels. Given the current state of flux in the fast-food industry, we are uncomfortable making a prediction or relying on the forecasts of others as to future sales trends for our restaurant properties. For this reason, we have based our plans and expectations on continuing to receive the minimum rent in 2006.

In order to protect our stockholders from declining restaurant revenues from 1992 through 2002, we began to acquire apartment communities in 1993. We believe that we can more effectively enhance the value of our common stock by acquiring and operating apartment communities. Accordingly, we focused our business primarily on the ownership and operation of apartment communities.

As a consequence of this refocused strategy, we may elect to sell our restaurant properties and reinvest the proceeds in additional apartment communities. No sale of the restaurants is pending, nor are we actively marketing the restaurants. We will only divest the restaurants if we believe doing so will enhance stockholder value.

If we do dispose of the restaurant properties, it is possible that we may incur a loss on the disposition of the properties. It is also possible that we may invest such sale proceeds in properties that yield significantly less than the \$3.8 million we currently receive from Boddie-Noell Enterprises.

Further, in the event we were to find a buyer, Boddie-Noell Enterprises has the right to purchase the restaurants from us on the same terms as that offer. This right may make it more difficult to find a suitable buyer or could adversely affect the price we might realize on any such sale.

For the year ended December 31, 2005, the restaurant properties accounted for 5.3% of our total revenues. All of the restaurant property revenue



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comes from Boddie-Noell Enterprises. The inability of Boddie-Noell Enterprises to pay us rent would adversely affect funds from operations and funds available for distribution.

Boddie-Noell Enterprises, Inc., our restaurant operator, may not renew the restaurant lease at the expiration of its initial term.

We lease our 40 restaurant properties to Boddie-Noell Enterprises, Inc. under a master lease that provides for annual rent equal to the greater of a specified minimum rent, currently \$3.8 million per year, or 9.875% of food sales. The initial term of this lease expires on December 31, 2007. Boddie-Noell Enterprises, at its sole option, has the right to renew the master lease for up to three five-year periods. Under the lease, Boddie-Noell Enterprises is required to give us notice of its intention to terminate at least 180 days prior to the expiration of the initial term; otherwise, the lease will automatically renew.

There is no assurance that Boddie-Noell Enterprises will renew the master lease. In the event Boddie-Noell Enterprises elects to terminate the lease, we would cease to receive rental payments from Boddie-Noell Enterprises and would be forced to seek alternative tenants for the properties, find alternate uses for the properties, or sell the properties.

In the event Boddie-Noell Enterprises does not renew the lease, there is no assurance that we will be able to fully replace the \$3.8 million in revenue that we currently receive from Boddie-Noell Enterprises.

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We have substantial debt obligations, which may reduce our operating performance and adversely affect our ability to pay distributions.

At December 31, 2005, on a consolidated basis, we had \$436.7 million in long-term debt, of which \$388.6 million is related to properties owned in fee by BNP Residential Properties and \$48.1 million is related to properties in which we have a partial ownership interest. Payments of principal and interest on borrowings may leave us with insufficient cash resources to operate the apartment communities or to pay the distributions we must pay to maintain our qualification as a REIT. Further, a high debt level creates an increased risk that we may default on our obligations. If we default, the banks that lent us funds could foreclose on the properties securing their loans.

Because we have a substantial amount of debt that bears interest at variable rates, increases in interest rates would reduce our net income.

At December 31, 2005, we had \$53.7 million in long-term debt at variable interest rates. In addition, we may incur additional debt in the future that also bears interest at variable rates. Variable-rate debt creates higher debt service requirements if market interest rates increase. Such an increase would adversely affect our cash flow and the amounts available to pay dividends.

If our debt cannot be paid, refinanced or extended at maturity, in addition to our failure to repay our debt, we may not be able to make distributions to stockholders at expected levels or at all.

We may obtain financing with "due-on-encumbrance" or "due-on-sale" clauses in which future refinancing or property sales could cause the maturity dates of the mortgages to accelerate and the financing to become due immediately. Thus, we could be required to sell properties on an all-cash basis, or the purchaser might be required to obtain new financing in connection with a sale. Alternatively or additionally, we may obtain mortgages that have balloon

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payments. Such mortgages involve greater risks than mortgages with principal amounts amortized over the term of the loan since our ability to repay the outstanding principal amount at maturity may depend on obtaining adequate refinancing or selling the property. The efficacy of either option would depend on economic conditions in general and the value of the underlying properties in particular. We cannot guarantee that we could refinance or repay any such mortgages at maturity. Further, a significant decline in the value of the underlying property could result in a loss of the property through foreclosure.

We may be liable for environmental contamination for which we do not have insurance and which might have a material adverse effect on our financial condition and results of operations.

Various federal, state and local laws subject property owners or operators to liability for the costs of removal or remediation of certain hazardous substances released on a property. Such laws often impose liability without regard to whether the owner or operator knew of, or was responsible for, the release of the hazardous substances. The presence of, or the failure to remediate properly, hazardous substances may adversely affect occupancy of any contaminated apartment communities, the ability of Boddie-Noell Enterprises to operate restaurants and our ability to sell or borrow against contaminated properties. In addition to the costs associated with investigation and remediation actions brought by governmental agencies, the presence of hazardous wastes on a property could result in personal injury or similar claims by private plaintiffs.

Various laws also impose, on persons who arrange for the disposal or treatment of hazardous or toxic substances, liability for the cost of removal or remediation of hazardous substances at the disposal or treatment facility. These laws often impose liability whether or not the person arranging for the disposal ever owned or operated the disposal facility.

Boddie-Noell Enterprises has agreed to pay for the costs of complying with applicable environmental laws, ordinances and regulations on the restaurant properties. However, the obligation to

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pay for such costs with respect to our other properties, or Boddie-Noell Enterprises' inability to pay for such costs on the restaurant properties, may adversely affect our operating costs and the value of our properties.

Phase I environmental site assessments have been obtained on all of our owned apartment communities. The purpose of Phase I environmental site assessments is to identify potential sources of contamination for which an owner may be responsible and to assess the status of environmental regulatory compliance. All of the restaurant properties were subjected to transaction screens in December 1995. A transaction screen involves a review of a property for the purpose of recommending whether we should perform a Phase I environmental site assessment. A transaction screen is significantly less thorough in scope than a Phase I environmental site assessment.

Neither the transaction screens nor the environmental site assessments revealed any environmental condition, liability or compliance concern that we believe would have a material adverse affect on our business, assets or results of operations. Nor are we aware of any such condition, liability or concern by any other means. However, it is possible that the transaction screens and the environmental site assessments relating to any one of the properties did not reveal all environmental conditions, liabilities, or compliance concerns. It is also possible that there are material environmental conditions, liabilities or

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compliance concerns that arose at a property after the related review was completed.

Unexpected costs associated with compliance with the Americans with Disabilities Act and other laws would impair our operating performance.

Under the Americans with Disabilities Act of 1990 (the "ADA"), all public accommodations and commercial facilities must meet certain federal requirements related to access and use by disabled persons. Compliance with the ADA requirements could require removal of access barriers. Additional federal, state and local laws exist that are related to access by disabled persons. These laws also may require modifications to our properties or restrict renovations of our properties. For example, the Fair Housing Amendments Act of 1988 (the "FHAA") requires apartment communities first occupied after March 13, 1991 to be designed and constructed so as to be accessible to the handicapped. Non-compliance with the ADA, FHAA and similar laws could result in the imposition of fines or an award of damages to private litigants.

Boddie-Noell Enterprises is financially responsible for upgrading the restaurant properties should such properties not be in compliance with the ADA. However, in the event Boddie-Noell Enterprises fails to upgrade properly the restaurants and there is a determination that the restaurant properties are not in compliance with the ADA, we could still face the imposition of fines or an award of damages to private litigants. If we were required to make unanticipated expenditures to comply with the ADA or other laws, our cash flow and the amounts available for distributions to you may be adversely affected.

The Federal Fair Housing Act and state fair housing laws prohibit discrimination on the basis of certain protected classes. We have a policy against these kinds of discriminatory behaviors and train our employees to avoid discrimination and the appearance of discrimination. We cannot assure you that an employee will not violate our policy against discrimination and violate the fair housing laws. Such a violation could subject us to legal action and awards of damages.

Because most of our directors have personal interests that could create a conflict with the interests of our stockholders, we may make decisions that are not in your best interest.

Of our six directors, four have personal interests that could create a conflict between what is in the best interest of our security holders and what is in the best interest of each such director.

- o Messrs. Payne and Wilkerson are executive officers of the company;
- o Messrs. Chrysson and Gilley own significant stakes in the operating partnership.

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Such conflicts of interests could influence board members to take action that is not in the best interest of our security holders.

If we do not qualify as a REIT, we will be subject to tax as a regular corporation and face substantial tax liability.

Beginning with our taxable year ended December 31, 1987, we have elected to be taxed as a REIT under Sections 856 through 860 of the Internal Revenue Code. We believe that beginning with that taxable year we have been organized and have operated in a manner that enables us to qualify for taxation as a REIT, and we intend to continue to operate in such a manner. We can provide

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no assurance, however, that we have operated or will operate in a manner so as to qualify or remain qualified as a REIT. We have not requested, and do not plan to request, a ruling from the Internal Revenue Service that we qualify as a REIT.

If we fail to qualify as a REIT, we would not be allowed a deduction for distributions to stockholders in computing our taxable income and would be subject to federal income tax at regular corporate rates. We also could be subject to the federal alternative minimum tax. Unless we are entitled to relief under specific statutory provisions, we could not elect to be taxed as a REIT for four taxable years following the year during which we were disqualified. Therefore, if we lose our REIT status, the funds available for distribution to you would be reduced substantially for each of the years involved.

At any time, the federal income tax laws governing REITs or the administrative interpretations of those laws may be amended. Any of those new laws or interpretations may take effect retroactively and could adversely affect us or you as a shareholder.

Complying with REIT requirements may cause us to forego otherwise attractive opportunities.

As a REIT, we are subject to annual distribution requirements, including a requirement that we currently distribute at least 90% of our "REIT taxable income" to our common shareholders. These requirements limit the amount of cash we have available for other business purposes, including amounts to fund our growth.

We expect that our cash flow will exceed our REIT taxable income, due to the allowance for depreciation and other non-cash charges in computing REIT taxable income. We anticipate that we generally will have sufficient cash or liquid assets to enable us to satisfy the distribution requirement. It is possible, however, that we may not have sufficient cash or other liquid assets to meet the 90% distribution requirement or to distribute such greater amount as may be necessary to avoid income and excise taxation. In such event, we may find it necessary to borrow funds to pay the required distribution or, if possible, pay taxable stock dividends in order to meet the distribution requirement or avoid such income or excise taxation.

Even if we remain qualified as a REIT, we may face other tax liabilities that reduce our cash flow.

Even if we qualify as a REIT, we and our subsidiaries will be subject to certain federal, state and local taxes on our income and property that could reduce operating cash flow.

Our charter does not permit ownership in excess of 9.8% of our capital stock, and attempts to acquire our capital stock in excess of the 9.8% limit are void without prior approval from our board of directors.

Our charter limits ownership of our capital stock by any single stockholder to 9.8% of the outstanding shares. The charter also prohibits anyone from buying shares if the purchase would cause us to lose our REIT status. This could happen if a share transaction results in fewer than 100 persons owning

all of our shares or five or fewer persons, applying certain broad attribution rules of the Internal Revenue Code, owning 50% or more of our shares. If you or anyone else acquires shares in excess of the ownership limit or in violation of the ownership requirements of the Internal Revenue Code for REITs, we:

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- o will consider the transfer to be null and void;
- o will not reflect the transaction on our books;
- o may institute legal action to enjoin the transaction;
- o will not pay dividends or other distributions with respect to those shares;
- o will not recognize any voting rights for those shares;
- o will consider the shares held in trust for the benefit of the company; and
- o will either direct the affected person to sell the shares and turn over any profit to us, or we will redeem the shares. If we redeem the shares, it will be at a price equal to the lesser of:
  - (a) the price paid by the transferee of the shares or
  - (b) the average of the last reported sales prices on the American Stock Exchange on the 10 trading days immediately preceding the date fixed for redemption by our board of directors.

An individual who acquires shares that violate the above rules bears the risk that (1) he may lose control over the power to dispose of the shares, (2) he may not recognize profit from the sale of such shares if the market price of the shares increases and (3) he may be required to recognize a loss from the sale of such shares if the market price decreases.

Because provisions contained in Maryland law and our governing documents discourage hostile takeover attempts, investors may be prevented from receiving a "control premium" for their shares.

Provisions contained in our charter and bylaws, as well as Maryland general corporation law and the partnership agreement of the operating partnership, discourage hostile takeovers, which may prevent stockholders from receiving a "control premium" for their shares. These provisions include the following:

- o Ownership Limit. The 9.8% ownership limit discussed above may have the effect of precluding acquisition of control of us by a third party without the consent of our board of directors.
- o Required Consent of the Operating Partnership for Significant Corporate Action. A provision in the operating partnership agreement prohibits us from engaging in certain transactions that could result in a change of control without the approval of the holders of a majority of the outstanding units, including units that we own. While we expect that we will always hold a majority of the outstanding units, we cannot guarantee that this will be the case. If we ever own less than a majority of the outstanding units, this voting requirement might limit the possibility for an acquisition or change in control of the company, even if such acquisition or change in control would be in your (the stockholders') best interests. As of December 31, 2005, we owned 80% of the operating partnership common units.
- o Anti-Takeover Protections of Operating Partnership Agreement. The operating partnership agreement contains provisions relating to limited partners' redemption rights in the event of certain changes of

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control of the company. These provisions require an acquiror to maintain the

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operating partnership structure and to maintain a limited partner's right to continue to hold units with future redemption rights. Such provision could have the effect of discouraging a third party from making an acquisition proposal, even if such proposal were in our stockholders' best interests.

- o Poison Pill. We adopted a preferred share purchase rights plan (sometimes referred to as a "poison pill") in March 1999. The plan involves the issuance of preferred share purchase rights to all stockholders. The rights entitle stockholders to purchase capital stock at a discount if a person or group purchases or makes a tender offer for 15% or more of our common stock. Our board of directors may redeem the rights at \$.01 per right until the acquisition of 15% or more of our common stock by a person or group. The purpose of the poison pill is to ensure that any potential purchaser of the company must negotiate with our board before an acquisition. The poison pill may discourage offers for the company, even those in the best interest of the stockholders.
- o Maryland's Unsolicited Takeovers Act. In 1999, the State of Maryland enacted legislation that enhances the power of Maryland corporations to protect themselves from unsolicited takeovers. Among other things, the legislation permits our board, without stockholder approval, to amend our charter to:
  - o stagger our board of directors into three classes;
  - o provide that only remaining directors may fill a vacancy on the board;
  - o provide that only the board can fix the size of the board; and
  - o require that special stockholder meetings may only be called by holders of a majority of the voting shares entitled to be cast at the meeting.

If we lose any of our executive officers, our operating performance could suffer.

We are dependent on the efforts of our executive officers, particularly Philip S. Payne, D. Scott Wilkerson, Pamela B. Bruno and Eric S. Rohm. While we believe that we could find replacements for these key personnel, if necessary, the loss of their services could have an adverse effect on our operations. Messrs. Payne, Wilkerson and Rohm and Ms. Bruno have entered into employment contracts with us.

### ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

### ITEM 2. PROPERTIES

#### Apartment Communities

Through the operating partnership, we own and operate 30 apartment communities consisting of 7,946 apartment units. We also serve as general partner of limited partnerships that own three apartment properties with 713

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apartment units, which we also manage. For the fourth quarter of 2005, our average economic occupancy rate was 94.1%, and our average monthly revenue per occupied unit was \$746. The average age of the apartment communities is 14 years. Our apartment communities are generally wood framed, two- and three-story buildings, with exterior entrances, individually metered gas and electric service, submetered water service, and individual heating and cooling systems.

Our apartment units are comprised of 38% one-bedroom units, 54% two-bedroom units, and 8% three-bedroom units. The units average 980 square feet in area and are well equipped with modern appliances and other conveniences. Our communities generally include swimming pools, tennis courts and clubrooms, and most have exercise facilities.

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As of December 31, 2005, our total investment, on a historical cost basis, in our 30 owned apartment communities was \$509.8 million, and the net carrying value of our 30 apartment communities was \$442.4 million (an average of \$14.7 million per community). In addition, we include three apartment properties owned by limited partnerships that we consolidate, with a cost basis of \$49.8 million and net carrying value of \$42.1 million. The apartment properties are held subject to loans, discussed in the notes to the financial statements.

The table at page 17 summarizes information about each of our apartment communities.

### Restaurant Properties

We lease the restaurant properties on a triple-net basis to Boddie-Noell Enterprises, Inc. under a master lease. The master lease, as amended in 1995, has a primary term expiring in December 2007, but grants Boddie-Noell Enterprises three five-year renewal options. Boddie-Noell Enterprises pays annual rent equal to the greater of the specified minimum rent or 9.875% of food sales from the restaurants. Under certain conditions, and subject to our approval, Boddie-Noell Enterprises has the right to substitute another restaurant property for a property covered by the lease. Assuming renewal of the lease, after December 31, 2007, Enterprises has the right to terminate the lease on up to five restaurant properties per year by offering to purchase them under specified terms.

The original lease was for 47 restaurant properties. Since 1999, we have sold seven restaurant properties deemed non-economic to Boddie-Noell Enterprises under an agreement that allowed the lessee to close up to seven restaurants and buy them back for no less than net carrying value. As a result of these sales, we received total proceeds of \$4.4 million, which equaled the net carrying value of the properties.

The minimum rent on the remaining 40 restaurants is \$3.8 million per year.

The average acquisition cost of the original 47 restaurant properties was \$920,000 per property. The net carrying value of the 40 restaurant properties held at December 31, 2005, was \$24.8 million (an average of \$620,000 per property). The restaurant properties are held subject to a line of credit loan, discussed in the notes to the financial statements.

The restaurant properties are operated by Boddie-Noell Enterprises, which is responsible for all aspects of the operation, maintenance and upkeep of the properties. In addition, Boddie-Noell Enterprises is responsible for the cost of any improvement, expansion, remodeling or replacement required to keep the properties competitive or in conformity with applicable codes and standards.

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Thirty-nine of the restaurant properties are operated as Hardee's restaurants pursuant to franchise agreements with Hardee's Food Systems, Inc. One property is operated as a "B-B-Q & Ribs" restaurant. Boddie-Noell Enterprises converted this property to the B-B-Q & Ribs concept in 2002 and paid for the entire cost of the conversion, approximately \$500,000. There is no applicable franchise agreement for the converted restaurant, as Boddie-Noell Enterprises owns the B-B-Q & Ribs concept.

Each of the restaurant properties consists of a one-story brick, stucco or wood building that embodies a contemporary style with substantial plate glass areas. The buildings average 3,400 square feet and are located on sites averaging 1.2 acres. The buildings are suitable for conversion to a number of uses, but the exteriors would have to be substantially modified prior to their use as restaurants of another concept or for non-restaurant applications.

The locations of our restaurant properties are listed on page 19 of this Annual Report.

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### Property Insurance

We carry insurance coverage on our properties of types and in amounts that we believe are in line with coverage customarily obtained by owners of similar properties. In addition, properties that we manage but do not own are covered by insurance policies under which we are a named insured. Our restaurant properties are subject to an indemnification agreement whereby Boddie-Noell Enterprises, the lessee, is responsible for all claims, including those relating to environmental matters, arising from a restaurant property. Boddie-Noell Enterprises is required to provide insurance, which identifies the company as a named insured, on each restaurant property.

We believe all of our properties are adequately insured, including insurance for acts of terrorism at all of our apartment properties. There are types of losses, however, such as from wars or catastrophic acts of nature, for which we cannot obtain insurance at all or at a reasonable cost. In the event of an uninsured loss or a loss in excess of our insurance limits, we could lose both the revenues generated from the affected property and the capital we have invested in the affected property. It is possible, depending on the specific circumstances of the affected property, that we could be liable for any mortgage indebtedness or other obligations related to the property. Any such loss could materially and adversely affect our business and financial condition and results of operations.

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### INFORMATION ABOUT APARTMENT COMMUNITIES

| Community | Location | No. of<br>Apt.<br>Units | Year<br>Compl | Date<br>Acquired | Total<br>Acreage | Total<br>Rentable<br>Area<br>(Sq. Ft.) | 1<br>BR | 2<br>BR |
|-----------|----------|-------------------------|---------------|------------------|------------------|--|---------|---------|
|-----------|----------|-------------------------|---------------|------------------|------------------|--|---------|---------|

Owned communities:



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|                   |                    |     |      |       |      |         |     |     |
|-------------------|--------------------|-----|------|-------|------|---------|-----|-----|
| Abbingtion Place  | Greensboro, NC     | 360 | 1997 | 12/97 | 37.4 | 400,728 | 96  | 216 |
| Allerton Place    | Greensboro, NC     | 228 | 1998 | 9/98  | 19.2 | 241,842 | 54  | 126 |
| Barrington Place  | Charlotte, NC      | 348 | 1999 | 5/02  | 29.3 | 386,964 | 132 | 192 |
| Brookford Place   | Winston-Salem, NC  | 108 | 1998 | 5/02  | 6.3  | 103,392 | 36  | 72  |
| Carriage Club     | Mooresville, NC    | 268 | 2000 | 6/04  | 22.5 | 253,114 | 110 | 136 |
| Chason Ridge      | Fayetteville, NC   | 252 | 1994 | 1/99  | 29.1 | 246,886 | 56  | 164 |
| Fairington        | Charlotte, NC      | 250 | 1981 | 8/04  | 32.0 | 267,300 | 108 | 106 |
| Hamptons          | Charlotte, NC      | 232 | 1986 | 10/05 | 33.1 | 245,338 | 28  | 184 |
| Laurel Springs 1  | High Point, NC     | 240 | 2003 | 3/05  | 19.0 | 228,000 | 120 | 120 |
| Laurel Springs 2  | High Point, NC     | 96  | 2004 | 3/05  | 7.9  | 122,808 | -   | 24  |
| Madison Hall      | Clemmons, NC       | 128 | 1997 | 8/98  | 10.5 | 110,352 | 42  | 86  |
| Mallard Creek 1   | Charlotte, NC      | 184 | 1988 | 12/94 | 18.4 | 167,920 | 67  | 117 |
| Mallard Creek 2   | Charlotte, NC      | 288 | 1997 | 8/03  | 25.0 | 321,190 | 103 | 140 |
| Marina Waterfront | Cornelius, NC      | 290 | 1994 | 9/02  | 33.6 | 254,356 | 128 | 126 |
| Oak Hollow 1      | Cary, NC           | 222 | 1983 | 7/98  | 30.0 | 215,960 | 56  | 165 |
| Oak Hollow 2      | Cary, NC           | 240 | 1986 | 12/00 | 26.8 | 220,840 | 160 | 80  |
| Oakbrook          | Charlotte, NC      | 162 | 1985 | 6/94  | 16.4 | 178,668 | 32  | 120 |
| Paces Commons     | Charlotte, NC      | 336 | 1988 | 6/93  | 24.8 | 322,046 | 154 | 142 |
| Paces Village     | Greensboro, NC     | 198 | 1988 | 4/96  | 15.5 | 167,886 | 88  | 110 |
| Pelham            | Greenville, SC     | 144 | 1985 | 3/03  | 10.1 | 158,264 | 40  | 104 |
| Pepperstone       | Greensboro, NC     | 108 | 1992 | 12/97 | 10.1 | 113,076 | -   | 108 |
| Salem Ridge       | Winston-Salem, NC  | 120 | 1984 | 3/05  | 6.8  | 87,784  | 40  | 80  |
| Savannah Place    | Winston-Salem, NC  | 172 | 1991 | 12/97 | 15.4 | 182,196 | 44  | 128 |
| Southpoint        | Durham, NC         | 192 | 1987 | 9/04  | 14.5 | 176,352 | 132 | 60  |
| Summerlyn Place   | Burlington, NC     | 140 | 1998 | 9/98  | 12.1 | 156,756 | 48  | 84  |
| Waterford Place   | Greensboro, NC     | 240 | 1997 | 12/97 | 20.6 | 277,296 | 72  | 120 |
| Woods Edge        | Durham, NC         | 264 | 1985 | 6/98  | 32.4 | 268,620 | 66  | 198 |
| Wind River        | Durham, NC         | 346 | 2000 | 5/04  | 29.4 | 391,120 | 128 | 153 |
| Canterbury        | Myrtle Beach, SC   | 630 | 1999 | 3/05  | 41.1 | 518,400 | 274 | 356 |
| Paces Watch       | Mt. Pleasant, SC   | 232 | 1987 | 5/05  | 19.7 | 201,068 | 132 | 100 |
| Waverly Place     | N. Charleston, SC  | 240 | 1986 | 4/05  | 21.3 | 194,994 | 114 | 126 |
| Latitudes         | Virginia Beach, VA | 448 | 1989 | 10/94 | 24.9 | 358,700 | 269 | 159 |
| Timbers           | Richmond, VA       | 240 | 1989 | 10/05 | 27.7 | 232,973 | 58  | 146 |

| Community          | Location          | Weighted<br>Average<br>Apt. Size<br>(Sq. Ft.) | Average Economic<br>Occupancy Percent (1) |      |      | Average<br>Monthly Revenue<br>per Occupied Unit |       |       |
|--------------------|-------------------|---|---|------|------|---|-------|-------|
|                    |                   |   | 2005                                      | 2004 | 2003 | 2005  | 2004  | 2003  |
| Owned communities: |                   |   |   |      |      |   |       |       |
| Abbingtion Place   | Greensboro, NC    | 1,113   | 93.8                                      | 94.2 | 90.9 | \$779   | \$760 | \$764 |
| Allerton Place     | Greensboro, NC    | 1,061   | 95.1                                      | 94.8 | 91.4 | 806   | 790   | 745   |
| Barrington Place   | Charlotte, NC     | 1,112   | 94.6                                      | 94.4 | 94.3 | 771   | 756   | 748   |
| Brookford Place    | Winston-Salem, NC | 961   | 96.0                                      | 97.0 | 95.1 | 683   | 679   | 667   |
| Carriage Club      | Mooresville, NC   | 944   | 96.0                                      | 95.3 | -    | 757   | 743   | -     |
| Chason Ridge       | Fayetteville, NC  | 980   | 93.8                                      | 96.4 | 96.6 | 781   | 797   | 753   |
| Fairington         | Charlotte, NC     | 1,069   | 94.7                                      | 93.7 | -    | 733   | 708   | -     |
| Hamptons           | Charlotte, NC     | 1,057   | 96.0                                      | -    | -    | 711   | -     | -     |
| Laurel Springs 1   | High Point, NC    | 950   | 94.0                                      | -    | -    | 634   | -     | -     |
| Laurel Springs 2   | High Point, NC    | 1,279   | 89.6                                      | -    | -    | 846   | -     | -     |
| Madison Hall       | Clemmons, NC      | 862   | 95.4                                      | 94.0 | 94.2 | 602   | 600   | 578   |
| Mallard Creek 1    | Charlotte, NC     | 912   | 94.5                                      | 95.0 | 93.3 | 643   | 635   | 663   |
| Mallard Creek 2    | Charlotte, NC     | 1,115   | 93.5                                      | 93.8 | 92.0 | 783   | 747   | 739   |
| Marina Waterfront  | Cornelius, NC     | 877   | 95.3                                      | 94.6 | 91.0 | 837   | 772   | 750   |

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|                 |                    |       |      |      |      |     |     |     |
|-----------------|--------------------|-------|------|------|------|-----|-----|-----|
| Oak Hollow 1    | Cary, NC           | 982   | 96.5 | 93.9 | 90.0 | 614 | 616 | 617 |
| Oak Hollow 2    | Cary, NC           | 920   | 91.9 | 92.0 | 89.1 | 605 | 604 | 599 |
| Oakbrook        | Charlotte, NC      | 1,100 | 94.3 | 94.6 | 91.9 | 729 | 698 | 709 |
| Paces Commons   | Charlotte, NC      | 958   | 94.5 | 95.2 | 92.2 | 667 | 632 | 660 |
| Paces Village   | Greensboro, NC     | 848   | 96.0 | 94.9 | 94.3 | 678 | 675 | 654 |
| Pelham          | Greenville, SC     | 1,106 | 94.7 | 95.6 | 91.1 | 570 | 559 | 569 |
| Pepperstone     | Greensboro, NC     | 1,047 | 96.7 | 96.3 | 93.8 | 696 | 668 | 655 |
| Salem Ridge     | Winston-Salem, NC  | 732   | 97.3 | -    | -    | 531 | -   | -   |
| Savannah Place  | Winston-Salem, NC  | 1,059 | 93.1 | 93.0 | 93.4 | 727 | 716 | 699 |
| Southpoint      | Durham, NC         | 919   | 96.1 | 91.3 | -    | 702 | 690 | -   |
| Summerlyn Place | Burlington, NC     | 1,120 | 95.6 | 94.3 | 93.5 | 827 | 826 | 832 |
| Waterford Place | Greensboro, NC     | 1,155 | 94.5 | 95.1 | 91.8 | 904 | 883 | 852 |
| Woods Edge      | Durham, NC         | 1,018 | 94.0 | 93.6 | 92.7 | 694 | 705 | 722 |
| Wind River      | Durham, NC         | 1,130 | 94.4 | 86.1 | -    | 800 | 820 | -   |
| Canterbury      | Myrtle Beach, SC   | 822   | 96.6 | -    | -    | 621 | -   | -   |
| Paces Watch     | Mt. Pleasant, SC   | 867   | 96.2 | -    | -    | 856 | -   | -   |
| Waverly Place   | N. Charleston, SC  | 812   | 93.9 | -    | -    | 658 | -   | -   |
| Latitudes       | Virginia Beach, VA | 800   | 96.3 | 97.5 | 96.5 | 978 | 919 | 873 |
| Timbers         | Richmond, VA       | 971   | 88.3 | -    | -    | 871 | -   | -   |

(continued)

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| Community                 | Location           | No. of<br>Apt.<br>Units | Year<br>Compl | Date<br>Acquired | Total<br>Acreage | Total<br>Rentable<br>Area<br>(Sq. Ft.) | Apartme<br>Unit Ty |         |
|---------------------------|--------------------|-------------------------|---------------|------------------|------------------|--|--------------------|---------|
|                           |                    |                         |               |                  |                  |  | 1<br>BR            | 2<br>BR |
| Consolidated communities: |                    |                         |               |                  |                  |  |                    |         |
| Marina Shores             | Virginia Beach, VA | 392                     | 1991          | 1/05             | 16.3             | 379,030                                | 126                | 187     |
| Villages                  | Carrboro, NC       | 264                     | 1975          | 1/05             | 19.7             | 252,766                                | 139                | 125     |
| Villages Phase 5          | Carrboro, NC       | 57                      | 1987          | 1/05             | 5.3              | 54,177                                 | 25                 | 24      |

| Community                 | Location           | Weighted<br>Average<br>Apt. Size<br>(Sq. Ft.) | Average Economic<br>Occupancy Percent (1) |      |      | Average<br>Monthly Revenue<br>per Occupied Unit |      |      |
|---------------------------|--------------------|---|---|------|------|---|------|------|
|                           |                    |   | 2005                                      | 2004 | 2003 | 2005  | 2004 | 2003 |
| Consolidated communities: |                    |   |   |      |      |   |      |      |
| Marina Shores             | Virginia Beach, VA | 967   | 96.7                                      | -    | -    | 1,173   | -    | -    |

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|                  |              |     |      |   |   |     |   |   |
|------------------|--------------|-----|------|---|---|-----|---|---|
| Villages         | Carrboro, NC | 957 | 89.8 | - | - | 666 | - | - |
| Villages Phase 5 | Carrboro, NC | 950 | 94.5 | - | - | 779 | - | - |

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### RESTAURANT PROPERTIES LOCATIONS

Virginia  
(27 properties)

Ashland  
106 North Washington

Blackstone  
North Main Street

Bluefield  
701 South College Street

Chester  
12401 Jefferson Davis Hwy.

Clarksville  
916 Virginia Avenue

Clintwood  
U.S. Highway 83

Dublin  
208 College Avenue

Franklin  
105 North Mechanic Street

Galax  
425 Main Street

Hopewell  
East City Point Road

Lebanon  
Route 1

Lynchburg  
8411 Timberlake Road  
2231 Langhorne road

Norfolk  
3908 Princess Anne Road

Orange  
200 Madison Road

Petersburg  
1865 Crater Road, South

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Richmond

921 Myers Street  
6850 Forest Hill Avenue  
7917 Midlothian Pike

Roanoke

4407 Abenham Avenue SW  
3401 Hollins Road

Rocky Mount

322 Tanyard Road, NE

Smithfield

Smithfield Shopping Center

Verona

160 East Route 612

Virginia Beach

4261 Holland Road  
1951 Lynnhaven Parkway

Wise

US Highway 23, Business

North Carolina

(13 properties)

Burlington

2712 Alamance Road

Denver

Route 16

Eden

202 West Kings Highway

Fayetteville

3505 Ramsey Street  
360 North Eastern Blvd.

Hillsborough

380 S. Churton Street

Kinston

200 West Vernon Street  
1404 Richlands Street

Newton

South Ashe & North "D"

Siler City\*

Chatham Shopping Center

Spring Lake

400 South Main Street

Thomasville

1116 East Main Street  
Randolph Street

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\*operated as a "B-B-Q & Ribs." All other sites are operated as "Hardee's."

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### ITEM 3. LEGAL PROCEEDINGS

We are a party to a variety of legal proceedings arising in the ordinary course of business. We do not expect any of these matters, individually or in aggregate, to have a material adverse impact on the company.

In the event a claim was successful, we believe that we are adequately covered by insurance and indemnification agreements. We have insurance coverage on each of our apartment communities. Our restaurant properties are subject to an indemnification agreement whereby Enterprises, the lessee, is responsible for all claims arising from a restaurant property. In addition, Enterprises is required to provide insurance, which identifies the company as a named insured, on each restaurant property. Each apartment property that we manage but do not own is covered by an insurance policy under which we are a named insured.

### ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of security holders during the fourth quarter of fiscal year 2005.

## PART II

### ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

#### Market Information, Holders and Dividends

Our common stock is traded on the American Stock Exchange under the symbol "BNP." There were 1,230 common shareholders of record on February 28, 2006. The table below shows, for the periods indicated, the range of high, low, and closing sale prices of our common stock as reported by the American Stock Exchange and the dividends paid per share. As of February 28, 2006, the closing price of the company's common stock was \$17.15 per share.

|                | High     | Stock Price<br>Low | Close    |    |
|----------------|----------|--------------------|----------|----|
|                |          |                    |          |    |
| 2005:          |          |                    |          |    |
| Fourth quarter | \$ 16.05 | \$ 13.53           | \$ 16.00 | Di |
| Third quarter  | 16.04    | 13.75              | 14.35    | Pe |
| Second quarter | 16.10    | 15.45              | 16.00    |    |
| First quarter  | 16.29    | 15.65              | 16.00    |    |
| 2004:          |          |                    |          |    |
| Fourth quarter | \$ 16.20 | \$ 13.62           | \$ 16.10 |    |
| Third quarter  | 13.90    | 12.80              | 13.68    |    |
| Second quarter | 13.24    | 12.35              | 13.14    |    |
| First quarter  | 13.35    | 11.50              | 13.17    |    |

We have paid regular quarterly dividends to holders of our common stock

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since our inception, and we intend to continue to do so. In January 2006, the Board of Directors declared a regular quarterly dividend of \$0.26 per common share, payable February 15, 2006, to shareholders of record on February 1, 2006.

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We anticipate that we will pay all dividends from current funds from operations. We expect distributions to substantially exceed the 90% annual distribution requirement for a REIT.

We have a dividend reinvestment plan that is available to all shareholders of record. Under this plan, as amended in February 2004, the plan administrator, Wachovia Bank, N. A., reinvests dividends on behalf of plan participants in our common stock. We will either issue new shares or direct Wachovia to purchase shares on the open market. In addition, shareholders who participate in the plan may elect to make direct cash investments or supplement their reinvestment program with additional cash investments of any amount from \$25 to \$25,000 per quarter. Participants do not pay any commissions on stock purchased under the plan.

We have included information regarding securities authorized for issuance under equity compensation plans in Part III, Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters of this Annual Report.

### Sales of Unregistered Securities

On January 26, 2005, we acquired Boddie Investment Company ("BIC") through a merger. Because of this merger, we succeeded BIC as the general partner of, and acquired an economic interest in, three limited partnerships. As consideration in the merger, we privately issued 508,578 shares of common stock pursuant to the exemption provided by Section 4(2) of the Securities Act. We issued those shares, which had a value on that date of \$16.10 per share, to B. Mayo Boddie and Nicholas B. Boddie. Upon closing the merger, we canceled 72,399 shares of our common stock that BIC held immediately before the merger. The value of the transaction, before the impact of the cancelled shares, was \$8.2 million based on the \$16.10 per share value.

In 2001, 2002 and 2003, we issued a total of 909,090 shares of our Series B Cumulative Convertible Preferred Stock ("preferred stock") to a single investor for total proceeds of \$10.0 million in cash. These shares were issued pursuant to the exemption from the registration requirements of the Securities Act of 1933 set forth in Section 4(2) of the Act. The purchaser was Preferred Investment I, LLC, an accredited investor, and offers were not accompanied by any form of general solicitation. The managing member of the purchaser became one of our directors in 2001.

In October 2005, we notified the holder of our preferred stock that the company was exercising its option to redeem all 909,090 shares of the preferred stock. In accordance with the certificate of designation governing the preferred stock, the holder elected to convert all of the shares of preferred stock to shares of the company's common stock. Accordingly, on November 14, 2005, the company issued 909,090 shares of its common stock and cancelled 909,090 shares of preferred stock. The transaction was accomplished pursuant to the exemption from registration under Sections 3(a)(9) and 4(2) of the Securities Act of 1933.

### ITEM 6. SELECTED FINANCIAL DATA

We present below selected financial information. We encourage you to read the financial statements and the notes accompanying the financial statements in this Annual Report. This information is not intended to be a

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replacement for the financial statements.

This financial information includes all apartment communities and restaurant properties that we owned or included in our consolidation for each period shown.

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|  | Year ended December 31 |           |           |           |
|--|------------------------|-----------|-----------|-----------|
|  | 2005                   | 2004      | 2003      | 2002      |
| -----  |                        |           |           |           |
| (in thousands, except per share and property data)                 |                        |           |           |           |
| Operating data: (1)  |                        |           |           |           |
| Revenue:   |                        |           |           |           |
| Apartment rental income  | \$ 67,029              | \$ 44,929 | \$ 37,475 | \$ 32,890 |
| Restaurant rental income   | 3,830                  | 3,830     | 3,908     | 4,021     |
| Other income   | 1,154                  | 1,227     | 1,277     | 1,253     |
| -----  |                        |           |           |           |
| Total revenue  | 72,012                 | 49,986    | 42,660    | 38,164    |
| Expenses:  |                        |           |           |           |
| Apartment operations   | 26,243                 | 18,119    | 15,458    | 12,682    |
| Administrative costs   | 6,255                  | 4,520     | 3,907     | 3,358     |
| Interest and penalties paid at<br>debt refinance                   | 24,701                 | 14,445    | 13,000    | 11,452    |
| Depreciation   | 16,602                 | 11,491    | 10,040    | 8,794     |
| Amortization and write-off<br>of loan costs                        | 726                    | 450       | 322       | 351       |
| Deficit distributions to<br>minority partners,<br>consolidated LPs | 7,861                  | -         | -         | -         |
| -----  |                        |           |           |           |
| Total expenses   | 82,389                 | 49,025    | 42,727    | 36,637    |
| -----  |                        |           |           |           |
|  | (10,377)               | 961       | (66)      | 1,527     |
| Loss (income) attributed to<br>minority interests -                |                        |           |           |           |
| - Consolidated limited<br>partnerships                             | 350                    | -         | -         | -         |
| - Operating partnership  | 1,975                  | 1         | 174       | (279)     |
| -----  |                        |           |           |           |
| (Loss) income from<br>continuing operations                        | (8,052)                | 962       | 107       | 1,248     |
| Income from<br>discontinued operations, net                        | 6,563                  | 77        | -         | -         |
| -----  |                        |           |           |           |
| Net (loss) income  | (1,488)                | 1,039     | 107       | 1,248     |
| Cumulative preferred dividend                                      | (833)                  | (1,000)   | (661)     | (323)     |
| -----  |                        |           |           |           |
| Income (loss) attributed to common<br>shareholders                 | \$ (2,322)             | \$ 39     | \$ (553)  | \$ 925    |
| =====  |                        |           |           |           |
| Earnings per share, basic and<br>diluted -                         |                        |           |           |           |
| (loss) income attributed to<br>common shareholders                 | \$ (0.25)              | \$ 0.01   | \$ (0.09) | \$ 0.16   |
| =====  |                        |           |           |           |
| Dividends per common share   | \$ 1.00                | \$ 1.00   | \$ 1.00   | \$ 1.24   |
| =====  |                        |           |           |           |

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Balance Sheet data:

|  |            |            |            |            |
|--|------------|------------|------------|------------|
| Real estate assets (before accumulated depreciation) |            |            |            |            |
| - Apartment communities                              | \$ 559,560 | \$ 389,119 | \$ 299,661 | \$ 275,713 |
| - Restaurant properties                              | 37,405     | 37,405     | 37,405     | 39,159     |
| Real estate assets, net                              | 509,297    | 360,071    | 281,014    | 265,423    |
| Total assets   | 524,063    | 367,764    | 287,200    | 271,723    |
| Total debt   | 436,712    | 286,425    | 229,714    | 211,585    |
| Minority interests                                   | 21,207     | 14,394     | 15,895     | 17,947     |
| Shareholders' equity                                 | 60,429     | 62,996     | 38,733     | 39,271     |

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|  | Year ended December 31                             |           |           |           |
|--|--|-----------|-----------|-----------|
|  | 2005   | 2004      | 2003      | 2002      |
|  | -----  |           |           |           |
|  | (in thousands, except per share and property data) |           |           |           |
| <b>Apartment Properties data:</b>                                  |  |           |           |           |
| Apartment communities owned at year end                            | 30   | 24        | 19        | 18        |
| Apartment units owned at year end                                  | 7,945  | 6,113     | 4,859     | 4,427     |
| Average apartment economic occupancy                               | 94.7%  | 94.4%     | 92.8%     | 92.8%     |
| Average monthly revenue per occupied unit                          | \$ 742   | \$ 737    | \$ 725    | \$ 733    |
| <b>Other data:</b>   |  |           |           |           |
| Earnings before interest, taxes, depreciation and amortization (2) | \$ 39,514  | \$ 27,347 | \$ 23,295 | \$ 22,124 |
| Funds from operations (2)  | 13,133   | 11,447    | 9,313     | 9,998     |
| Funds available for distribution (2)                               | 19,014   | 9,988     | 7,904     | 8,865     |
| Net cash provided by (used in):                                    |  |           |           |           |
| Operating activities (3)   | \$ 12,793  | \$ 12,677 | \$ 9,594  | \$ 10,118 |
| Investing activities (3)   | (61,444)   | (52,848)  | (25,275)  | (32,669)  |
| Financing activities   | 51,245   | 40,123    | 15,361    | 22,018    |
| <b>Weighted average number of shares and units outstanding:</b>    |  |           |           |           |
| Preferred B shares   | 790  | 909       | 601       | 293       |
| Common shares  | 9,389  | 7,617     | 5,868     | 5,787     |
| Operating partnership minority units                               | 2,301  | 1,856     | 1,843     | 1,786     |

(1) We sold an apartment community in October 2005 that we originally acquired in July 2004. 2004 amounts have been reclassified to present the operations of this community as "discontinued operations."

(2) Earnings before interest, taxes, depreciation and amortization, funds from operations, and funds available for distribution amounts reflect measurements for the operating partnership (before deduction for minority interest).

Earnings before interest, taxes, depreciation and amortization is



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frequently referred to as "EBITDA." This measurement is derived directly from amounts included in the Statement of Operations. We consider EBITDA to be a useful measurement of operations performance before the impact of financial structure and significant non-cash charges.

We calculated EBITDA as follows:

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|   | Year ended December 31 |           |           |           |
|---|------------------------|-----------|-----------|-----------|
|   | 2005                   | 2004      | 2003      | 2002      |
|   | -----                  |           |           |           |
|   | (in thousands)         |           |           |           |
| Net (loss) income   | \$ (1,488)             | \$ 1,039  | \$ 107    | \$ 1,248  |
| Interest and<br>refinance penalties   | 24,701                 | 14,445    | 13,000    | 11,452    |
| Depreciation  | 16,602                 | 11,491    | 10,040    | 8,794     |
| Deficit distributions to<br>minority partners (a)   | 7,861                  | -         | -         | -         |
| Amortization and write-off of<br>unamortized loan costs   | 726                    | 450       | 322       | 351       |
| Minority interests  | (668)                  | 16        | (174)     | 279       |
| Discontinued operations and<br>gain on sale of real estate<br>assets                                | (8,220)                | (95)      | -         | -         |
|   | -----                  |           |           |           |
| Earnings before interest,<br>taxes, depreciation (and<br>deficit distributions) and<br>amortization | \$ 39,514              | \$ 27,347 | \$ 23,295 | \$ 22,124 |
|   | =====                  |           |           |           |

(a) Deficit distributions to minority partners are charges recognized in our statement of operations when a consolidated limited partnership distributes cash to a minority partner in excess of the positive balance in such partner's capital account. Deficit distributions to minority partners may occur when the fair value of the underlying real estate exceeds its depreciated net book value because the underlying real estate has appreciated or maintained its value. As a result, deficit distributions to minority partners represent, in substance, either our recognition of depreciation previously allocated to that partner or a cost related to the minority partner's share of real estate appreciation.

Funds from operations is frequently referred to as "FFO." FFO is defined by the National Association of Real Estate Investment Trusts ("NAREIT") as "net income (computed in accordance with generally accepted accounting principles), excluding gains (losses) from sales of property, plus depreciation and amortization, and after adjustments for unconsolidated partnerships and joint ventures." Our calculation of FFO is consistent with FFO as defined by NAREIT. Because we hold all of our assets in and conduct all of our operations through the operating partnership, we measure FFO at the operating partnership level (i.e., after deducting the minority interests in FFO of the consolidated limited partnerships, but before deducting the minority interest in the operating partnership).

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Historical cost accounting for real estate assets implicitly assumes that the value of real estate assets diminishes predictably over time. In fact, real estate values have historically risen or fallen with market conditions. FFO is intended to be a standard supplemental measure of operating performance that excludes historical cost depreciation from - or "adds it back" to - GAAP net income. We consider FFO to be useful in evaluating potential property acquisitions and measuring operating performance.

Funds available for distribution is frequently referred to as "FAD." We calculate FAD as FFO plus non-cash expenses, plus (less) gains (losses) from sale of property, less recurring capital expenditures. We believe that, together with net income and cash flows from operating activities, FAD provides investors with an additional measure to evaluate the ability of the operating partnership to incur and service debt, to fund acquisitions and other capital expenditures, and to

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fund distributions to shareholders and minority unitholders.

Funds from operations and funds available for distribution do not represent net income or cash flows from operations as defined by generally accepted accounting principles. You should not consider FFO or FAD to be alternatives to net income as reliable measures of the company's operating performance; nor should you consider FFO or FAD to be alternatives to cash flows from operating, investing or financing activities (as defined by generally accepted accounting principals) as measures of liquidity.

Funds from operations and funds available for distribution do not measure whether cash flow is sufficient to fund all of our cash needs, including principal amortization, capital improvements and distributions to shareholders. FFO and FAD do not represent cash flows from operating, investing or financing activities as defined by generally accepted accounting principles. Further, FFO and FAD as disclosed by other REITs might not be comparable to our calculation of FFO or FAD.

We provide a reconciliation of net income to FFO, along with a reconciliation of net cash provided by operating activities to FAD, under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operations - Funds From Operations" in this Annual Report.

- (3) Beginning in 2004, we have presented operating activities in our consolidated statements of cash flows using the direct method, which provides cash flow amounts corresponding directly to lines in our statements of operations. We have adjusted the 2003 and 2002 comparative amounts in our consolidated statements of cash flows to conform to the 2004 presentation by reclassifying the net cash flows related to funding of lender reserves for apartment property replacements from operating activities to investing activities. This reclassification has no impact on the net change in cash and cash equivalents for 2003 and 2002, only in the subtotals for net cash provided by operating activities and net cash used in investing activities. The net effect on net cash provided by operating activities is a decrease of \$213,000 in 2003, and an increase of \$133,000 in 2002, from amounts previously reported.

### ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Some of the information in this discussion and analysis of financial

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condition and results of operations may contain forward-looking statements. Please review our Caution Regarding Forward-Looking Statements at the beginning of this Annual Report. In addition, you should read this discussion in conjunction with the financial statements and notes thereto included in this Annual Report.

### Overview

2005 was by far the most active year in our history.

During the year we continued to expand and improve our portfolio with the acquisition of eight apartment properties and the general partner interest in partnerships owning three apartment communities. As a result of these acquisitions the number of apartments we own increased by 30% and the number of units under our control increased by 42%. These new properties are consistent with our strategy of focusing on middle-market properties, in good to excellent locations, with good "bone structure". What is most interesting about the 2005 acquisitions is how they were acquired. Four of the properties were acquired in cash transactions; four were acquired using UpREIT units, and the three general partner interests were acquired through a corporate merger. We have emphasized in the past that we would be flexible in how we approached acquisitions, and the 2005 acquisitions illustrate that flexibility. Going forward we will continue to seek acquisitions similar to these. You should be aware, however, that in recent months pricing for apartment communities has become very competitive. While

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we intend to continue to expand the portfolio, we will be very judicious and will only purchase where we believe it to be in our best long-term interest.

An essential part of our strategy of providing high quality middle market housing is maintaining our properties to very high standards. Integral to this is our rehabilitation program. We believe that we can create value by updating older properties that are otherwise structurally sound and have solid market locations. During the year we completed rehabilitation projects at two of our apartment properties. We will continue to seek properties that present this type of opportunity.

In 2005 we began a major effort to improve the efficiency of our corporate operations and to better position ourselves for future growth. To this end, we added a Vice President of Operations in 2005 and began a ground-up review of our operating systems. By year end we had implemented a number of significant changes and anticipate more to come. While there have been significant costs associated with this project, we believe that the long-term benefits warrant the expenditures.

One of our primary concerns entering 2005 was our exposure to rising interest rates. In this report last year we said that we intended to monitor the situation and that we might take steps to reduce our exposure if we felt it was warranted. Shortly before year end we decided to replace \$47.8 million of fixed rate loans carrying interest rates of 6.97% with \$73.8 million of fixed rate loans carrying interest rates of approximately 5.53%. We used approximately \$22.3 million of the net proceeds of the refinance to pay down our variable-rate line of credit. At year end the interest rate on that line of credit was approximately 6.12%. As part of the refinancing of these loans we incurred approximately \$1.6 million in one-time prepayment fees that are a charge against net income, funds from operations and funds available for distribution. While the year-end refinance transactions had an immediate negative impact on our reported results for 2005, we believe the long-term impact of these transactions will be quite beneficial. As a result of these transactions, we have

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substantially reduced our exposure to increases in interest rates and the low fixed rates obtained on the replacement loans will result in substantial interest savings over the next few years.

A highlight of 2005 was the sale of Savannah Shores Apartments. This was the first time in our history that we have sold an apartment community. When we buy a property we generally expect to own and operate the property for ten years or more. Savannah Shores was no exception, but dynamic market conditions led to our receiving unsolicited offers for the property at prices we felt warranted an immediate sale. You should not view the sale of Savannah Shores as a change in our business strategy. We still believe that holding properties for long periods of time is generally in our best interest. However, we are open to shorter holding periods when the situation warrants.

From an operational point of view, 2005 was a good year for us. We saw continued improvement in apartment operating results with "same-units" NOI growth of 4.7% in 2005. This was primarily the result of a 2.4% increase in "same-units" apartment revenue. We entered 2005 with high occupancy and anticipated that any increase in rental revenue would, by necessity, come from increasing rental rates. While maximizing apartment revenue is always a balancing act between occupancy and rental rate, we were relatively pleased with our ability to increase rental rates in 2005 without having to sacrifice occupancy.

Overall, we were pleased with our operating results for 2005. Total funds from operations showed good improvement, 14.7%, despite the fact that we incurred approximately \$1.6 million in one-time prepayment charges related to our year-end refinancing transactions. Funds from operations per share for the year declined to \$1.13, but again this was net of the one-time refinancing charges that equated to approximately \$0.14 per share.

We are quite optimistic about 2006. We have a solid portfolio of extremely well maintained apartment properties in excellent locations. We are confident that given our properties, our markets, our strategy, and the current economic environment, we will be able to achieve reasonable growth in

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apartment rental income in 2006. We believe that the key to success in 2006 will be basic apartment operations - marketing, leasing, and maintenance - something with which we are particularly comfortable and adept.

### Capital Resources and Liquidity

#### Capital Resources

We completed a number of significant investing and financing transactions in 2005. In addition, and for the first time in our history, we entered into and completed a contract for sale of an apartment community.

Our balance sheet at December 31, 2005, compared to December 31, 2004, reflects significant growth and complexity in our financial reporting. We provide the following supplemental consolidating summary information, in response to requests from members of the investment community, for use in understanding the changes in our structure:

2005

-----  
Consolidated                      Owned

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|  | Consolidated | Elim       | LPs (1)   | Properties | Pr    |
|--|--------------|------------|-----------|------------|-------|
|  | (000's)      | (000's)    | (000's)   | (000's)    |       |
| Balance Sheet at December 31, 2005, compared to December 31, 2004: |              |            |           |            |       |
| Real estate investments, net                                       |              |            |           |            |       |
| of depreciation  | \$ 509,297   | \$ -       | \$ 42,044 | \$ 467,253 | \$    |
| Cash and cash equivalents  | 3,111        | -          | 805       | 2,306      |       |
| Prepaid expenses and   |              |            |           |            |       |
| other assets   | 8,034        | (3,586)    | 696       | 10,924     |       |
| Deferred financing costs, net                                      | 2,380        | (154)      | 604       | 1,930      |       |
| Intangible assets, net   | 1,240        | -          | -         | 1,240      |       |
|  | -----        | -----      | -----     | -----      | ----- |
|  | \$ 524,063   | \$ (3,740) | \$ 44,149 | \$ 483,653 | \$    |
|  | =====        | =====      | =====     | =====      | ===== |
| Notes payable  | \$ 436,712   | \$ (2,282) | \$ 50,419 | \$ 388,576 | \$    |
| Accounts payable and   |              |            |           |            |       |
| accrued expenses   | 1,419        | (52)       | 139       | 1,332      |       |
| Accrued interest   | 1,345        | -          | 204       | 1,141      |       |
| Consideration due for acquisitions                                 | 1,000        | -          | -         | 1,000      |       |
| Deferred revenue and   |              |            |           |            |       |
| security deposits  | 1,950        | (154)      | 122       | 1,982      |       |
|  | -----        | -----      | -----     | -----      | ----- |
|  | 442,426      | (2,489)    | 50,884    | 394,031    |       |
| Minority interests -   |              |            |           |            |       |
| - Consolidated limited partnerships                                | -            | -          | -         | -          |       |
| - Operating partnership  | 21,207       | -          | -         | 21,207     |       |
| Shareholders' equity   | 60,429       | (1,251)    | (6,735)   | 68,414     |       |
|  | -----        | -----      | -----     | -----      | ----- |
|  | \$ 524,063   | \$ (3,740) | \$ 44,149 | \$ 483,653 | \$    |
|  | =====        | =====      | =====     | =====      | ===== |

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Acquisition of Boddie Investment Company; consolidated limited partnerships

In January 2005, we acquired Boddie Investment Company ("BIC") through a merger. We issued 509,000 shares of our common stock valued at \$8.2 million, and cancelled 72,000 shares of common stock that BIC held immediately before the merger. As a result of this acquisition, we assumed the role of general partner and acquired economic interests in three limited partnerships. Prior to this acquisition, we managed the apartment communities owned by these partnerships on a contract basis; we will continue to manage these properties.

A summary of assets acquired in the BIC acquisition, along with our allocation of costs assigned to those assets, follows (all amounts in thousands):

|   |          |
|---|----------|
| Investments in limited partnerships:  |          |
| Marina Shores Associates One, Limited Partnership (50% interest)                                      | \$ 5,940 |
| The Villages of Chapel Hill Limited Partnership (1% interest)   | 2        |
| The Villages of Chapel Hill - Phase 5 Limited Partnership (1% interest)                               | 7        |
| BNP common stock held by BIC (which we immediately retired) 1,166                                     |          |
| Receivables from the Villages Partnership for general partners' advances and accrued interest thereon | 1,220    |

-----  
 \$ 8,335  
 =====

Although the amounts related to this acquisition seem relatively insignificant at first glance, the accounting for the investments in limited partnerships is complex, and the impact on presentation of our consolidated financial statements is rather significant. We have included a detailed discussion of our accounting treatment for each of the investments in limited partnerships in Notes 1 and 2 of our financial statements included in this Annual Report on Form 10-K

We acquired a 50% general partner interest in Marina Shores Associates One, Limited Partnership ("Marina Shores Partnership"). Under the terms of the partnership agreement, the general partner controls the activities of the partnership. We therefore included the accounts of this partnership in our consolidated financial statements effective January 26, 2005, by applying traditional purchase accounting methods. We recorded our prorata interest in the partnership's assets and liabilities at the lower of our cost or fair value. We reflected the noncontrolling, or "minority," partner's 50% interest in the partnership's assets and liabilities at historical cost, except to adjust the minority partner's capital account (which was previously in a deficit balance) to \$-0-. Very shortly before our acquisition of the 50% general partner interest, the Marina Shores real estate assets appraised for approximately \$45 million, compared to net carrying value of approximately \$11 million. The initial inclusion of the Marina Shores Partnership in our consolidation resulted in (amounts in thousands):

|   |           |
|---|-----------|
| Increase in real estate investments - 392 apartment units | \$ 26,254 |
| Increase in net operating assets                          | 950       |
| Increase in long term debt - first deed of trust          | (21,264)  |
| Minority interest in consolidated limited partnerships    | -         |
|   | -----     |
| Increase in net assets                                    | \$ 5,940  |
|   | =====     |

Very shortly after our acquisition of BIC, the Marina Shores Partnership refinanced its long-term debt and issued a \$33.9 million fixed-rate first deed of trust note payable. This 10-year loan provides for interest at an effective rate of 5.1%. We have included a more detailed description of this note payable in Note 5 of our financial statements included in this Annual Report.

The Marina Shores Partnership first applied proceeds of this loan to retire the existing debt, then distributed \$6.8 million to its limited partner and \$3.7 million to our operating partnership. In 2005, the Marina Shores Partnership made distributions totaling \$7.9 million to its limited partner and \$4.7 million

to our operating partnership. The Marina Shores Partnership generates positive cash flows, and we currently expect that the Marina Shores Partnership will continue to make regular distributions of approximately \$360,000 per year each to the limited partner and our operating partnership.

Prior to consolidation in our financial statements, the fair value of the real estate held by the Marina Shores Partnership significantly exceeded its depreciated net book value because the underlying real estate had appreciated

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significantly since the Marina Shores Partnership's original formation in the late 1980s. In our initial consolidation of this partnership, we reset the minority limited partner's capital account to \$-0-.

Distributions to the limited partner subsequent to inclusion of the Marina Shores Partnership in our consolidated financial statements are, and will generally be, reflected as charges against income in our consolidated financial statements as "deficit distributions to minority partners." In accordance with GAAP, deficit distributions to minority partners are charges recognized in our income statement when a consolidated limited partnership makes distributions to a minority partner in excess of the positive balance in such partner's capital account. Deficit distributions represent, in substance, either our recognition of the depreciation previously allocated to the minority partner or a cost related to the minority partner's share of real estate appreciation. The cash outlay is, in fact, made by the consolidated limited partnership, and there is no economic effect to the operating partnership.

We acquired a 1% general partner interest in The Villages of Chapel Hill Limited Partnership ("Villages Partnership"). We determined that the Villages Partnership is a variable interest entity, or "VIE," as defined by GAAP, because the limited partnership does not have sufficient equity to carry out its principal activities without additional subordinated financial support from the general partner. We also concluded that we are the "primary beneficiary" of the Villages Partnership. Because the Villages Partnership is a VIE and we are the primary beneficiary, we included the accounts of this partnership in our consolidated financial statements effective January 26, 2005, by recording all of the partnership's assets, liabilities and noncontrolling interests at fair value. In our initial consolidation of the Villages Partnership, we recorded the minority partners' capital accounts at \$350,000. The initial inclusion of the Villages Partnership in our consolidation resulted in (amounts in thousands):

|   |           |
|---|-----------|
| Increase in real estate investments - 264 apartment units | \$ 14,188 |
| Increase in net operating assets                          | 145       |
| Increase in long-term debt - first deed of trust          | (12,094)  |
| Subordinated long-term debt to BNP*                       | (1,888)   |
| Minority interest in consolidated limited partnerships    | (350)     |
|   | -----     |
| Increase in net assets                                    | \$ 2      |
|   | =====     |

\* The subordinated long-term debt to BNP is eliminated in consolidation against related receivable balances.

We acquired a 1% general partner interest in The Villages of Chapel Hill - Phase 5 Limited Partnership ("Villages - Phase 5 Partnership"). Under the terms of the partnership agreement, the general partner controls the activities of the partnership; we therefore included the accounts of this partnership in our consolidated financial statements effective January 26, 2005, by applying traditional purchase accounting methods. The initial inclusion of the Villages - Phase 5 Partnership in our consolidation resulted in (amounts in thousands):

|  |          |
|--|----------|
| Increase in real estate investments - 57 apartment units | \$ 2,596 |
| Increase in net operating assets                         | 239      |
| Increase in long term debt - first deed of trust         | (2,828)  |
| Minority interest in consolidated limited partnerships   | -        |
|  | -----    |
| Increase in net assets                                   | \$ 7     |
|  | =====    |

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We allocate proportional income and losses of the consolidated limited partnerships to minority partners; however, we may allocate losses to a minority partner only to the extent of the carrying amount of the interest of that minority partner. When losses attributable to the minority limited partners of a consolidated limited partnership exceed their positive capital balances, we record a charge to our earnings, even though there is no cash outlay by the operating partnership. During 2005, after losses of the Villages Partnership reduced the minority limited partners' capital accounts to \$-0-, we recorded charges for losses (resulting primarily from depreciation) of the consolidated limited partnerships totaling \$126,000.

### Acquisition of Shugart properties

In March 2005, we completed the acquisition of a portfolio of four apartment properties from entities that we call the "Shugart Parties." The aggregate purchase price for the properties totaled \$52.1 million, including approximately \$0.3 million in net operating assets, paid through assumption or refinancing of \$42.8 million of debt on the properties and \$9.3 million paid in operating partnership units with an imputed value of \$13.50 per unit. Under the terms of the exchange agreements, we issued 689,000 operating partnership units at closing, and will issue an additional 74,000 deferred units in March 2006. The allocation of the purchase price includes the following significant components:

| Property                     | Apt.<br>Units | Contract Price | Debt Assumed | Val<br>Oper<br>Partners |
|------------------------------|---------------|----------------|--------------|-------------------------|
|                              |               | (000's)        | (000's)      | (0                      |
| Canterbury Apartments        | 630           | \$ 25,750      | \$ 22,992    | \$                      |
| Laurel Springs Apartments    | 240           | 14,610         | 11,320       |                         |
| Laurel Springs II Apartments | 96            | 7,090          | 5,850        |                         |
| Salem Ridge Apartments       | 120           | 4,360          | 2,610        |                         |

The assets and liabilities of these apartment properties are included in our consolidated financial statements as of March 31, 2005. We operate Laurel Springs and Laurel Springs II Apartments as one community.

Immediately upon completion of this acquisition, we retired a \$1.5 million variable rate note related to Canterbury Apartments. The remaining assumed debt includes three fixed-rate notes totaling \$35.4 million at effective interest rates ranging from 5.0% to 6.8% and a \$5.9 million variable-rate note with interest at 30-day LIBOR plus 1.9%. We have included a more detailed description of these notes payable in Note 5 of our financial statements included in this Annual Report.

### Other acquisitions

During 2005, we completed four additional apartment property acquisitions with combined contract prices totaling \$73.5 million:

| Property                 | Apt.<br>Units | Contract Price | Date Acquired |
|--------------------------|---------------|----------------|---------------|
|                          |               | (000's)        |               |
| Waverly Place Apartments | 240           | \$13,100       | April 2005    |



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|                        |     |        |              |
|------------------------|-----|--------|--------------|
| Paces Watch Apartments | 232 | 20,450 | May 2005     |
| Hamptons Apartments    | 232 | 17,500 | October 2005 |
| Timbers Apartments     | 240 | 22,450 | October 2005 |

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We made these acquisitions in separate transactions from unaffiliated third parties. For tax purposes, the acquisitions of Hamptons and Timbers were structured as a tax-deferred exchange under Section 1031 of the Internal Revenue Code in conjunction with the sale of Savannah Shores Apartments discussed below.

In conjunction with these acquisitions, we issued three fixed-rate notes payable totaling \$42.4 million and a variable-rate note payable with interest at 30-day LIBOR plus 1.65%. A more detailed description of these notes payable is included in Note 5 of our financial statements included in this Annual Report.

### Sale of Savannah Shores Apartments

During the third quarter of 2005, we received and accepted an unsolicited offer for Savannah Shores Apartments. Our business strategy is to purchase apartment properties with the expectation of holding and operating them for the long term. This was our intention with Savannah Shores; however, in view of the extraordinary pricing offered, we believe that completing this sale was in the best interest of our shareholders.

We acquired Savannah Shores Apartments in July 2004 for an initial purchase price of \$12.5 million, paid through issuance of operating partnership units with total imputed value of \$0.1 million, assumption of \$12.2 million in debt obligations, and assumption of \$0.2 million net operating liabilities. The acquisition agreement provided for potential earn-out of additional purchase consideration of up to \$1.7 million, which we paid through issuance of additional operating partnership units in October 2005.

In October 2005, we sold Savannah Shores Apartments for a contract price of \$22.75 million to an unaffiliated party. Net proceeds of the sale were \$22.2 million, and we recorded a gain on the sale of real estate assets of \$8.1 million. We applied the sale proceeds to retire a \$9.0 million variable-rate note, then reinvested the remaining proceeds to acquire Hamptons and Timbers Apartments, discussed above.

### Debt refinancing transactions

During the second quarter of 2005, in refinance transactions, we issued two fixed-rate notes payable totaling \$22.6 million. The new notes provide for interest at a 5.28% effective rate, interest-only payments through mid-2008, with amortizing payments thereafter through maturity in mid-2015. We applied proceeds of these notes to retire an \$11.5 million variable-rate note payable, to retire a \$5.5 million 8.55% fixed-rate note payable, and to reduce the outstanding balance on our revolving line of credit.

In late December 2005, in conjunction with refinancing of existing debt, we issued five fixed-rate notes payable totaling \$73.8 million. The new notes provide for interest at 5.57% and 5.66% effective rates, interest-only payments through 2013 and 2012, respectively, with amortizing payments thereafter through maturity in January 2016. We applied proceeds of these notes to retire \$47.8 million in 6.97% fixed-rate, interest-only notes that were scheduled to mature in 2007, pay prepayment penalties of \$1.6 million, and to reduce the outstanding balance on our revolving line of credit to \$-0-.

Short-term interest rates increased steadily throughout 2005, with

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expectations that both short- and long-term rates will rise in 2006. To reduce our exposure to the risk of rising interest rates, we elected to refinance a number of loans during 2005. While this decision did cause us to incur a substantial one-time charge of approximately \$2.1 million associated with the prepayment of the refinanced loans, it also provides significant offsetting benefits.

- o As a result of the refinancing transactions, only 12.3% of our debt, on a consolidated basis, is floating (variable) rate;

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- o The refinancing transactions allowed us to substantially reduce the interest rate on the loans that were replaced and to lock the rates for ten years. To a large extent, the interest savings from this rate reduction over the next two years will offset the prepayment penalties incurred; and
- o The refinancing freed up working capital that was trapped in the properties secured by the refinanced loans. Over the years, the properties secured by refinanced loans had appreciated in value. By refinancing, we were able to capture some of this appreciation in the form of additional loan proceeds. We used these proceeds to pay down our operating line of credit. As a result, we entered 2006 with a \$-0- balance on our \$40 million line of credit.

A more detailed description of these transactions is included in Note 5 of our financial statements included in this Annual Report.

### Line of credit facilities

In conjunction with the various acquisition and financing transactions described above, during 2005 we made net draws on our revolving line of credit secured by Latitudes Apartments totaling \$18.8 million, and made net payments of \$29.0 million to reduce the outstanding balance to \$-0- at December 31, 2005. In November 2005, we modified this line of credit to increase our maximum loan amount to \$40.0 million and extend the term of the loan through January 2009. As of December 31, 2005, the full \$40.0 million was available for future draw.

In June 2005, we modified our line of credit secured by 40 restaurant properties to extend the maturity date to January 2008. We will be required to reduce the current \$14.7 million balance of this loan by \$833,000 in January 2007.

### Equity transactions

In November 2005, the company exercised its option to redeem all 909,000 shares of Series B Cumulative Convertible Preferred Stock ("preferred stock"), and the holder elected to convert all of the shares of preferred stock to shares of the company's common stock on a one-for-one basis.

In August 2005, the Board of Directors granted and issued 200,000 restricted shares of the company's common stock to four of our executive officers. We refer to these shares as "nonvested shares" in our consolidated financial statements. All of the shares were unvested on the date of grant, and will vest 10% per year beginning July 1, 2006, and on each July 1 thereafter until fully vested. Because grantees fully participate in dividends, the fair value of the nonvested shares is equal to the market value on the grant date \$15.70 per share, or a total of \$3.1 million.

In addition to the transactions described above, during 2005, we also:

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- o Issued 57,500 shares of our common stock upon exercise of options by two employees for proceeds of \$682,000;
- o Issued 52,000 shares of our common stock through our Dividend Reinvestment and Stock Purchase Plan for proceeds of \$810,000; and
- o Issued 78,000 shares of our common stock to redeem the same number of operating partnership units from minority unitholders.

Capital structure at the end of 2005

All of our properties are encumbered by or serve as collateral for debt. As of December 31, 2005, on a consolidated basis, long-term debt totaled \$436.7 million, including \$383.0 million of notes payable

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at effective fixed interest rates ranging from 5.0% to 7.4% (the weighted average rate for fixed-rate notes was 5.8%), and \$53.7 million at variable rates indexed primarily on 30-day LIBOR rates. Of the \$436.7 million in consolidated debt, \$388.6 million is related to properties wholly owned by the company, and \$48.1 million is related to properties in which the company owns a partial interest.

A summary of scheduled principal payments on long-term debt is included in Item 7A, Quantitative and Qualitative Disclosures about Market Risk, and in the notes to the financial statements included in this Annual Report. Significant scheduled balloon payments include maturities of:

- o \$7.9 million due in 2006 for two loans;
- o \$8.2 million due in 2007 for one loan;
- o \$63.2 million due in 2008, for eight loans;
- o \$41.5 million due in 2009, for three loans; and
- o \$18.3 million due in 2010, for one loan.

All of these loans are secured by real estate assets. The two loans maturing in 2006 are variable rate loans. At our option, we may extend one of these loans, with a balance of \$5.8 million, to 2008. We are reasonably certain that we can extend or refinance these loans at rates at or below those currently in place.

At December 31, 2005, we had 10.4 million common shares outstanding. In addition, there were 2.5 million operating partnership minority common units outstanding.

We intend to pursue our growth strategy through the utilization of our flexible capital structure. This may include the issuance of operating partnership units, common stock and/or preferred stock, additional debt, and joint venture investments. We may use our lines of credit or variable- and fixed-rate, long-term debt to acquire and refinance apartment communities.

Cash Flows and Liquidity

Net cash provided by operating activities totaled \$12.8 million in 2005, compared to \$12.7 million in 2004 and \$9.6 million in 2003. The 2005 amount for cash flows from operating activities is net of \$2.1 million in penalties paid in refinance activities. The increase in cash flows from

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operating activities reflects the positive impact of new apartment communities and improvements in apartments operating results.

Investing and financing activities focused primarily on apartment acquisitions and capital expenditures at apartment communities, along with payments of dividends and distributions. During the three-year period, we acquired a total of 15 apartment properties, disposed of one apartment property and added three additional apartment properties in consolidation.

We paid dividends to common shareholders of \$0.25 per share per quarter in each quarter of 2005, 2004, and 2003. Our payout ratio (the ratio of common dividends plus distributions paid, divided by operating partnership funds from operations) was 87.0% in 2005, 82.1% in 2004, and 82.5% in 2003. Our 2005 payout ratio based on funds from operations adjusted to add back the one-time \$2.1 million in penalties paid in refinance transactions would be 74.8%.

In January 2006, we announced an increase in our regular quarterly dividend from \$0.25 per share per quarter to \$0.26 per share. We intend to pay dividends quarterly, expect that these dividends will substantially exceed the 90% distribution requirements for REITs, and anticipate that all dividends will be paid from current funds from operations.

We generally expect to meet our short-term liquidity requirements through net cash provided by operations and utilization of credit facilities. We believe that net cash provided by operations is, and will continue to be, adequate to meet the REIT operating requirements in both the short- and the long term.

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We anticipate funding our future acquisition activities primarily by using short-term credit facilities as an interim measure, to be replaced by funds from equity offerings, long-term debt, or joint venture investments. We expect to meet our long-term liquidity requirements, such as scheduled debt maturities and repayment of short-term financing of possible property acquisitions, through long-term secured and unsecured borrowings and the issuance of debt securities or additional equity securities. We believe we have sufficient resources to meet our short-term liquidity requirements.

We received 5.3% of our revenue from continuing operations from rent received from Boddie-Noell Enterprises for use of our restaurant properties in 2005, compared to 7.7% in 2004 and 9.2% in 2003. Over time, we expect that restaurant rental income will continue to represent a decreasing percentage of our total revenue.

Boddie-Noell Enterprises is a privately owned company with total assets exceeding \$260 million and net equity exceeding \$90 million. Its principal line of business is the operation of over 300 Hardee's restaurants. In addition to its Hardee's operations, Boddie-Noell Enterprises is the owner of Texas Steakhouse and Saloon, a casual dining concept; Cafe Carolina, a cafe bakery/fast casual dining concept; and B-B-Q & Ribs, a fast-food barbeque concept. Boddie-Noell Enterprises also operates a number of Moe's Southwestern Grills, a fast-food Mexican concept. In addition to its restaurant operations, Boddie-Noell Enterprises conducts extensive real estate investment and development activities through BNE Land and Development. These activities involve a full range of property types, including land, commercial, retail, office, apartment and single-family properties. Based on discussions with management and review of their financial statements, we believe that Boddie-Noell Enterprises will have sufficient liquidity and capital resources to meet its obligations under the master lease as well as its general corporate operating needs.

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There is no assurance that Boddie-Noell Enterprises will renew the master lease that currently expires in December 2007. In the event Boddie-Noell Enterprises elects to terminate the lease, we would cease to receive rental payments from Boddie-Noell Enterprises and would be forced to seek alternative tenants for the properties, find alternate uses for the properties, or sell the properties. In the event Boddie-Noell Enterprises does not renew the lease, there is no assurance that we will be able to fully replace the \$3.8 million in revenue that we currently receive from Boddie-Noell Enterprises.

### Results of Operations

#### Discontinued operations

In October 2005, we sold Savannah Shores Apartments, an apartment community that we acquired in July 2004. In accordance with GAAP, we present the results of operations of this apartment community as discontinued operations in our statements of operations, for both 2005 and 2004. The change in presentation for the now discontinued operation does not have any impact on our financial condition or overall results of operations as previously presented.

Unless specifically noted, the following discussion relates to results of continuing operations for both 2005 and 2004. Amounts for 2004 in these comparisons will differ from the amounts we provided in our 2004 Annual Report. Presentation of results of operations for 2003 is not affected by the classification of Savannah Shores Apartments as discontinued operations.

#### 2005 compared to 2004

Results of operations for 2005, compared to 2004, reflect significant growth in our company and increased complexity in our financial reporting. We provide the following supplemental consolidating information, in response to requests from members of the investment community, for use in comparing our operating results for 2005 and 2004:

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|  | 2005         |         |                         |                     | Pr |
|--|--------------|---------|-------------------------|---------------------|----|
|  | Consolidated | Elim    | Consolidated<br>LPs (1) | Owned<br>Properties |    |
|  | (000's)      | (000's) | (000's)                 | (000's)             |    |
| Operating Results - 12 months ended December 31: |              |         |                         |                     |    |
| Revenues:  |              |         |                         |                     |    |
| Apartment rental income                          | \$ 67,029    | \$ -    | \$ 7,126                | \$ 59,903           | \$ |
| Restaurant rental income                         | 3,830        | -       | -                       | 3,830               |    |
| Management fee income                            | 131          | (357)   | -                       | 488                 |    |
| Casualty gains                                   | 668          | -       | -                       | 668                 |    |
| Interest and other income                        | 355          | (144)   | 31                      | 467                 |    |
|  | 72,012       | (501)   | 7,157                   | 65,356              |    |
| Expenses:  |              |         |                         |                     |    |
| Apartment operations                             | 26,243       | (357)   | 3,018                   | 23,582              |    |
| Administration expenses                          | 6,255        | -       | -                       | 6,255               |    |
| Interest   | 22,555       | (128)   | 2,473                   | 20,211              |    |
| Penalties paid at debt refinance                 | 2,146        | -       | 519                     | 1,628               |    |

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|  |            |       |            |          |
|--|------------|-------|------------|----------|
| Depreciation   | 16,602     | -     | 1,392      | 15,211   |
| Amortization, loan costs   | 432        | (16)  | 70         | 377      |
| Write-off of unamortized loan costs<br>at debt refinance                                 | 294        | -     | 160        | 134      |
| Deficit distributions to minority<br>partners of consolidated limited<br>partnerships(2) | 7,861      | -     | 7,861      | -        |
|  | 82,389     | (501) | 15,492     | 67,398   |
| (Loss) income from<br>continuing operations  | (10,377)   | -     | (8,335)    | (2,042)  |
| Income from<br>discontinued operations   | 88         | -     | -          | 88       |
| Gain on sale of real estate assets   | 8,132      | -     | -          | 8,132    |
| (Loss) income before<br>minority interests   | (2,156)    | \$ -  | \$ (8,335) | \$ 6,179 |
| Minority interests -<br>- Consolidated limited partnerships                              | 350        |       |            |          |
| - Operating partnership  | 318        |       |            |          |
| Net (loss) income  | \$ (1,488) |       |            | \$       |
| (Loss) income before<br>minority interest  | \$ (2,156) | \$ -  | \$ (8,335) | \$ 6,179 |
| Casualty gains   | (668)      | -     | -          | (668)    |
| Gain on sale of real estate assets   | (8,132)    | -     | -          | (8,132)  |
| Cumulative preferred dividend  | (833)      | -     | -          | (833)    |
| Amortization, lease intangible   | 193        | -     | -          | 193      |
| Depreciation -<br>- Continuing operations  | 16,602     | -     | 1,392      | 15,211   |
| - Discontinued operations  | 259        | -     | -          | 259      |

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|  | 2005         |         |                         |                    |    |
|--|--------------|---------|-------------------------|--------------------|----|
|  | Consolidated | Elim    | Consolidated<br>LPs (1) | Owed<br>Properties | Pr |
|  | (000's)      | (000's) | (000's)                 | (000's)            |    |
| Deficit distributions  | 7,861        | -       | 7,861                   | -                  |    |
| Minority interest in FFO of<br>consolidated limited partnerships | 13,125       | -       | 917                     | 12,208             |    |
|  | 8            | -       | 8                       | -                  |    |
| Funds from operations(3)   | \$ 13,133    | \$ -    | \$ 925                  | \$ 12,208          | \$ |

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### Revenues

Revenues in 2005 totaled \$72.0 million, an increase of 44.1% compared to 2004. This increase is primarily attributable to increases in apartment revenues, our primary business activity. Apartment related income (apartment rental income plus income from management and investment activities) accounted for 94.7% of our total revenue in 2005, compared to 92.3% in 2004.

Apartment rental income in 2005 totaled \$67.0 million, an increase of 49.2%, or \$22.1 million, compared to 2004. This increase is attributable to:

- o Apartment acquisitions in 2004 and 2005 - these 11 owned communities contributed \$18.4 million in 2005, compared to \$4.3 million in 2004. The first of these communities was acquired in May 2004;
- o Apartment communities that we consolidate effective January 2005 - these three partial-interest communities contributed \$7.1 million in 2005; and
- o Increased revenues at "same-units" communities - the 19 apartment communities that we owned as of January 1, 2004, contributed \$41.5 million in 2005, compared to \$40.6 million in 2004.

On a same-units basis, average economic occupancy was 94.6% in 2005 compared to 94.8% in 2004, and average monthly revenue per occupied unit was \$753 in 2005 compared to \$734 in 2004. In 2005, for all owned apartment communities, average economic occupancy was 94.7%, and average revenue per occupied unit was \$742.

Apartments NOI (apartment rental income less apartment operating expenses) totaled \$40.8 million in 2005, an increase of 52.1%, or \$14.0 million, compared to 2004. On a same-units basis, apartments NOI increased by 4.7% in 2005 compared to 2004.

Restaurant rental income totaled \$3.8 million in both 2005 and 2004. We received the minimum rent specified in the lease agreement in both years. Under our master lease with Boddie-Noell

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Enterprises, restaurant rental income payments are the greater of specified minimum rent or 9.875% of food sales. Minimum rent is set at approximately \$8,000 per month, or \$96,000 per year, per restaurant property. We currently hold 40 restaurant properties under this lease, and minimum rent is currently set at \$319,000 per month, or \$3.8 million per year.

Same-store sales (all 40 of the restaurant properties were open throughout all of 2005 and 2004) declined by 5.9% in 2005 compared to 2004. Sales at these restaurants would have to increase by 7.1% before we would receive percentage rent in excess of the minimum.

Management fee income totaled \$131,000 in 2005, compared to \$761,000 in 2004. This decrease is consistent with expectations, and is attributable to the elimination of management fees for consolidated limited partnerships and our acquisition of four managed properties in the first quarter of 2005. Going forward, we expect that management fees will be insignificant.

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We recorded casualty gains of \$668,000 in 2005 and \$269,000 in 2004, related to fires that occurred at apartment properties - in each case, one building incurred significant damage. We received, or expect to receive, insurance proceeds for the casualties, against which we identified and wrote off the net carrying values of the assets destroyed. GAAP require us to recognize the difference between the insurance proceeds and the net carrying value of the destroyed assets as a gain. However, we intend to reinvest all of the insurance proceeds in replacement assets. We are insured for the losses, including rent continuation insurance that covers 100% of lost rental income.

### Expenses

Total expenses, including non-cash charges for depreciation, amortization and write-off of unamortized loan costs, totaled \$82.4 million in 2005, an increase of 68.1% compared to 2004. This increase is primarily attributable to growth in the size of our apartment operations, along with charges for deficit distributions to a minority partner in a consolidated limited partnership.

We reflect the unaffiliated partners' share of the underlying net assets of the three consolidated limited partnerships as "minority interest in consolidated limited partnerships." When these consolidated limited partnerships make cash distributions to partners in excess of the carrying amount of the minority interest as measured by GAAP, we record a charge equal to the amount of such excess distributions, even though there is no economic effect or cost to the operating partnership. We report this charge in our consolidated financial statements of operations as deficit distributions to minority partners. We recorded charges for deficit distributions to the minority partner in the Marina Shores Partnership totaling \$7.9 million in 2005.

Apartment operations expense totaled \$26.2 million in 2005, an increase of 44.8%, or \$8.1 million, compared to 2004. This line item includes only direct costs of on-site apartment operations. The increase is attributable to:

- o Apartment acquisitions in 2004 and 2005 - apartment operations expense for these 11 owned communities totaled \$7.3 million in 2005, compared to \$1.8 million in 2004; and
- o Apartment communities that we consolidate effective January 2005 - apartment operations expense for these three partial-interest communities totaled \$2.7 million in 2005.

On a same-units basis, apartment operations expense declined by 1.0% in 2005 compared to 2004.

Operating expenses for restaurant properties are insignificant because the triple-net lease arrangement requires the lessee to pay virtually all of the expenses associated with the restaurant properties.

Apartment administration costs (the costs associated with oversight, accounting and support of our apartment management activities) totaled \$3.2 million in 2005, an increase of 45.5%, or \$1.0 million, compared to 2004. This increase is primarily attributable to additional corporate support and operations staff. In 2005 we began a major effort to improve our systems and operations - including adding a vice president of operations position, substantial upgrades to our computer systems, adding certain operational personnel and expanding our operating facility. Our objective in undertaking this effort is to increase the efficiency of our operations and to allow us to continue to grow without disruption. While this effort entails considerable



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up-front costs, we believe that it will yield significant long-term cost benefits.

Corporate administration expense totaled \$3.0 million in 2005, an increase of 31.6%, or \$0.7 million, compared to 2004. This increase is primarily attributable to a \$284,000 increase in professional fees associated with requirements of Section 404 of the Sarbanes-Oxley Act of 2002 and late audit fee billings, along with increases in executive compensation.

Effective August 1, 2005, the Board of Directors granted and caused the company to issue 200,000 restricted shares of the company's common stock to four of our executive officers. We refer to these shares as "nonvested shares" in our consolidated financial statements. All of the shares were unvested on the date of grant, and will vest 10% per year beginning July 1, 2006, and on each July 1 thereafter until fully vested. During 2005, we recorded \$143,000 in service cost related to nonvested common stock, included in corporate administration expense in our financial statements. We will continue to recognize the cost of these awards on a straight-line basis for each annual vesting period ending June 30 through 2015.

Interest expense totaled \$22.6 million in 2005, an increase of 56.1%, or \$8.1 million, compared to 2004. This increase is primarily attributable to new debt issued or assumed in conjunction with acquisitions of apartment communities during 2004 and 2005, along with the impact of consolidating three limited partnerships in 2005. Overall, weighted average interest rates were 5.8% in 2005, compared to 5.7% in 2004, reflecting the impact of steady increases in variable interest rates over the last 12 months, mitigated somewhat by the favorable impact of our refinancing activities during 2005.

During 2005 we recorded \$2.1 million in charges for penalties paid at refinance of debt, including \$519,000 paid by the Marina Shores Partnership in January 2005 and \$1.6 million paid by the operating partnership in conjunction with refinance transactions in late December 2005.

Depreciation expense totaled \$16.6 million in 2005, an increase of 44.5%, or \$5.1 million, compared to 2004. This increase is primarily attributable to acquisitions of apartment communities, along with depreciation expense for the apartment communities that we consolidate effective January 2005.

### Net income

Consolidated earnings from continuing operations before non-cash charges (for depreciation, amortization and write-off of unamortized loan costs at refinance) and before the \$7.9 million charge for deficit distributions to a minority partner totaled \$14.8 million, an increase of 14.8%, or \$1.9 million, compared to 2004. This increase reflects the positive impact of new apartment communities and improvements in apartment revenues, offset by \$2.1 million in charges for prepayment penalties paid in loan refinance transactions.

The net loss from continuing operations, before minority interests, totaled \$10.4 million, compared to \$1.0 million income before minority interests in 2004. The 2005 losses again reflect the impact of \$2.1 million in prepayment penalties paid in loan refinance transactions, \$0.3 million in charges to write off unamortized loan costs at refinance and \$7.9 million in charges for deficit distributions to a minority partner (which involved no cash outlay or economic effect to the operating partnership).

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partnerships, measured on a year-to-date basis, to minority partners. However, we may allocate losses to a minority partner only to the extent of the carrying amount of the interest of that minority partner. When losses attributable to the minority limited partners of a consolidated limited partnership exceed their positive capital balances, we record a charge, even though there is no cash outlay by the operating partnership. During 2005, we recorded charges of \$126,000 to absorb losses that could not be allocated to minority partners' accounts. As of the end of 2005, all of the capital accounts of minority partners in the consolidated limited partnerships have been depleted, and we expect to continue to record charges for these losses going forward.

Minority interests in the consolidated limited partnerships and the operating partnership absorbed \$2.3 million of the consolidated losses from continuing operations in 2005. The comparable allocation to the minority interest in the operating partnership in 2004 was only \$1,000. After allocating these losses to minority interests, the net loss from continuing operations was \$8.1 million in 2005, compared to \$1.0 million net income from continuing operations in 2004.

Amounts for discontinued operations reflect the operating results of Savannah Shores Apartments from July 2004 through October 2005. Savannah Shores generated \$88,000 in operating income in 2005, compared to \$95,000 in operating income in 2004. In October 2005, we sold Savannah Shores Apartments for a contract price of \$22.75 million to an unaffiliated third party. Net proceeds of the sale were \$22.2 million, and we recorded a gain on the sale of real estate assets of \$8.1 million. After allocating \$1.7 million of the income from discontinued operations to operating partnership minority unitholders, income from discontinued operations totaled \$6.6 million in 2005, compared to \$77,000 in 2004. The net loss was \$1.5 million in 2005, compared to net income of \$1.0 million in 2004.

In November 2005, we redeemed all of the outstanding shares of preferred stock in exchange for shares of our common stock. Because the preferred shareholder had priority over common shareholders for receipt of dividends prior to this conversion, we deduct the amount of net income to be paid to the preferred shareholder in calculating net income available to common shareholders - \$833,000 in 2005 and \$1.0 million in 2004.

The net loss attributed to common shareholders in 2005 was \$2.3 million, or \$0.25 on a diluted per share basis, compared to net income in 2004 of \$39,000, or \$0.01 on a diluted per share basis.

2004 compared to 2003

### Revenues

Revenues in 2004 totaled \$50.0 million, an increase of 17.2% compared to 2003. Apartment related income accounted for 92.3% of our total revenue in 2004, compared to 90.8% in 2003.

Apartment rental income in 2004 totaled \$44.9 million, an increase of 19.9%, or \$7.5 million, compared to 2003. \$6.0 million of this increase is attributable to rental income at six apartment communities that we acquired during 2004 and 2003. On a same-units basis (for the 4,427 units that we owned throughout all of both 2004 and 2003), apartment rental income increased by \$1.4 million, or 4.0%, compared to 2003.

On a same-units basis, average economic occupancy was 94.8% in 2004 compared to 92.9% in 2003, and average monthly revenue per occupied unit was \$739 in 2004 compared to \$728 in 2003. In 2004, for all apartment units, average economic occupancy was 94.4%, and average revenue per occupied unit was \$737.

Restaurant rental income in 2004 totaled \$3.8 million, a decline of 2.0% compared to 2003. The decrease in restaurant rental income is due to the sale of two restaurant properties in 2003. We received the minimum rent specified in the lease agreement throughout both years.

Same-store sales (for the 40 restaurants that were open throughout all of both 2004 and 2003) increased by 8.5% in 2004 compared to 2003. For the first time in almost nine years, during the second and third quarters of 2004, sales at our restaurant properties exceeded the threshold for percentage rent; however, for the full 12-month period, sales fell 1.3% short of the threshold for rent exceeding the minimum rent.

Management fee income in 2004 totaled \$0.8 million, a decline of 12.8% compared to 2003. This decrease is primarily attributable to our acquisitions of two previously managed properties (one in August 2003, and one in July 2004).

#### Expenses

Total expenses, including non-cash charges for depreciation, amortization and write-off of unamortized loan costs, totaled \$49.0 million in 2004, an increase of 14.7% compared to 2003.

Apartment operations expense totaled \$18.1 million in 2004, an increase of 17.2%, or \$2.6 million, compared to 2003. This increase is primarily attributable to operating expenses at six apartment communities that we acquired during 2004 and 2003. On a same-units basis, apartment operations expense increased by only 0.3% in 2004 compared to 2003.

Apartment administration expense totaled \$2.2 million in 2004, an increase of 29.2% compared to 2003. Corporate administration expense totaled \$2.3 million in 2004, an increase of 5.2% compared to 2003. These increases are attributable to additional corporate support staff, software and insurance costs, as well as approximately \$100,000 spent in 2004 for development of compliance documentation required by Section 404 of the Sarbanes-Oxley Act of 2002.

Interest expense totaled \$14.4 million in 2004, an increase of 11.1%, or \$1.4 million, compared to 2003. This increase reflects the impact of a net increase in outstanding debt, primarily at fixed rates, in 2004, related to apartment acquisitions. Overall, weighted average interest rates were 5.7% in 2004 and 5.9% in 2003.

Depreciation expense totaled \$11.5 million in 2004, an increase of 14.5%, or \$1.5 million, compared to 2003. This increase is attributable to the addition of six apartment communities during 2004 and 2003 and the impact of additions and replacements at other apartment communities. We generally assign those additions and replacements shorter lives than the composite lives we assigned at the acquisition of the assets to which the additions and replacements relate.

#### Net income

Earnings from continuing operations before non-cash charges for depreciation, amortization and write-off of unamortized loan costs totaled \$12.9 million in 2004, an increase of \$2.6 million, or 25.3%, compared to 2003. Net income from continuing operations, before minority interests, totaled \$961,000 in 2004, compared to a loss of \$66,000 in 2003.

Net income (after the minority interest in the operating partnership

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net income or loss, and before deduction for cumulative preferred dividend) was \$1.0 million in 2004, compared to \$107,000 in 2003.

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Income attributed to common shareholders in 2004 was \$39,000, or \$0.01 on a diluted per share basis, compared to loss attributed to common shareholders in 2003 of \$553,000, or \$0.09 on a diluted per share basis.

These favorable comparisons are primarily attributable to the positive impact of new apartment communities and improvements in apartment operating results.

### Funds from Operations - 2005, 2004 and 2003

Funds from operations and funds available for distribution are defined in footnote 2 at page 23. Both of these measures are made at the operating partnership level. You should read and understand that footnote before reviewing the following discussion.

We calculated FFO of the operating partnership as follows:

|   | 2005       | 2004      |    |
|---|------------|-----------|----|
|   | (000's)    | (000's)   |    |
| Net (loss) income   | \$ (1,488) | \$ 1,039  | \$ |
| Add income (loss) attributed to minority interests                                      | (668)      | 16        |    |
| Less cumulative preferred dividend  | (833)      | (1,000)   |    |
| Less gain on sale of real estate investments  | (8,132)    | -         |    |
| Less casualty gains   | (668)      | (269)     |    |
| Add amortization of in-place lease intangible   | 193        | -         |    |
| Add depreciation -  |            |           |    |
| - continuing operations   | 16,602     | 11,491    |    |
| - discontinued operations   | 259        | 170       |    |
| Add deficit distributions to minority partners of consolidated limited partnerships (1) | 7,861      | -         |    |
| Add minority interest in FFO of consolidated limited partnerships                       | 8          | -         |    |
| Funds from operations   | \$ 13,133  | \$ 11,447 | \$ |
|   | \$ 13,133  | \$ 11,447 | \$ |

Funds from operations in 2005 totaled \$13.1 million, an increase of 14.7% compared to 2004, in spite of \$1.6 million in charges for prepayment penalties (\$2.1 million in prepayment penalties paid in debt refinance transactions in 2005 on a consolidated basis, less \$0.5 million charge absorbed by the minority partner interest in the Marina Shores Partnership). Funds from operations in 2004 totaled \$11.5 million, an increase of 22.9% compared to 2003. These comparisons reflect the positive impact of new apartment communities and improved margins in apartment operations in 2004 and 2005.

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Funds available for distribution in 2005 (which also includes the \$1.6 million charge for prepayment penalties) totaled \$19.0 million, an increase of

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90.4% compared to 2004 - if not for the 2005 gain on sale of real estate assets and charge for prepayment penalties, this increase would be 25.2%. Funds available for distribution in 2004 totaled \$10.0 million, an increase of 26.4% compared to 2003. The disparity between comparisons of FFO and FAD against prior year periods generally arises from the impact of recurring capital expenditures, which we deduct in our measurement of FAD. Recurring capital expenditures include operating replacements such as floor coverings, appliances and HVAC, as well as expenditures for capital replacements such as roofs and exterior paint. Recurring capital expenditures at owned apartment properties averaged \$368 per apartment unit in 2005, \$354 per apartment unit in 2004, and \$374 per apartment unit in 2003.

A reconciliation of net cash provided by operating activities (as defined by GAAP and reflected in our consolidated statements of cash flows) to FAD follows:

|   | 2005      | 2004      |
|---|-----------|-----------|
|   | (000's)   | (000's)   |
| Net cash provided by operating activities   | \$ 12,793 | \$ 12,677 |
| Less cumulative preferred dividend  | (833)     | (1,000)   |
| Add gain on sale of real estate investments   | 8,132     | -         |
| Less casualty losses  | -         | (14)      |
| Less recurring capital expenditures   | (3,018)   | (1,918)   |
| Add amortization of interest defeasance   | -         | 105       |
| Add change in operating assets and liabilities, net                                       | 1,912     | 138       |
| Add minority interest in reconciling items arising from consolidated limited partnerships | 28        | -         |
|   | \$ 19,014 | \$ 9,988  |
| Funds available for distribution  | \$ 19,014 | \$ 9,988  |

Other information about our historical cash flows follows:

|  | 2005      | 2004      |
|--|-----------|-----------|
|  | (000's)   | (000's)   |
| Net cash provided by (used in)   |           |           |
| Operating activities   | \$ 12,793 | \$ 12,677 |
| Investing activities   | (61,444)  | (52,848)  |
| Financing activities   | 51,245    | 40,123    |
| Dividends and distributions paid to                                    |           |           |
| Preferred shareholder  | \$ 1,083  | \$ 1,000  |
| Common shareholders  | 9,306     | 7,551     |
| Minority unitholders in operating partnership                          | 2,121     | 1,847     |
| Scheduled debt principal payments, exclusive of financing transactions | \$ 2,379  | \$ 1,378  |
| Non-recurring capital expenditures                                     |           |           |
| Acquisition improvements and replacements                              | \$ 2,117  | \$ 1,104  |
| Apartment property additions and betterments                           | 1,935     | 1,613     |
| Reconstruction and replacement of casualty losses                      | 1,227     | 526       |

|  | 2005    | 2004    |
|--|---------|---------|
|  | (000's) | (000's) |
| Weighted average Preferred B shares outstanding                      | 790     | 909     |
| Weighted average common shares outstanding                           | 9,389   | 7,617   |
| Weighted average operating partnership<br>minority units outstanding | 2,301   | 1,856   |

#### Inflation

We do not believe that inflation poses a material risk to the company. The leases at our apartment properties are short term in nature. None are longer than two years. The restaurant properties are leased on a triple-net basis, which places the risk of rising operating and maintenance costs on the lessee.

#### Off balance sheet arrangements

We received \$3.8 million in rent from Boddie-Noell Enterprises for use of our restaurant properties in 2005. In addition to rental payments to us, Boddie-Noell Enterprises is responsible for all of the costs associated with the maintenance and operations of these properties, including property taxes, property insurance and capital replacements and betterments to the real estate assets.

#### Contractual obligations

Our contractual obligations as of December 31, 2005, are summarized as follows (all amounts in thousands):

|   | Total             | Payments due by period |                  |                  |
|---|-------------------|------------------------|------------------|------------------|
|   |                   | Less<br>than 1 year    | 1 - 3 years      | 3 - 5 years      |
| Long-term debt obligations  |                   |                        |                  |                  |
| - owned properties  | \$ 388,576        | \$ 10,167              | \$ 76,732        | \$ 65,223        |
| - consolidated limited partnerships   | 48,136            | 811                    | 1,728            | 1,897            |
| Operating lease - corporate office  | 545               | 225                    | 320              | -                |
| Purchase obligations for improvements<br>and replacements to real estate assets | 2,532             | 2,532                  | -                | -                |
| <b>Total</b>  | <b>\$ 439,789</b> | <b>\$ 13,735</b>       | <b>\$ 78,780</b> | <b>\$ 67,120</b> |

#### Environmental matters

Phase I environmental studies performed on the apartment communities when we acquired each of them did not identify any problems that we believe would have a material adverse effect on our results of operations, liquidity or

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capital resources. Environmental transaction screens for each of the restaurant properties in 1995 did not indicate existence of any environmental problems that warranted further investigation. Boddie-Noell Enterprises has indemnified us under the master lease for environmental problems associated with the restaurant properties.

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### Critical accounting policies

We identify and discuss our significant accounting policies that directly impact our financial statements in the notes to those financial statements included in this Annual Report. Those policies that may be of particular interest to readers of this Annual Report are further discussed below.

#### Accounting for general partner interests in limited partnerships

As managing general partner in three real estate limited partnerships, we have the ability to exercise significant influence over operating and financial policies and activities. The appropriate accounting treatment for our interests in these partnerships varies.

If the partnership is considered a variable interest entity ("VIE") and we are the "primary beneficiary," as defined by GAAP, we include the accounts of the partnership in our consolidated financial statements. We initially record all of the VIE's assets, liabilities and minority interests at fair value. If we, as general partner, control a partnership that is not a VIE, we also include the accounts of the partnership in our consolidated financial statements. We initially record our prorata interest in the partnership's assets and liabilities at the lower of our cost or fair value; we reflect the minority partners' interest in the partnership's assets and liabilities at historical cost, except to adjust an existing deficit capital account balance to \$-0-.

If a consolidated limited partnership makes distributions to a minority partner in excess of the positive balance in such partner's capital account, we record a charge to our earnings for "deficit distributions to minority partners," even though the cash outlay is made by the consolidated limited partnership, and not by our operating partnership.

We allocate proportional income and losses of the consolidated limited partnerships to minority partners; however, we may allocate losses to a minority partner only to the extent of his positive capital account balance. If losses attributable to a minority partner exceed his capital account balance, we record a charge to our earnings to absorb those losses, even though our operating partnership suffers no adverse economic effect.

#### Purchase price allocation for apartment community acquisitions

In connection with the acquisition of an apartment community, we perform a valuation and allocation to each significant asset and liability in such transaction, based on their estimated fair values at the date of acquisition. Significant tangible asset values generally include real estate investments, which we subsequently depreciate over their estimated useful lives. We include an estimate of intangible asset values, generally consisting of at-market, in-place leases, and amortize these amounts over the remaining lease terms as a reduction in reported rental income. In general, we have found that the average remaining life of in-place leases at acquisition date ranged from five to nine months, and such intangible assets represented approximately 0.1% to 0.3% of contract prices.

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### Capital expenditures and depreciation

In general, for the 16 apartment properties acquired before 2002, we compute depreciation using the straight-line method over composite estimated useful lives of the related assets, generally 40 years for buildings, 20 years for land improvements, 10 years for fixtures and equipment, and five years for floor coverings.

For apartment properties acquired after 2001, we performed detailed analyses of components of the real estate assets acquired. For these properties, we assigned estimated useful lives, based on age and

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condition at acquisition, as follows: base building structure, 43-60 years; land improvements, 7-20 years; short-lived building components, 5-20 years; and fixtures, equipment and floor coverings, 5-10 years.

We generally complete and capitalize acquisition improvements (planned expenditures we identify when we acquire the property and that are intended to position the property consistent with our physical standards) within one to two years of acquisition of the related apartment property. We capitalize non-recurring expenditures for additions and betterments to buildings and land improvements. In addition, we generally capitalize recurring capital expenditures for exterior painting, roofing, and other major maintenance projects that substantially extend the useful life of existing assets. For financial reporting purposes, we depreciate these additions and replacements on a straight-line basis over estimated useful lives of 5-20 years. We retire replaced assets with a charge to depreciation for any remaining carrying value. We capitalize all floor covering, appliance, and HVAC replacements, and depreciate them using a straight-line, group method over estimated useful lives of 5-10 years.

Capital expenditures at our owned apartment communities during 2005 totaled \$7.9 million, including \$2.1 million for acquisition improvements, \$1.9 million for additions and betterments, \$1.2 million for reconstruction and replacement of casualty losses, and \$2.7 million in recurring capital expenditures.

We expense ordinary repairs and maintenance costs at apartment communities. Repairs and maintenance at our owned apartment communities during 2005 totaled \$8.7 million, including \$3.2 million in compensation of service staff and \$5.5 million in payments for materials and contracted services.

Costs of repairs, maintenance, and capital replacements and improvements at restaurant properties are borne by the lessee.

### Impairment of long-lived assets

We evaluate our real estate assets when significant adverse changes in operations or economic conditions occur in order to assess whether any impairment indicators are present that affect the recovery of the recorded values. If we considered any real estate assets to be impaired as defined by GAAP, we would record a loss to reduce the carrying value of the property to its estimated fair value. Through December 31, 2005, there have been no such circumstances, and we considered none of our assets impaired.

### Revenue recognition

We record rental and other income monthly as it is earned. We record rental payments that we receive prior to the first of a given month as prepaid



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rent. We hold tenant security deposits in trust in bank accounts separate from operating cash (these amounts are included in other current assets on our balance sheet), and we record a corresponding liability for security deposits on our balance sheet.

We amortize any cash concessions given at the inception of an apartment lease over the approximate life of the lease, which is generally one year or less. In general, cash concessions range from \$100 to \$300 and are taken by residents during the first two months of the lease.

### Stock-based compensation

The company has one employee Stock Option and Incentive Plan in place, which we describe in more detail in the notes to our financial statements in this Annual Report. Prior to July 1, 2005, we accounted for options granted under this plan using the intrinsic value method; no stock-based employee compensation expense was reflected in our earnings, as all outstanding options had been granted at

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exercise prices equal to market value of the underlying stock on the dates of grant. All outstanding options were fully vested by the end of 2004.

Effective July 1, 2005, we adopted the fair value recognition provisions of Statement No. 123, as revised in 2004 ("FAS 123(R)"), using the modified-prospective transition method. Under this transition method, compensation cost recognized in the second half of 2005 includes compensation cost for all share-based payments granted subsequent to July 1, 2005, based on the grant-date fair value estimated in accordance with the provisions of FAS 123(R). Under the modified-prospective transition method, there is no compensation cost recognized for previously granted options that were fully vested prior to July 1, 2005.

### Additional Information

We provide the following information to analysts and other members of the financial community for use in their detailed analysis. This information has not been included in our Annual Report to Shareholders.

A summary of capital expenditures for owned apartment properties, in aggregate and per apartment unit, follows:

|                                 | 2005           |              | 2004           |              | 2003           |
|---------------------------------|----------------|--------------|----------------|--------------|----------------|
|                                 | Total          | Per unit     | Total          | Per unit     | Total          |
|                                 | (000's)        |              | (000's)        |              | (000's)        |
| Recurring capital expenditures: |                |              |                |              |                |
| Floor coverings                 | \$1,255        | \$173        | \$ 775         | \$143        | \$ 772         |
| Appliances/HVAC                 | 464            | 64           | 385            | 71           | 256            |
| Exterior paint                  | 11             | 2            | -              | -            | 183            |
| Computer/support equipment      | 107            | 15           | 4              | 1            | 85             |
| Other                           | 832            | 115          | 754            | 139          | 436            |
|                                 | <u>\$2,669</u> | <u>\$368</u> | <u>\$1,918</u> | <u>\$354</u> | <u>\$1,731</u> |

Non-recurring capital

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expenditures:

|                                 |         |         |         |
|---------------------------------|---------|---------|---------|
| Acquisition improvements        | \$2,117 | \$1,104 | \$1,053 |
| Additions and betterments       | 1,621   | 1,541   | 508     |
| Replacements of casualty losses | 1,227   | 526     | -       |
| Computer/support equipment      | 314     | 72      | 57      |
|                                 | -----   | -----   | -----   |
|                                 | \$5,279 | \$3,243 | \$1,619 |
|                                 | =====   | =====   | =====   |

### ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

All of our long-term debt is collateralized by real estate investments. A summary of long-term debt as of December 31, 2005 and 2004 is included in the notes to the financial statements included in this Annual Report. At December 31, 2005, on a consolidated basis, long-term debt totaled \$436.7 million, including \$383.0 million of notes payable at effective fixed interest rates ranging from 5.0% to 7.4% (the weighted average rate for fixed-rate notes was 5.8%), and \$53.7 million at variable rates indexed on 30-day LIBOR rates. Of the \$436.7 million in consolidated debt, \$388.6 million is related to properties wholly owned by the company, and \$48.1 million is related to properties in which the company has a partial interest.

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The weighted-average interest rate on debt outstanding at year end was 5.8% in 2005, 5.9% in 2004, and 5.8% in 2003. At our current level of variable-rate debt, a 1% change in variable interest rates would increase or decrease our annual interest expense by approximately \$550,000.

The table below provides information about our long-term debt instruments and presents expected principal maturities and related weighted average interest rates on those instruments:

|  | Expected maturity dates |          |          |          |          |           |
|--|-------------------------|----------|----------|----------|----------|-----------|
|  | 2006                    | 2007     | 2008     | 2009     | 2010     | Later     |
| -----                                  |                         |          |          |          |          |           |
| (all dollar amounts in thousands)      |                         |          |          |          |          |           |
| For owned properties:                  |                         |          |          |          |          |           |
| Fixed rate notes                       | \$ 2,103                | \$ 2,254 | \$41,946 | \$31,247 | \$20,914 | \$236,454 |
| Average interest rate                  | 5.9%                    | 5.9%     | 6.5%     | 5.3%     | 6.8%     | 5.7%      |
| Variable rate notes                    | \$ 8,064                | \$ 8,237 | \$24,296 | \$13,062 | \$ -     | \$ -      |
| Average interest rate                  | 6.4%                    | 6.3%     | 6.2%     | 6.2%     |          |           |
| For consolidated limited partnerships: |                         |          |          |          |          |           |
| Fixed rate notes (1)                   | \$ 627                  | \$ 664   | \$ 698   | \$ 743   | \$ 786   | \$ 43,594 |
| Average interest rate                  | 5.7%                    | 5.7%     | 5.7%     | 5.7%     | 5.7%     | 5.8%      |

We estimate the fair value of fixed-rate and variable-rate notes using discounted cash flow analyses, based on our current incremental borrowing rates for similar types of borrowing arrangements. On a consolidated basis, the carrying value of our notes payable at December 31, 2005, approximated fair value.

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### ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The financial statements and supplementary data are listed under Item 15(a) and filed as part of this Annual Report on the pages indicated.

### ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

In September 2005, we announced that we had dismissed Ernst & Young LLP and engaged Grant Thornton LLP as the new principal accountant to audit the company's consolidated financial statements. The Audit Committee of the Board of Directors approved the decision to change accountants.

Ernst & Young LLP's reports on the company's consolidated financial statements for the years ended December 31, 2004 and 2003 did not contain an adverse opinion or a disclaimer of opinion, nor were such reports qualified or modified as to uncertainty, audit scope, or accounting principles.

In connection with Ernst & Young LLP's audits of the company's consolidated financial statements for the years ended December 31, 2004 and 2003, and through September 16, 2005, there had been no disagreements between the company and Ernst & Young LLP on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure, which disagreements, if not resolved to the satisfaction of Ernst & Young LLP, would have caused Ernst & Young LLP to make reference to the subject matter of such disagreement in its reports. No "reportable events" (as defined by Item 304(a)(1)(v) of Regulation S-K) occurred during the two most recent fiscal years and through September 16, 2005.

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### ITEM 9A. CONTROLS AND PROCEDURES

#### Management's Conclusions Regarding the Effectiveness of Disclosure Controls and Procedures

We have performed a review and evaluation, under the supervision and with the participation of management, including the Chairman, Chief Executive Officer and the Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this annual report on Form 10-K. Based on our review and evaluation, the Chairman, Chief Executive Officer and Chief Financial Officer have concluded that, as of December 31, 2005, our disclosure controls and procedures, as designed and implemented, were effective to provide reasonable assurance that information required to be disclosed in the reports we file and submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported as and when required, including reasonable assurance that information required to be disclosed by us in such reports is accumulated and communicated to our management, including our Chairman, Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosures.

#### Management Report on Internal Control Over Financial Reporting

Management of the company is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rules 13a-15(f) and 15d-15(f) promulgated under the Exchange Act as a process designed by, or under the supervision of, the company's principal executive and principal financial officers and effected by the company's Board of Directors, management and other personnel, to provide

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reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles, and includes those policies and procedures that:

- o pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the company's assets;
- o provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and the company's Board of Directors; and
- o provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

There are inherent limitations to the effectiveness of any system of internal controls, including the possibility of human error and the circumvention or overriding of controls and procedures. Accordingly, even effective internal control over financial reporting may not prevent or detect misstatements. Further, projections of any evaluation of effectiveness to future periods are subject to the risks that controls may become inadequate because of changes in conditions or that the degree of compliance with policies or procedures may deteriorate.

Management has assessed the effectiveness of our internal control over financial reporting as of December 31, 2005. In making this assessment, management used criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control-Integrated Framework. Based on our assessment, the company's management believes that, as of December 31, 2005, the company's internal control over financial reporting was effective based on those criteria. There were no material weaknesses identified in the course of our review and evaluation.

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Our independent registered public accounting firm, Grant Thornton LLP, has issued an audit report on management's assessment of the company's internal control over financial reporting, a copy of which is included herein.

### Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting identified in connection with our fourth quarter 2005 evaluation of such internal control that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

### Report of Independent Registered Public Accounting Firm

Board of Directors and Shareholders  
BNP Residential Properties, Inc.

We have audited management's assessment, included in the accompanying Management Report on Internal Control Over Financial Reporting, that BNP Residential Properties, Inc. (a Maryland corporation) maintained effective internal control over financial reporting as of December 31, 2005, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organization of the Treadway Commission (COSO). BNP Residential Properties,

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Inc.'s management is responsible for maintaining effective control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorization of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projection of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that BNP Residential Properties, Inc. maintained effective internal control over financial reporting as of December 31, 2005, is fairly stated, in all material respects, based on criteria established in Internal Control - Integrated Framework issued by the Committee of

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Sponsoring Organizations of the Treadway Commission (COSO). Also in our opinion, BNP Residential Properties, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2005, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of BNP Residential Properties, Inc. as of December 31, 2005, and the related consolidated statements of operations, shareholder's equity, and cash flows for the year then ended and our report dated March 6, 2006 expressed an unqualified opinion on those statements.

/s/Grant Thornton LLP

Charlotte, North Carolina

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March 6, 2006

### ITEM 9B. OTHER INFORMATION

None.

### PART III

### ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

The current directors hold office for the terms described below or until their successors are elected and qualified. The current members of our Board of Directors are identified in the following table, followed by biographical information on each member.

| Name   | Age | Position  | Director Since |
|--|-----|---|----------------|
| -----  |     |   |                |
| Directors serving until the 2006 annual meeting: |     |   |                |
| W. Michael Gilley                                | 50  | Director  | December 1997  |
| Peter J. Weidhorn                                | 58  | Director  | December 2001  |
| Directors serving until the 2007 annual meeting: |     |   |                |
| Philip S. Payne                                  | 54  | Chairman  | December 1997  |
| Stephen R. Blank                                 | 60  | Director  | May 1999       |
| Directors serving until the 2008 annual meeting: |     |   |                |
| D. Scott Wilkerson                               | 48  | Director, President,<br>Chief Executive Officer | December 1997  |
| Paul G. Chrysson                                 | 51  | Director  | December 1997  |

Philip S. Payne - Chairman of the Board of Directors. Mr. Payne joined BT Venture Corporation, which was subsequently purchased by the company, in 1990 as Vice President of Capital Markets Activities and became Executive Vice President and Chief Financial Officer in January 1993. He was named Treasurer in April 1995 and a Director in December 1997. In January 2004, Mr. Payne was named Chairman of the Board of Directors. From 1987 to 1990, he was a principal in Payne Knowles Investment Group, a financial planning firm. From 1983 to 1987, he was a registered representative with Legg Mason Wood Walker. From 1978 to 1983, Mr. Payne practiced law, and he currently maintains his license to practice law in Virginia. He received a BS degree from the College of William and Mary in 1973 and a JD degree in 1978 from the same institution. He is a member of the board of directors of the National Multi Housing Council and is a member of the Urban Land Institute (Multi Family Council - Gold). In addition, he is a

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member of the board of directors of Ashford Hospitality Trust, a REIT focused on the hospitality industry, and serves as chairman of its audit committee.

D. Scott Wilkerson - Director, President, Chief Executive Officer. Mr. Wilkerson joined BT Venture Corporation, which was subsequently purchased by the company, in 1987 and served in various officer-level positions, including Vice President of Administration and Finance and Vice President for Acquisitions and Development before becoming President in January 1994. He was named Chief Executive Officer in April 1995 and a Director in December 1997. From 1980 to 1986, Mr. Wilkerson was with Arthur Andersen LLP in Charlotte, North Carolina, serving as tax manager from 1985 to 1986. His specialization was in the representation of real estate investors, developers and management companies. Mr. Wilkerson received a BS degree in accounting from the University of North Carolina at Charlotte in 1980. He is a certified public accountant and licensed

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real estate broker. He serves on the boards of directors of the National Multi Housing Council and the National Apartment Association. He is President of the Apartment Association of North Carolina and is a past president of the Charlotte Apartment Association. He is active in various professional, civic and charitable activities.

Stephen R. Blank - Director. Mr. Blank is a Senior Fellow, Finance, with the Urban Land Institute, and an Adjunct Professor at the Columbia University Graduate School of Business. From 1993 to 1998, he was the Managing Director for Real Estate Investment Banking with CIBC Oppenheimer Corp. He is an independent trustee of Ramco-Gershenson Properties Trust and Atlantic Realty Trust, and serves on the board of directors of MFA Mortgage Investments, Inc. In addition, he serves as a member of the board of advisors of Paloma, LLC, the principal investor in a private multifamily real estate investment trust. Mr. Blank serves as the chair of the audit committees for both Ramco-Gershenson Properties Trust and MFA Mortgage Investments, Inc. He has over 20 years experience as a senior real estate investment banking officer, advising and evaluating a wide array of real estate companies, including publicly reporting companies.

Paul G. Chrysson - Director. Mr. Chrysson is President of C.B. Development Company, Inc., a developer of single-family and multi-family residential properties. Mr. Chrysson is a member of the Board of Advisors of Wachovia Bank (Forsyth County). He is a former director of Triad Bank and United Carolina Bank (North Carolina) and has served on the boards of various charitable organizations. He has been a licensed real estate broker since 1974 and has been actively involved in construction since 1978.

W. Michael Gilley - Director. Mr. Gilley is a private real estate investor and developer of single-family and multi-family residential properties. From January 1995 to January 1997, he was Executive Vice President of Greenbriar Corporation. He also served on their board of directors from September 1994 to September 1996. He has been a licensed real estate broker since 1984.

Peter J. Weidhorn - Director. Mr. Weidhorn is a consultant and private real estate investor in the multi-family housing market. From 1998 to 2000, he was Chairman of the Board, President and Director of WNY Group, Inc., a real estate investment trust that owned and operated 8,000 apartment units throughout New Jersey, Pennsylvania, Delaware and Maryland prior to its sale to the Kushner Companies. From 1981 to 1998, he was President of WNY Management Corp. Mr. Weidhorn serves on the boards of directors of Monmouth Real Estate Investment Corporation and The Community Development Trust, and is a past president of the New Jersey Apartment Association. Mr. Weidhorn currently serves as the chair of the audit committees of both Monmouth Real Estate Investment Corporation and The Community Development Trust. He has over 30 years of experience in the management, acquisition, and financing of commercial real estate. Mr. Weidhorn is a certified public accountant (inactive). He is active in various professional, civic and charitable activities.

We have set forth below a listing and brief biography of each of the executive officers of the company.

| Name               | Age | Position                                     | Office |
|--------------------|-----|--|--------|
| Philip S. Payne    | 54  | Chairman of the Board of Directors           | Octob  |
| D. Scott Wilkerson | 48  | Director, President, Chief Executive Officer | Octob  |

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|                 |    |  |  |
|-----------------|----|--|--|
| Eric S. Rohm    | 36 | Vice President, Secretary, General Counsel                                 |  |
| Pamela B. Bruno | 52 | Vice President, Treasurer, Chief<br>Financial Officer, Assistant Secretary |  |

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Messrs. Payne and Wilkerson are also members of our Board of Directors. Brief biographies of Messrs. Payne and Wilkerson are included above. Biographical information for our other executive officers follows.

Eric S. Rohm - Vice President, Secretary, General Counsel. Mr. Rohm joined the company in December 2002 as Vice President and General Counsel, and was named Secretary in May 2004. Prior to joining the company, Mr. Rohm was a partner in the Real Estate Department of Kennedy Covington Lobdell & Hickman, LLP in Charlotte, North Carolina, where he practiced law from 1994 to 2002. Mr. Rohm received an AB degree in government from Georgetown University in 1991, and his JD degree from The Ohio State University College of Law in 1994. Mr. Rohm is licensed to practice law in the State of North Carolina and is a member of the North Carolina State Bar, the North Carolina Bar Association, and the Association of Corporate Counsel.

Pamela B. Bruno - Vice President, Treasurer, Chief Financial Officer, Assistant Secretary. Ms. Bruno joined BT Venture Corporation in 1993 as Controller and became our Vice President and Chief Accounting Officer in October 1994. She was named Treasurer in May 2004, and named Chief Financial Officer in August 2005. From 1984 to 1993, Ms. Bruno was with Ernst & Young LLP, in Charlotte, North Carolina, and Anchorage, Alaska, serving as audit manager from 1987 through 1993. She received a BS degree in accounting from the University of North Carolina at Charlotte in 1984. She is a licensed certified public accountant and is a member of the North Carolina Association of Certified Public Accountants.

Other operating officers, along with brief biographical information, follow.

| Name              | Age | Position                            | Office |
|-------------------|-----|-------------------------------------|--------|
| Alex S. Burris    | 37  | Vice President, Operations          | June   |
| Teresa M. Sandman | 36  | Vice President, Property Management | May 2  |

Alex S. Burris - Vice President, Operations. Mr. Burris joined the company in June 2005 as Vice President of Operations. Prior to joining the company, Mr. Burris was vice president of information technology at Summit Properties, Inc., from November 1994 to May 2005. He received BS degrees in accounting and business administration from the University of North Carolina at Charlotte in 1991 and his MBA degree from the Fuqua School of Business at Duke University in 2004. Mr. Burris is a certified public accountant.

Teresa M. Sandman - Vice President, Property Management. Ms. Sandman joined the company in January 1991 and has served in various property management positions. She was named vice president in May 2004. She is a licensed real estate broker and holds designations as certified apartment manager and certified apartment property supervisor. She is a member of the Institute of Real Estate Management.

Audit committee financial experts

The members of our Audit Committee are Messrs. Blank, Gilley, and Weidhorn. Our Board of Directors has determined that Messrs. Blank and Weidhorn qualify as "audit committee financial experts"



as defined by SEC regulations. All three members are considered "independent" as defined by SEC regulations and rules of the American Stock Exchange, and "financially literate" under the rules of the American Stock Exchange. Messrs. Blank's and Weidhorn's relevant experience is described above in the biographical information for each.

#### Section 16(a) Beneficial Ownership Reporting Compliance

Based solely on a review of the copies of the forms in its possession, and on written representations from certain reporting persons, the company believes that during 2005 all of its executive officers and directors filed the reports required under Section 16(a) on a timely basis.

#### Code of Ethics

Our Board of Directors has adopted a Code of Conduct and Business Ethics that is applicable to all directors, officers and employees of the company. You may view this document at our Internet website at [www.bnp-residential.com](http://www.bnp-residential.com). You may obtain a copy of this document free of charge by mailing a written request to: Investor Relations, BNP Residential Properties, Inc., 301 South College Street, Suite 3850, Charlotte, NC 28202, or by sending an email request to: [investor.relations@bnp-residential.com](mailto:investor.relations@bnp-residential.com).

#### ITEM 11. EXECUTIVE COMPENSATION

##### Executive Compensation

The following tables provide information regarding the annual and long-term compensation of our chief executive officer, and the four other most highly paid officers of the company. We refer to them as the "named executive officers."

| Name and Principal Position  | Year | Annual compensation |        |           | Long-term Compensation Restricted Award |
|--|------|---------------------|--------|-----------|---|
|  |      | Salary              | Bonus  | Other (1) |   |
| D. Scott Wilkerson, President,<br>Chief Executive Officer                                      | 2005 | \$270,000           | \$ -   | \$184,500 | \$1,000                                 |
|  | 2004 | 228,750             | 11,250 | 59,189    |   |
|  | 2003 | 225,000             | -      | -         |   |
| Philip S. Payne, Chairman of the<br>Board of Directors   | 2005 | 270,000             | -      | -         | 1,000                                   |
|  | 2004 | 228,750             | 11,250 | 67,500    |   |
|  | 2003 | 225,000             | -      | -         |   |
| Eric S. Rohm, Vice President,<br>Secretary, General Counsel                                    | 2005 | 180,000             | -      | -         | 4,000                                   |
|  | 2004 | 145,000             | 15,000 | -         |   |
|  | 2003 | 140,000             | -      | -         |   |
| Pamela B. Bruno, Vice President,<br>Treasurer, Chief Financial Officer,<br>Assistant Secretary | 2005 | 180,000             | -      | -         | 4,000                                   |
|  | 2004 | 145,000             | 15,000 | 8,100     |   |
|  | 2003 | 136,250             | 18,750 | -         |   |
| Alex S. Burris, Vice President -<br>Operations   | 2005 | 80,770              | -      | -         |   |

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(1) Amounts reflect the value realized in exercise of stock options.

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(2) All restricted stock awards were nonvested at the date of grant, August 1, 2005, and will vest 10% per year beginning July 1, 2006, and on each July 1 thereafter until fully vested. All shares carry dividend and voting rights. As of December 31, 2005, all such shares were nonvested, and amounts and values of such restricted shares were 70,000 shares valued at \$1,120,000 for each of Messrs. Wilkerson and Payne, and 30,000 shares valued at \$480,000 for each of Mr. Rohm and Ms. Bruno.

The following table provides information regarding exercises of stock options by named executive officers during 2005 as well as the value of unexercised stock options held by named executive officers as of December 31, 2005. No options were granted during the year ended December 31, 2005.

| Name               | Number of Shares Acquired in Exercise | Value Realized in Exercise | Number of Securities Underlying Unexercised Options at Fiscal Year End Exercisable/Unexercisable |   | Value of Unexercised In-the-Money Options at Fiscal Year End Exercisable/Unexercisable |
|--------------------|---------------------------------------|----------------------------|--|---|--|
| D. Scott Wilkerson | 50,000                                | \$184,500                  | 50,000   | - | \$143,750  |
| Philip S. Payne    | -                                     | -                          | 100,000  | - | 331,250  |
| Pamela B. Bruno    | -                                     | -                          | 30,000   | - | 95,000   |

We do not have a long-term incentive plan in place other than our Stock Option and Incentive Plan described in Item 12 below.

### Compensation of Directors

During 2005, we paid directors' fees to each director who is not an executive officer of the company. During the year ended December 31, 2005, Messrs. Blank, Chrysson, Gilley, and Weidhorn were each paid annual retainers of \$12,000 plus fees totaling \$9,250 each for participation in board meetings. Messrs. Payne and Wilkerson did not receive any compensation for their service as directors.

### Employment Contracts and Termination of Employment and Change-in-Control Arrangements

In November 2005, the company executed definitive employment agreements and related restricted stock grants, effective August 1, 2005, with each of Philip S. Payne, Chairman of the Board of Directors, D. Scott Wilkerson, President and Chief Executive Officer, Pamela B. Bruno, Vice President, Treasurer and Chief Financial Officer, and Eric S. Rohm, Vice President, Secretary and General Counsel.

The term of each agreement for Messrs. Payne and Wilkerson is three years. For each of Ms. Bruno and Mr. Rohm, the term is one year. Each agreement

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automatically renews daily for the applicable term unless prior written notice is given. Messrs. Payne and Wilkerson will each be paid a base salary of \$300,000 per year. Ms. Bruno and Mr. Rohm will each be paid a base salary of \$200,000 per year. The Board of Directors may grant an annual bonus to each executive at its discretion. The executives are also entitled to other customary employment benefits including health, life and supplemental insurance and paid time off.

The Board also granted restricted stock awards as of August 1, 2005, to the executives discussed above. Messrs. Payne and Wilkerson each received 70,000 shares, and Ms. Bruno and Mr. Rohm each received 30,000 shares. The shares vest annually at the rate of 10% per year, subject to applicable change-of-control provisions discussed below. The restricted stock carries all rights of ownership, including the receipt of dividends. The full terms of the restricted stock grants are included in the employment agreements.

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Upon termination by the company without cause or by the executive for good reason (as those terms are defined in the respective employment agreements), not in connection with a change in control, each executive will receive:

- o a lump sum equal to the remaining employment term times the sum of the executive's current base salary and average annual bonuses earned over the three years prior to the effective date of termination; the executive also will be entitled to continued health, life and disability coverage for the remainder of the contract term or until securing other employment, subject to limitations imposed by tax laws and the company's plans;
- o any unvested company stock options and unvested shares of restricted stock that would have vested during the remainder of the executive's employment terms will vest; and
- o the executive will receive cash payments during the applicable remaining employment term equal to any dividend declared during that period on any shares of restricted stock that the executive forfeited as a result of his or her termination.

Upon a change in control, or if the executive is terminated without cause in contemplation of a change in control, each executive will receive:

- o a lump sum equal to his/her current base salary for the remaining employment term (unless the executive is offered and accepts employment with the acquiror);
- o a lump sum equal to the fair market value of 150,000 shares for Messrs. Payne and Wilkerson, and 25,000 shares for Ms. Bruno and Mr. Rohm;
- o a lump sum equal to the sum of each Special Dividend Amount with respect to any Special Dividend paid while the executive is employed under the agreement and before a change in control; and
- o full and immediate vesting of all company stock options and shares of restricted stock issued to the executive.

A Special Dividend is any dividend that exceeds previous customary amounts, exceeds cash flow from operations for the period, and follows a significant asset disposition or refinancing. The Special Dividend Amount is the product of

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the per share amount of a Special Dividend and 150,000 shares for Messrs. Payne and Wilkerson, and 25,000 shares for Ms. Bruno and Mr. Rohm.

### Compensation Committee Interlocks and Insider Participation

The members of our Compensation Committee are Messrs. Weidhorn, Blank and Chrysson. All three members are considered "independent" as defined by rules of the American Stock Exchange. Mr. Weidhorn is identified in Item 13. Certain Relationships and Related Transactions in our discussion of "BNP Residential Properties, Inc. and Preferred Investment I, LLC." Mr. Chrysson is identified in Item 13 in our discussion of "BNP Residential Properties, Inc. and the Chrysson Parties."

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### ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

#### Equity Compensation Plan

We have reserved 903,000 shares of the company's common stock for issuance under our employee Stock Option and Incentive Plan. Options and nonvested stock have been granted to employees at prices equal to the fair market value of the stock on the dates of grant. Options are generally exercisable in four annual installments beginning one year after the date of grant, and expire ten years after the date of grant.

The following table provides summary information, as of December 31, 2005, about securities to be issued under our equity compensation plan. More detailed information is provided in the notes to our financial statements included in this Annual Report.

| Plan category  | Number of securities to be issued upon exercise of outstanding options, warrants and rights | Weighted average exercise price of outstanding options, warrants and rights | Number of shares remaining available for future issuance under equity compensation plans |
|--|---|---|--|
| Equity compensation plans approved by security holders     | 270,000   | \$12.08   | 6  |
| Equity compensation plans not approved by security holders | -   | -   | -  |
| Total  | 270,000   | \$12.08   | 6  |

#### Security Ownership of Certain Beneficial Owners and Management - Common Stock

The following table provides certain information regarding beneficial ownership of common stock as of February 28, 2006, by each person or group known to be the beneficial owner of more than 5% of the company's common stock.

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| Name and address of beneficial owner   | Common Shares   |   |
|--|-----------------|---|
|  | Beneficially Ow | P |
|  | Number          |   |
| Cliffwood Partners LLC and affiliates<br>11726 San Vicente Blvd., #600, Los Angeles CA 90049 | 552,900         |   |

The following table provides certain information regarding beneficial ownership of common stock as of February 28, 2006, by each of the directors and named executive officers, and by all directors and officers as a group.

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| Directors and Officers (1)   | Common Shares      |         |
|--|--------------------|---------|
|  | Beneficially Owned |         |
|  | Number             | Percent |
| Philip S. Payne (2)  | 259,570            | 2.5%    |
| D. Scott Wilkerson (3)   | 163,343            | 1.6%    |
| Stephen R. Blank   | 1,000              | *       |
| Paul G. Chrysson (4)   | 293,766            | 2.8%    |
| W. Michael Gilley (5)  | 292,145            | 2.7%    |
| Peter J. Weidhorn  | 469,817            | 4.5%    |
| Pamela B. Bruno (6)  | 70,621             | *       |
| Eric S. Rohm   | 30,000             | *       |
| All directors and executive officers<br>as a group (8 persons) (7) | 1,580,262          | 14.2%   |

\* Less than 1 percent.

(1) Address for each person listed herein is 301 South College Street, Suite 3850, Charlotte NC 28202.

(2) Includes exercisable options for 100,000 shares of common stock.

(3) Includes exercisable options for 50,000 shares of common stock.

(4) Includes 276,766 shares issuable (at the company's option) in satisfaction of the right to redeem the same number of units owned by Mr. Chrysson in the operating partnership.

(5) Includes 292,145 shares issuable (at the company's option) in satisfaction of the right to redeem the same number of units owned by Mr. Gilley in the operating partnership.

(6) Includes exercisable options for 28,000 shares of common stock.

(7) Includes exercisable options for 178,000 shares and 568,911 shares issuable (at the company's option) in satisfaction of the right to redeem the same number of units in the operating partnership.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

BNP Residential Properties, Inc. and Preferred Investment I, LLC

During 2001 through 2003, we issued a total of 909,090 shares of our Series B Cumulative Convertible Preferred Stock to Preferred Investment I, LLC for net proceeds of \$9.6 million. We redeemed these preferred shares in November 2005 on a one-for-one basis through issuance of 909,090 shares of our common stock to Preferred Investment I, LLC, of which 454,545 were registered to Weidhorn Enterprises, a partnership between Peter J. Weidhorn and his wife.

Peter J. Weidhorn, the managing member of Preferred Investment I, LLC, ceased serving as the Series B Director on our Board of Directors upon

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redemption and was named as a regular director by our Board of Directors, to serve until our next annual meeting.

BNP Residential Properties, Inc. and the Chrysson Parties

In July 2004, we acquired Savannah Shores Apartments from members of a group that we refer to as the Chrysson Parties. We subsequently sold this property in October 2005. The initial purchase price was \$12.5 million, including assumption of \$12.2 million in debt obligations and \$0.2 million net operating liabilities in excess of operating assets acquired, and issuance of 7,695 operating partnership units with an imputed value of \$0.1 million. The acquisition agreement provided for potential earn-out of additional purchase consideration of up to \$1.7 million, which we paid through issuance of 130,770 operating partnership units in October 2005. In previous years during 1997 through 2002, we issued 1.5 million operating partnership common units to acquire eight apartment communities from this group.

Messrs. Chrysson and Gilley, who serve on our Board of Directors, are members of the Chrysson Parties.

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Notes Receivable from Management

In 1996 through 1999, Messrs. Payne and Wilkerson each borrowed \$70,000 on an interest-free basis from the company. The loans are secured by shares of the company's common stock and are payable in full six months after termination of employment.

### ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Grant Thornton LLP has served as our principal accountant and independent auditor since September 2005. Ernst & Young LLP served as our principal accountant and independent auditor from October 1996 until September 2005.

The Board of Directors, upon the recommendation of the Audit Committee, engaged Grant Thornton LLP to serve as our independent auditors for the fiscal year ending December 31, 2005. The Audit Committee also approves in advance all engagements of Grant Thornton LLP for audit-related, tax and other services.

The Board of Directors, upon the recommendation of the Audit Committee, engaged Ernst & Young LLP to serve as our independent auditors for the fiscal years ending December 31, 2004, and through September 2005. Ernst & Young LLP continues to provide tax compliance services. The Audit Committee also approves in advance all engagements of Ernst & Young LLP for audit-related, tax and other services.

The following table reflects fees from Grant Thornton LLP, and Ernst & Young LLP for services rendered to the company and its subsidiaries in 2005 and 2004:

| Nature of Services   | 2005       |
|--|------------|
| -----  |            |
| Grant Thornton LLP:  |            |
| Audit fees -   | \$ 242,000 |
| For audit of our 2005 annual financial statements , audit of | \$         |

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internal control over financial reporting (in 2005), and review of financial statements included in our Forms 10-Q for the periods ended March 31, June 30 and September 30, 2005

|  |         |
|--|---------|
| Audit-related fees -   | 16,000  |
| For services related to business acquisitions in 2005  |         |
| All other fees - (none in 2005 or 2004)  | -       |
| Ernst & Young LLP:   |         |
| Audit fees -   | 140,000 |
| For review of financial statements included in our Forms 10-Q for the periods ended March 31 and June 30, 2005, and late/additional billings for audit services provided in 2004; and for audit of our 2004 annual financial statements and audit of internal control over financial reporting (in 2004) |         |

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| Nature of Services   | 2005    |
|--|---------|
| Audit-related fees -   | 40,000  |
| For services related to business acquisitions, accounting consultations, SEC registration statements, and audit of the company's 401(k) plan (in 2004) |         |
| Tax fees -   | 130,000 |
| For tax compliance, tax advice, and tax planning   |         |
| All other fees - (none in 2005 or 2004)  | -       |

In addition, the Board of Directors, upon the recommendation of the Audit Committee, engaged Reznick Group and its affiliate, Reznick Fedder & Silverman PC, to provide additional audit- and accounting-related services. Fees from Reznick Group for assistance to management in our review and evaluation of internal control over financial reporting were \$104,000 in 2005 and \$137,000 in 2004.

### PART IV

#### ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

##### (a) 1. and 2. Financial Statements and Schedules

The financial statements and schedules listed below are filed as part of this Annual Report on the pages indicated.

Index to Financial Statements and Schedules

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Reports of Independent Registered Public Accounting Firms -

- Grant Thornton LLP

- Ernst & Young LLP

Consolidated Balance Sheets as of December 31, 2005 and 2004

Consolidated Statements of Operations for the Years Ended

December 31, 2005, 2004, and 2003

Consolidated Statements of Shareholders' Equity for the Years Ended

December 31, 2005, 2004, and 2003

Consolidated Statements of Cash Flows for the Years Ended

December 31, 2005, 2004, and 2003

Notes to Consolidated Financial Statements

Statements of Revenue and Certain Operating Expenses of Acquired Properties

Hamptons Apartments - For the year ended December 31, 2004, and 93 for the nine months ended September 30, 2005 (unaudited)

Timbers Apartments - For the year ended December 31, 2004, and 96 for the nine months ended September 30, 2005 (unaudited)

Schedules:

Schedule III - Real Estate and Accumulated Depreciation

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The financial statements and schedules are filed as part of this report. All other schedules are omitted because they are not applicable or the required information is included in the financial statements or notes thereto.

(a) 3. Exhibits

The Registrant agrees to furnish a copy of all agreements related to long-term debt upon request of the Commission.

Exhibit No.

- 2.1\* Master Agreement of Merger and Acquisition by and among BNP Residential Properties, Inc., BNP Residential Properties Limited Partnership, Paul G. Chrysson, James G. Chrysson, W. Michael Gilley, Matthew G. Gallins, James D. Yopp, and the partnerships and limited liability companies listed therein, dated September 22, 1997 (filed as Exhibit 2.1 to Registration Statement No. 333-39803 on Form S-2, December 16, 1997, and incorporated herein by reference)
- 2.2\* Amendment to Master Agreement of Merger and Acquisition dated September 22, 1997, by and among BNP Residential Properties, Inc., BNP Residential Properties Limited Partnership, Paul G. Chrysson, James G. Chrysson, W. Michael Gilley, Matthew G. Gallins, James D. Yopp, and the partnerships and limited liability companies listed therein, dated November 3, 1997 (filed as Exhibit 2.3 to BNP Residential Properties, Inc. Current Report on Form 8-K dated December 1, 1997, and incorporated herein by reference)
- 3.1\* Articles of Incorporation (filed as Exhibit 3.1 to BNP Residential Properties, Inc., Current Report on Form 8-K dated March 17, 1999, and incorporated herein by reference)
- 3.2\* Articles Supplementary, Classifying and Designating 909,090 Shares of Series B Cumulative Convertible Preferred Stock, dated December 28, 2001 (filed as Exhibit 3.1 to BNP Residential Properties, Inc. Current Report on Form 8-K dated December 28, 2001, and incorporated herein by reference)
- 3.3\* Amended and Restated By-Laws adopted May 20, 2004 (filed as



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- Exhibit 3.1 to BNP Residential Properties, Inc., Current Report on Form 8-K dated July 14, 2004, and incorporated herein by reference)
- 4.1\* Rights Agreement, dated March 18, 1999, between the Company and First Union National Bank (filed as Exhibit 4 to BNP Residential Properties, Inc. Current Report on Form 8-K dated March 17, 1999, and incorporated herein by reference)
- 4.2\* Registration Rights Agreement By and Among BNP Residential Properties, Inc. and Preferred Investment I, LLC, dated December 28, 2001 (filed as Exhibit 4 to BNP Residential Properties, Inc. Current Report on Form 8-K dated December 28, 2001, and incorporated herein by reference)
- 10.1 Employment Agreement dated August 1, 2005, between BNP Residential Properties, Inc. and Philip S. Payne
- 10.2 Employment Agreement dated August 1, 2005, between BNP Residential Properties, Inc. and D. Scott Wilkerson
- 10.3 Employment Agreement dated August 1, 2005, between BNP Residential Properties, Inc. and Pamela B. Bruno
- 10.4 Employment Agreement dated August 1, 2005, between BNP Residential Properties, Inc. and Eric S. Rohm
- 10.5\* Second Amended and Restated Agreement of Limited Partnership of BNP Residential Properties Limited Partnership dated as of March 17, 1999 (filed as Exhibit 10.1 to the company's Annual Report on Form 10-K for the year ended December 31, 1998, and incorporated herein by reference)

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- 10.6\* Amendment to Second Amended and Restated Agreement of Limited Partnership of BNP Residential Properties Limited Partnership, dated December 28, 2001 (filed as Exhibit 10.1 to BNP Residential Properties, Inc. Current Report on Form 8-K dated December 28, 2001, and incorporated herein by reference)
- 10.7\* Investment Agreement By and Between BNP Residential Properties, Inc. and Preferred Investment I, LLC, dated December 28, 2001 (filed as Exhibit 10.2 to BNP Residential Properties, Inc. Current Report on Form 8-K dated December 28, 2001, and incorporated herein by reference)
- 10.8\* Amended and Restated Master Lease Agreement dated December 21, 1995, between BNP Residential Properties, Inc. and Boddie-Noell Enterprises, Inc. (filed as Exhibit 10.1 to BNP Residential Properties, Inc. Annual Report on Form 10-K dated December 31, 1995, and incorporated herein by reference)
- 10.9\* Amended and Restated 1994 Stock Option and Incentive Plan (filed as Exhibit 10.1 to BNP Residential Properties, Inc. Current Report on Form 8-K dated May 19, 2005, and incorporated by reference herein)
- 10.10\* Purchase Agreement by and among BNP Residential Properties, Inc. and Purchasers for 1,175,519 shares of common stock, dated as of February 17, 2004 (filed as Exhibit 10.1 to BNP Residential Properties, Inc. Current Report on Form 8-K dated February 23, 2004, and incorporated herein by reference)
- 10.11\* Purchase Agreement by and among BNP Residential Properties, Inc. and Purchasers for 1,420,000 shares of common stock, dated as of July 14, 2004 (filed as Exhibit 10.1 to BNP Residential Properties, Inc. Current Report on Form 8-K dated July 14, 2004, and incorporated herein by reference)
- 10.12\* Exchange Agreement among BNP Residential Properties, Inc., BNP Residential Properties Limited Partnership, and Beach Investment Properties, LLC and members thereof, dated as of December 7,

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- 2004 (filed as Exhibit 10.9 to BNP Residential Properties, Inc. Annual Report on Form 10-K for the year ended December 31, 2004, and incorporated herein by reference)
- 10.13\* Exchange Agreement among BNP Residential Properties, Inc., BNP Residential Properties Limited Partnership, and Timberline Ventures, LLC and members thereof, dated as of December 7, 2004 (filed as Exhibit 10.10 to BNP Residential Properties, Inc. Annual Report on Form 10-K for the year ended December 31, 2004, and incorporated herein by reference)
- 10.14\* Exchange Agreement among BNP Residential Properties, Inc., BNP Residential Properties Limited Partnership, and Laurel Springs II, LLC and members thereof, dated as December 7, 2004 (filed as Exhibit 10.11 to BNP Residential Properties, Inc. Annual Report on Form 10-K for the year ended December 31, 2004, and incorporated herein by reference)
- 10.15\* Exchange Agreement among BNP Residential Properties, Inc., BNP Residential Properties Limited Partnership, and Salem Ridge/Shugart, LLC and members thereof, dated as of December 7, 2004 (filed as Exhibit 10.12 to BNP Residential Properties, Inc. Annual Report on Form 10-K for the year ended December 31, 2004, and incorporated herein by reference)
- 21 Subsidiaries of the Registrant
- 23.1 Consent of Grant Thornton LLP
- 23.2 Consent of Ernst & Young LLP
- 31.1 Rule 13a-14(a)/15d-14(a) Certification by Chairman
- 31.2 Rule 13a-14(a)/15d-14(a) Certification by Chief Executive Officer
- 31.3 Rule 13a-14(a)/15d-14(a) Certification by Chief Financial Officer
- 32.1 Section 1350 Certification by Chairman, Chief Executive Officer, and Chief Financial Officer
- \* Incorporated herein by reference

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

BNP RESIDENTIAL PROPERTIES, INC.  
(Registrant)

Date: March 6, 2006

/s/ Philip S. Payne

-----  
Philip S. Payne  
Chairman

Date: March 6, 2006

/s/ D. Scott Wilkerson

-----  
D. Scott Wilkerson  
President, Chief Executive Officer

Date: March 6, 2006

/s/ Pamela B. Bruno

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Pamela B. Bruno  
Vice President, Chief Financial Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

| Signature:  | Title:  | Date:         |
|---|---|---------------|
| /s/ Philip S. Payne<br>-----<br>Philip S. Payne       | Chairman of the Board of Directors                    | March 6, 2006 |
| /s/ D. Scott Wilkerson<br>-----<br>D. Scott Wilkerson | President, Chief Executive<br>Officer, Director       | March 6, 2006 |
| /s/ Pamela B. Bruno<br>-----<br>Pamela B. Bruno       | Vice President, Treasurer,<br>Chief Financial Officer | March 6, 2006 |
| /s/ Stephen R. Blank<br>-----<br>Stephen R. Blank     | Director  | March 6, 2006 |
| /s/ Paul G. Chrysson<br>-----<br>Paul G. Chrysson     | Director  | March 6, 2006 |
| /s/ W. Michael Gilley<br>-----<br>W. Michael Gilley   | Director  | March 6, 2006 |
| /s/ Peter J. Weidhorn<br>-----<br>Peter J. Weidhorn   | Director  | March 6, 2006 |

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## Report of Independent Registered Public Accounting Firm

Board of Directors and Shareholders  
BNP Residential Properties, Inc.

We have audited the accompanying consolidated balance sheet of BNP Residential Properties, Inc. (a Maryland corporation) as of December 31, 2005, and the related consolidated statements of operations, shareholder's equity, and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan

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and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of BNP Residential Properties, Inc. as of December 31, 2005, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The schedule titled "Schedule III - Real Estate and Accumulated Depreciation" is presented for the purposes for additional analysis and is not a required part of the basic financial statements. This schedule has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of BNP Residential Properties, Inc.'s internal control over financial reporting as of December 31, 2005, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated March 6, 2006 expressed an unqualified opinion thereon.

/s/Grant Thornton LLP

Charlotte, North Carolina  
March 6, 2006

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Report of Independent Registered Public Accounting Firm

Board of Directors and Shareholders  
BNP Residential Properties, Inc.

We have audited the accompanying consolidated balance sheet of BNP Residential Properties, Inc. as of December 31, 2004 and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the two years in the period ended December 31, 2004. Our audits also included the 2004 and 2003 information in the financial statement schedule listed in the Index at Item 15(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a

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test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of BNP Residential Properties, Inc. at December 31, 2004 and the consolidated results of its operations and its cash flows for each of the two years in the period ended December 31, 2004, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the 2004 and 2003 information in the financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ Ernst & Young LLP

Greenville, South Carolina  
March 2, 2005

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BNP RESIDENTIAL PROPERTIES, INC.  
Consolidated Balance Sheets  
(all amounts in thousands except share data)

|  | December 31       |       |
|--|-------------------|-------|
|  | 2005              | 2004  |
|  | -----             | ----- |
| <b>Assets</b>                                |                   |       |
| Real estate investments at cost:             |                   |       |
| Apartment properties                         | \$ 559,560        |       |
| Restaurant properties                        | 37,405            |       |
|  | -----             |       |
|  | 596,965           |       |
| Less accumulated depreciation                | (87,668)          |       |
|  | -----             |       |
|  | 509,297           |       |
| Cash and cash equivalents                    | 3,111             |       |
| Prepaid expenses and other assets            | 8,034             |       |
| Deferred financing costs, net                | 2,380             |       |
| Intangible assets, net                       | 1,240             |       |
|  | -----             |       |
| <b>Total assets</b>                          | <b>\$ 524,063</b> |       |
|  | =====             |       |
| <b>Liabilities and Shareholders' Equity</b>  |                   |       |
| Deed of trust and other notes payable        | \$ 436,712        |       |
| Accounts payable and accrued expenses        | 1,419             |       |
| Accrued interest on notes payable            | 1,345             |       |
| Consideration due for completed acquisitions | 1,000             |       |
| Deferred revenue and security deposits       | 1,950             |       |
|  | -----             |       |
|  | 442,426           |       |

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|   |            |
|---|------------|
| Minority interest in consolidated limited partnerships  | -          |
| Minority interest in operating partnership  | 21,207     |
| Shareholders' equity:   |            |
| Preferred stock, \$.01 par value, 10,000,000 shares authorized,<br>909,090 shares issued and outstanding at December 31, 2004   | -          |
| Common stock, \$.01 par value, 100,000,000 shares authorized,<br>10,385,890 shares issued and outstanding at<br>December 31, 2005 (including 200,000 nonvested shares), and<br>8,652,740 shares issued and outstanding at December 31, 2004 | 102        |
| Additional paid-in capital  | 122,516    |
| Dividend distributions in excess of net income  | (62,189)   |
|   | -----      |
| Total shareholders' equity  | 60,429     |
|   | -----      |
| Total liabilities and shareholders' equity  | \$ 524,063 |
|   | =====      |

See accompanying notes.

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BNP RESIDENTIAL PROPERTIES, INC.  
Consolidated Statements of Operations  
(all amounts in thousands except per share amounts)

|   | Years ended December 31 |           |
|---|-------------------------|-----------|
|   | 2005                    | 2004      |
|   | -----                   | -----     |
| Revenues  |                         |           |
| Apartment rental income   | \$ 67,029               | \$ 44,929 |
| Restaurant rental income  | 3,830                   | 3,830     |
| Management fee income   | 131                     | 761       |
| Casualty gains  | 668                     | 269       |
| Interest and other income   | 355                     | 197       |
|   | -----                   | -----     |
|   | 72,012                  | 49,986    |
| Expenses  |                         |           |
| Apartment operations  | 26,243                  | 18,119    |
| Apartment administration  | 3,216                   | 2,210     |
| Corporate administration  | 3,039                   | 2,309     |
| Interest  | 22,555                  | 14,445    |
| Penalties paid at debt refinance                                      | 2,146                   | -         |
| Depreciation  | 16,602                  | 11,491    |
| Amortization of deferred loan costs                                   | 432                     | 365       |
| Write-off of unamortized loan costs at debt refinance                 | 294                     | 85        |
| Deficit distributions to minority partners                            | 7,861                   | -         |
|   | -----                   | -----     |
|   | 82,389                  | 49,025    |
| (Loss) income from continuing operations<br>before minority interests | (10,377)                | 961       |
| Loss (income) attributed to minority interests                        |                         |           |
| - Consolidated limited partnerships                                   | 350                     | -         |

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|   |            |         |
|---|------------|---------|
| - Operating partnership                         | 1,975      | 1       |
| <hr style="border-top: 1px dashed black;"/>     |            |         |
| (Loss) income from continuing operations        | (8,052)    | 962     |
| Discontinued operations:                        |            |         |
| Income from discontinued operations             | 88         | 95      |
| Gain on sale of real estate assets              | 8,132      | -       |
| (Income) loss attributed to minority interests  | (1,657)    | (17)    |
| <hr style="border-top: 1px dashed black;"/>     |            |         |
| Income from discontinued operations, net        | 6,563      | 77      |
| <hr style="border-top: 1px dashed black;"/>     |            |         |
| Net (loss) income                               | (1,488)    | 1,039   |
| Cumulative preferred dividend                   | (833)      | (1,000) |
| <hr style="border-top: 1px dashed black;"/>     |            |         |
| (Loss) income attributed to common shareholders | \$ (2,322) | \$ 39   |
| <hr style="border-top: 3px double black;"/>     |            |         |

(continued)

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BNP RESIDENTIAL PROPERTIES, INC.  
Consolidated Statements of Operations - continued  
(all amounts in thousands except per share amounts)

|   | Years ended December 31 |         |
|---|-------------------------|---------|
|   | 2005                    | 2004    |
| Weighted average common shares outstanding      | 9,389                   | 7,617   |
| Per common share amounts:                       |                         |         |
| Earnings per common share - basic               |                         |         |
| (Loss) income from                              |                         |         |
| - Continuing operations                         | \$ (0.87)               | \$ 0.13 |
| - Discontinued operations                       | 0.71                    | 0.01    |
| <hr style="border-top: 1px dashed black;"/>     |                         |         |
| Net (loss) income                               | (0.16)                  | 0.14    |
| (Loss) income attributed to common shareholders | (0.25)                  | 0.01    |
| Earnings per common share - diluted             |                         |         |
| (Loss) income from                              |                         |         |
| - Continuing operations                         | \$ (0.87)               | \$ 0.10 |
| - Discontinued operations                       | 0.71                    | 0.01    |
| <hr style="border-top: 1px dashed black;"/>     |                         |         |
| Net (loss) income                               | (0.16)                  | 0.11    |
| (Loss) income attributed to common shareholders | (0.25)                  | 0.01    |
| <hr style="border-top: 1px dashed black;"/>     |                         |         |
| Dividends declared per common share             | \$ 1.00                 | \$ 1.00 |

See accompanying notes.

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BNP RESIDENTIAL PROPERTIES, INC.  
Consolidated Statements of Shareholders' Equity  
(all amounts in thousands)

|   | Preferred Stock |          | Common Stock |        | Additional | Dividend      |
|---|-----------------|----------|--------------|--------|------------|---------------|
|   | Shares          | Amount   | Shares       | Amount | paid-in    | distributions |
|   |                 |          |              |        | capital    | in excess of  |
|   |                 |          |              |        |            | net income    |
| Balance December 31, 2002                         | 454             | \$ 5,000 | 5,831        | \$ 58  | \$ 70,725  | \$ (36,512)   |
| Preferred stock issued                            | 455             | 5,000    | -            | -      | (54)       | -             |
| Common stock issued                               | -               | -        | 76           | 1      | 803        | -             |
| Dividends paid - preferred                        | -               | -        | -            | -      | -          | (537)         |
| Dividends paid - common                           | -               | -        | -            | -      | -          | (5,859)       |
| Net income  | -               | -        | -            | -      | -          | 107           |
| Balance December 31, 2003                         | 909             | 10,000   | 5,907        | 59     | 71,473     | (42,800)      |
| Common stock issued                               | -               | -        | 2,746        | 27     | 31,747     | -             |
| Dividends paid - preferred                        | -               | -        | -            | -      | -          | (1,000)       |
| Dividends paid - common                           | -               | -        | -            | -      | -          | (7,551)       |
| Net income  | -               | -        | -            | -      | -          | 1,039         |
| Balance December 31, 2004                         | 909             | 10,000   | 8,653        | 87     | 103,221    | (50,311)      |
| Common stock issued                               | -               | -        | 824          | 6      | 9,162      | -             |
| Preferred stock conversion                        | (909)           | (10,000) | 909          | 9      | 9,991      | -             |
| Service cost related to<br>nonvested common stock | -               | -        | -            | -      | 143        | -             |
| Dividends paid - preferred                        | -               | -        | -            | -      | -          | (1,083)       |
| Dividends paid - common                           | -               | -        | -            | -      | -          | (9,306)       |
| Net loss  | -               | -        | -            | -      | -          | (1,488)       |
| Balance December 31, 2005                         | -               | \$ -     | 10,386       | \$ 102 | \$ 122,516 | \$ (62,189)   |

See accompanying notes.

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BNP RESIDENTIAL PROPERTIES, INC.  
Consolidated Statements of Cash Flows  
(all amounts in thousands)

|                                | Years ended December 31 |           |
|--------------------------------|-------------------------|-----------|
|                                | 2005                    | 2004      |
| Operating activities           |                         |           |
| Apartment rental receipts, net | \$ 68,175               | \$ 45,717 |
| Restaurant rental receipts     | 3,830                   | 3,920     |

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|   |           |          |
|---|-----------|----------|
| Management fee receipts   | 131       | 762      |
| Interest and other income receipts  | 372       | 185      |
| Operating and administrative expense payments   | (34,186)  | (23,402) |
| Interest payments   | (23,382)  | (14,504) |
| Penalties paid at debt refinance  | (2,146)   | -        |
|   | -----     | -----    |
| Net cash provided by operating activities   | 12,793    | 12,677   |
| Investing activities  |           |          |
| Acquisitions of apartment properties  | (75,439)  | (48,148) |
| Acquisition of Boddie Investment Company, net of cash included in accounts of consolidated limited partnerships | 368       | -        |
| Additions to apartment communities  | (8,370)   | (5,161)  |
| Net (funding of) release from lender reserves for replacements  | (616)     | (457)    |
| Net proceeds, sale of real estate investments   | 22,082    | -        |
| Casualty proceeds   | 533       | 918      |
|   | -----     | -----    |
| Net cash used in investing activities   | (61,444)  | (52,848) |
| Financing activities  |           |          |
| Net proceeds from issuance of preferred stock   | -         | -        |
| Net proceeds from issuance of common stock  | 1,383     | 31,462   |
| Distributions to minority partners in consolidated limited partnerships   | (7,861)   | -        |
| Distributions to operating partnership minority unitholders   | (2,121)   | (1,847)  |
| Payment of dividends to preferred shareholder   | (1,083)   | (1,000)  |
| Payment of dividends to common shareholders   | (9,306)   | (7,551)  |
| Proceeds from notes payable   | 200,913   | 111,906  |
| Principal payments on notes payable   | (129,390) | (91,941) |
| Payment of deferred financing costs   | (1,291)   | (906)    |
|   | -----     | -----    |
| Net cash provided by financing activities   | 51,245    | 40,123   |
|   | -----     | -----    |
| Net increase (decrease) in cash and cash equivalents  | 2,594     | (47)     |
| Cash and cash equivalents at beginning of year  | 517       | 564      |
|   | -----     | -----    |
| Cash and cash equivalents at end of year  | \$ 3,111  | \$ 517   |
|   | =====     | =====    |

(continued)

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BNP RESIDENTIAL PROPERTIES, INC.  
Consolidated Statements of Cash Flows - continued  
(all amounts in thousands)

|  | Years ended December 31 |          |
|--|-------------------------|----------|
|  | 2005                    | 2004     |
|  | -----                   | -----    |
| Reconciliation of net income to net cash provided by operating activities: |                         |          |
| Net (loss) income  | \$ (1,488)              | \$ 1,039 |
| Amortization of intangible for in-place leases at acquisitions             | 193                     | -        |
| Casualty gains, net of losses  | (668)                   | (255)    |
| Amortization of debt premium   | (168)                   | (105)    |

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|   |           |           |
|---|-----------|-----------|
| Write-off of unamortized loan costs at debt refinance                           | 327       | 85        |
| Depreciation and amortization of deferred loan costs                            | 17,034    | 11,856    |
| Depreciation and amortization from discontinued operations                      | 273       | 179       |
| Deficit distributions to minority partners in consolidated limited partnerships | 7,861     | -         |
| Gain on sale of real estate assets  | (8,132)   | -         |
| Minority interest in consolidated limited partnerships                          | (350)     | -         |
| Minority interest in operating partnership                                      | (318)     | 16        |
| Compensation cost related to nonvested common stock                             | 143       | -         |
| Changes in operating assets and liabilities:                                    |           |           |
| Prepaid expenses and other assets   | (1,125)   | (336)     |
| Accounts payable and accrued expenses   | (707)     | 119       |
| Deferred revenue, prepaid rent and security deposits                            | (80)      | 79        |
|   | -----     | -----     |
| Net cash provided by operating activities                                       | \$ 12,793 | \$ 12,677 |
|   | =====     | =====     |

See accompanying notes.

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BNP RESIDENTIAL PROPERTIES, INC.  
Notes to Consolidated Financial Statements  
December 31, 2005

### Note 1. Summary of significant accounting policies

#### Basis of presentation

The consolidated financial statements include the accounts of BNP Residential Properties, Inc. (the "company") and BNP Residential Properties Limited Partnership (the "operating partnership"). We prepared the accompanying consolidated financial statements in accordance with accounting principles generally accepted in the United States ("GAAP").

Effective January 26, 2005, in connection with an acquisition on that date, the consolidated financial statements also include the accounts of three real estate limited partnerships (the "consolidated limited partnerships") in which we have general partner interests. The assets of consolidated limited partnerships controlled by the operating partnership generally are not available to pay creditors of the company or the operating partnership.

All significant intercompany balances and transactions have been eliminated in these consolidated financial statements.

We are a self-administered and self-managed real estate investment trust ("REIT") with operations in North Carolina, South Carolina and Virginia. Our primary activity is the ownership and operation of apartment communities. As of December 31, 2005, we owned and managed 30 apartment communities containing 7,945 units, and served as general partner of limited partnerships that owned three apartment communities containing 713 units. In addition to our apartment communities, at December 31, 2005, we owned 40 properties that we lease on a triple-net basis to a restaurant operator. The lessee operates these properties as restaurants and, under the terms of the lease, is totally responsible for the operation and maintenance of the properties.

#### UpREIT structure

We are structured as an UpREIT, or umbrella partnership real estate investment

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trust. The company is the general partner and owns a majority interest in the operating partnership, through which we conduct all of our operations. At December 31, 2005, we owned 80% of the common ownership units of the operating partnership. We refer to the limited partners of the operating partnership as minority common unitholders or as the operating partnership minority interest. Limited partners will generally be able to redeem their units for cash or, at our option as general partner, for shares of common stock of the company on a one-for-one basis. UpREITs are generally structured so that distributions of cash from the operating partnership are allocated between the REIT and the limited partners based on their respective unit ownership.

### Reclassifications

We have reclassified certain 2004 and 2003 amounts to conform to the current year presentation in the accompanying financial statements.

### Segment reporting

Operating segments are revenue-producing components of the company for which separate financial information is produced internally for our management. Under this definition, we operated, for all periods presented, as a single segment (apartment operations). Our apartment operating activities are located within a relatively small geographic area, and our chief operating decision maker does not receive or utilize financial information on the basis of geographic areas. We evaluate each community's

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performance individually; however, all of these communities are garden-style construction, operate in the mid-market price range, share similar economic characteristics, and provide similar services. We do not conduct any operating activities with regard to restaurant rental income; the triple-net lease arrangement for these properties requires the lessee to pay virtually all of the costs associated with these properties.

### Accounting for general partner interests in limited partnerships

As managing general partner in three real estate limited partnerships, we have the ability to exercise significant influence over operating and financial policies. This influence is evident in the terms of the respective partnership agreements. In acting as general partner in these limited partnerships, we are committed to providing additional levels of funding to meet partnership operating deficits as may be needed. The appropriate accounting treatment for our interests in these partnerships varies, depending on whether or not the partnership is considered a variable interest entity ("VIE").

In January 2003, the Financial Accounting Standards Board ("FASB") issued Interpretation 46, "Consolidation of Variable Interest Entities" ("FIN46"). In December 2003, the FASB modified FIN 46 to make certain technical corrections and address certain implementation issues that had arisen. FIN 46 provided a new framework for identifying VIEs and determining when a company should include the assets, liabilities, noncontrolling interests and results of activities of a VIE in its consolidated financial statements. In general, a VIE is an entity or other legal structure used to conduct activities or hold assets that either (1) has an insufficient amount of equity to carry out its principal activities without additional subordinated financial support, (2) has equity owners that, as a group, are unable to make significant decisions about its activities, or (3) has equity owners that, as a group, do not have the obligation to absorb losses or the right to receive returns generated by its operations.

FIN 46, as modified, requires that a VIE be consolidated if a party with an ownership, contractual or other financial interest in the VIE (a "variable interest holder") is obligated to absorb a majority of the risk of loss from the

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VIE's activities, is entitled to receive a majority of the VIE's residual returns (if no party absorbs a majority of the VIE's losses), or both. A variable interest holder that consolidates the VIE is called the "primary beneficiary." Upon consolidation, the primary beneficiary generally must initially record all of the VIE's assets, liabilities and noncontrolling interests at fair value, and must subsequently account for the VIE as if it were consolidated based on majority voting interest.

If we, as general partner, control a partnership that is not a VIE, generally accepted accounting principles require that we consolidate the partnership in our financial statements. Upon consolidation, we record our prorata interest in the partnership's assets and liabilities at the lower of our cost or fair value, and we subsequently account for the partnership based on our prorata interest; the noncontrolling interests are reflected in our financial statements at their historical costs.

### Accounting for discontinued operations

FASB Statement 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," requires that the assets and liabilities and the results of operations of any properties that have been sold, or otherwise qualify as held for sale, be presented as discontinued operations in our consolidated financial statements, for both current and prior periods presented. In addition, the net gain or loss on the disposal of properties held for sale is presented as discontinued operations. A change in presentation for discontinued operations does not have any impact on our financial condition or results of operations. We record no depreciation for the community assets once the community is classified as held for sale.

### Real estate investments

Real estate investments are stated at the lower of cost, less accumulated depreciation, or fair value. In general, for properties acquired prior to 2002, we compute depreciation using the straight-line method over composite estimated useful lives of the related assets, generally 40 years for buildings, 20 years for land improvements, 10 years for fixtures and equipment, and five years for floor coverings. For properties acquired in 2002 and later years, we performed detailed analyses of components of the real estate assets acquired. For these properties, we assigned estimated useful lives as follows: base building structure,

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40-60 years; land improvements, 5-20 years; short-lived building components, 5-20 years; and fixtures, equipment and floor coverings, 5-10 years.

We generally complete and capitalize acquisition improvements (expenditures that have been identified at the time the property is acquired and which are intended to position the property consistent with our physical standards) within one to two years of acquisition of the related apartment property. We capitalize non-recurring expenditures for additions and betterments to buildings and land improvements. In addition, we generally capitalize recurring capital expenditures for exterior painting, roofing, and other major maintenance projects that substantially extend the useful life of existing assets. For financial reporting purposes, we depreciate these additions and replacements on a straight-line basis over estimated useful lives of 5-20 years. We capitalize all floor covering, appliance and HVAC replacements, and depreciate them using a straight-line, group method over estimated useful lives of 5-10 years. We retire replaced assets with a charge to depreciation for any remaining carrying value. We expense ordinary repairs and maintenance costs at apartment communities. Costs of repairs and maintenance and capital improvements at restaurant properties are borne by the lessee.

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We evaluate our real estate assets upon occurrence of significant adverse changes in operations, to assess whether any impairment indicators are present that affect the recovery of the recorded values. If we considered any real estate assets to be impaired, we would record a loss to reduce the carrying value of the property to its estimated fair value. At December 31, 2005 and 2004, none of our assets were considered impaired.

### Cash and cash equivalents

We consider all highly liquid investments with maturities of three months or less when purchased to be cash equivalents.

### Deferred costs and intangible assets

We defer financing costs and amortize them using the straight-line method over the terms of the related notes. If we pay down or retire notes prior to their maturity, we write off the related unamortized financing costs, reflected as a charge to operations. Accumulated amortization on these assets totaled \$1.0 million at December 31, 2005, and \$1.2 million at December 31, 2004.

As of December 31, 2005, we estimate future amortization of deferred financing costs will be as follows (in thousands):

|      |        |            |        |
|------|--------|------------|--------|
| 2006 | \$ 482 | 2009       | \$ 246 |
| 2007 | 461    | 2010       | 222    |
| 2008 | 344    | Thereafter | 625    |

Goodwill and intangible assets deemed to have indefinite lives are no longer amortized after December 31, 2001, but are subject to annual impairment tests. We perform these annual tests as of October 1 of each year. Based on our tests through October 1, 2005, we determined that the intangible related to our 1994 acquisition of management operations, net of accumulated amortization, is not impaired. The historical cost of this intangible asset is \$3.7 million, with accumulated amortization of \$2.6 million.

In conjunction with the acquisition of an apartment community, we estimate the fair value of at-market, in-place leases. We record these amounts as intangible assets and amortize them over the remaining lease terms with a charge to apartment rental income. In general, the average remaining life of in-place leases at acquisition dates in 2005 ranged from five to nine months, and intangible assets represented approximately 0.3% of contract prices. At December 31, 2005, the historical cost of these intangible assets is \$0.3 million, with accumulated amortization of \$0.2 million.

We defer costs incurred in connection with proposed investing and financing transactions until the proposed transactions are consummated. We include such costs in prepaid expenses and other assets on

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our balance sheet. If we determine that a proposed transaction is not probable, we charge these costs to expense.

### Fair values of financial instruments

The carrying amount reported on the balance sheet for cash and cash equivalents approximates fair value.

We estimate the fair value of fixed-rate notes and variable-rate notes payable using discounted cash flow analysis, based on our current incremental borrowing rates for similar types of borrowing arrangements. The aggregate fair value of our deed of trust and other notes payable was approximately \$437 million at December 31, 2005, and \$296 million at December 31, 2004.

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### Use of estimates

We are required to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes in order to prepare them in accordance with accounting principles generally accepted in the United States. Depreciation amounts included in these financial statements reflect our estimate of the life and related depreciation rates for rental properties. In addition, the carrying amount of the intangible asset related to acquisition of management operations reflects our assessment of the continuing value of this asset. Actual results could differ from these significant estimates.

### Revenue recognition, deferred revenue and security deposits

We record rental and other revenue as it is earned, net of our provision for estimated uncollectible revenues. We amortize any cash concessions given at the inception of an apartment lease over the approximate life of the lease, which is generally one year or less. We record rental payments received prior to the first of a given month as prepaid rent.

We hold tenant security deposits in trust in bank accounts separate from operating cash; related trust account balances are included in the balance sheet in other current assets.

In December 2000, we received an \$800,000 advance payment under a contract for use of our cable equipment at five apartment communities. This receipt, net of \$20,000 of related costs, was recorded as deferred revenue, and we are recognizing this rental revenue over the ten-year contract term beginning in 2001.

Deferred revenue and security deposits include the following amounts:

|  |    | December 31 |
|--|----|-------------|
|  |    | 2005        |
|  |    | -----       |
|  |    | (000's)     |
| Liability for tenant security deposits                               | \$ | 987         |
| Prepaid apartment rents  |    | 583         |
| Deferred cable revenue   |    | 380         |
| Prepaid restaurant rents   |    | -           |
| Insurance proceeds held pending reconstruction of apartment building |    | -           |
|  |    | -----       |
|  | \$ | 1,950       |
|  |    | =====       |

### Advertising costs

We expense advertising costs as they are incurred. Advertising expense totaled \$758,000 in 2005, \$530,000 in 2004, and \$500,000 in 2003.

### Earnings per share

We calculate earnings per share based on the weighted average number of shares outstanding during each year.

### Comprehensive income

Comprehensive income is defined as changes in shareholders' equity exclusive of transactions with owners (such as capital contributions and dividends). We did not have any comprehensive income items in 2005, 2004, or 2003, other than net income as reported.

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### Stock-based compensation

The company has one employee Stock Option and Incentive Plan in place, which is described more fully in Note 7.

Prior to July 1, 2005, as allowed by FASB Statement 148, "Accounting for Stock-Based Compensation - Transition and Disclosure," and FASB Statement 123, "Accounting for Stock-Based Compensation," we accounted for this plan using the intrinsic value method; no stock-based employee compensation cost was reflected in net income, as all options granted under this plan had an exercise price equal to the market value of the underlying common stock on the date of grant. All outstanding options were fully vested prior to the end of 2004. If we had applied the fair value recognition provisions of Statement 123 to stock-based employee compensation, the effect would have been to reduce net income as reported by \$200 in 2004, with no impact on net income as reported in 2005 or on basic and diluted earnings per share amounts as reported.

In December 2004 the FASB issued Statement No. 123 (revised 2004), "Share Based Payment," ("FAS 123(R)") which is a revision of Statement 123, and requires all share-based payments to employees, including grants of employee stock options, to be recognized in the statement of operations based on their fair values. Effective July 1, 2005, we adopted the fair value recognition provisions of FAS 123(R) using the modified-prospective transition method. Under this transition method, compensation cost recognized in the second half of 2005 includes compensation cost for all share-based payments granted subsequent to July 1, 2005, based on the grant-date fair value estimated in accordance with the provisions of FAS 123(R).

In August 2005, the Board of Directors granted and the company issued 200,000 restricted nonvested shares of the company's common stock to four of our executive officers. During 2005, we recorded \$143,000 in service cost related to nonvested common stock.

### Note 2. Consolidated limited partnerships

Effective January 26, 2005, we acquired Boddie Investment Company ("BIC") in exchange for shares of our common stock. As a result of this acquisition, in addition to other assets, we acquired certain economic interests in the following limited partnerships:

- o Marina Shores Associates One, Limited Partnership - 50% interest as general partner
- o The Villages of Chapel Hill Limited Partnership - 1% interest as general partner
- o The Villages of Chapel Hill - Phase 5 Limited Partnership - 1% interest as general partner

Prior to this acquisition, we managed, on a fee basis, the properties owned by these limited partnerships. Following our acquisition of BIC, a wholly owned subsidiary of the operating partnership acts as the managing general partner of these limited partnerships and continues to manage the properties. These limited partnerships are primarily funded with financing from third party lenders, which is secured by first deed of trust loans on the rental properties of the partnerships. The creditors of the limited partnerships generally do not have recourse to the operating partnership.

We determined that The Villages of Chapel Hill Limited Partnership ("Villages Partnership") is a VIE because the limited partnership does not have sufficient equity to carry out its principal activities without additional subordinated financial support from the general partner. We also determined that we are the

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primary beneficiary of the Villages Partnership. Our initial net investment in this general partnership

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interest was \$2,000. We included the accounts of this partnership in our consolidated financial statements effective January 26, 2005, by recording all of the Villages Partnership assets, liabilities and noncontrolling interests at fair value. In our initial consolidation of the Villages Partnership, we recorded the noncontrolling limited partners' capital accounts at \$350,000.

We determined that the Marina Shores Associates One, Limited Partnership ("Marina Shores Partnership") and The Villages of Chapel Hill - Phase 5 Limited Partnership ("Villages - Phase 5 Partnership") are not VIEs. However, under the terms of the partnership agreements for these partnerships, the general partner controls the activities of the partnership. Our initial investments in these general partnership interests were \$5.9 million for the Marina Shores Partnership interest and \$7,000 for the Villages - Phase 5 Partnership interest. We included the accounts of these partnerships in our consolidated financial statements effective January 26, 2005, by recording our prorata interest in the partnerships' assets and liabilities at the lower of our cost or fair value, including the noncontrolling interests in the partnerships' assets and liabilities at their historical costs, and by resetting the noncontrolling limited partners' capital accounts (which were previously in deficit balances) to \$-0-.

The initial inclusion of these partnerships in our consolidated financial statements resulted in increases to our balance sheet amounts as follows:

|                                | Real estate<br>investments | Net operating<br>assets | Deed<br>note |
|--------------------------------|----------------------------|-------------------------|--------------|
|                                | (000's)                    | (000's)                 | (            |
| Marina Shores Partnership      | \$ 26,254                  | \$ 950                  | \$           |
| Villages Partnership           | 14,188                     | 145                     |              |
| Villages - Phase 5 Partnership | 2,596                      | 239                     |              |
|                                | \$ 43,039                  | \$ 1,334                | \$           |
|                                | \$ 43,039                  | \$ 1,334                | \$           |

In addition, in consolidation we eliminated approximately \$1.9 million in notes and other receivables from The Villages Partnership that we acquired in the transaction with BIC.

We reflect the unaffiliated partners' interests in the Marina Shores Partnership, the Villages Partnership and the Villages - Phase 5 Partnership as minority interest in consolidated limited partnerships. Minority interest in consolidated limited partnerships represents the minority partners' share of the underlying net assets of these consolidated limited partnerships. When these consolidated limited partnerships make cash distributions to partners in excess of the positive carrying amounts of their minority interests, we record a charge equal to the amount of such excess distributions to minority partners. These charges decrease our net income (or increase our net loss); however, the cash outlay is, in fact, made by the consolidated limited partnership, and there is no cost to the operating partnership. During 2005, we recorded charges for deficit distributions to the minority partner in the Marina Shores Partnership totaling \$7.9 million.



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We allocate proportional income and losses of the consolidated limited partnerships, measured on a year-to-date basis, to minority partners. However, we may allocate losses to a minority partner only to the extent of the positive carrying amount of the interest of that minority partner. When losses attributable to the minority limited partners of a consolidated limited partnership exceed the carrying amount of the minority interest, we record a charge, even though there is no cash outlay by the operating partnership. During 2005, we recorded charges for consolidated limited partnership losses, resulting primarily from depreciation, along with costs related to refinance of the Marina Shores Partnership's first deed of trust loan, as follows (in thousands):

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|                                |    |       |
|--------------------------------|----|-------|
| Marina Shores Partnership      | \$ | 99    |
| Villages Partnership*          |    | 10    |
| Villages - Phase 5 Partnership |    | 17    |
|                                |    | ----- |
|                                | \$ | 126   |
|                                |    | ===== |

\*After charges for net losses of \$350,000 to reduce minority limited partners' capital accounts to \$-0-.

### Note 3. Discontinued operations

In October 2005, we sold Savannah Shores Apartments for a contract price of \$22.75 million to an unaffiliated third party. Net proceeds of the sale were \$22.2 million, and we recorded a gain on the sale of real estate assets of \$8.1 million.

We acquired Savannah Shores Apartments in July 2004 for an initial purchase price of \$12.5 million, paid through issuance of operating partnership units with total imputed value of \$0.1 million, assumption of \$12.2 million in debt obligations, and assumption of \$0.2 million net operating liabilities. The acquisition agreement provided for potential earn-out of additional purchase consideration of up to \$1.7 million, which we paid through issuance of additional operating partnership units in October 2005.

We have presented the operations of this community as discontinued operations in our statements of operations for 2005 and 2004. Operating results of this community were as follows:

|   |    | 2005<br>(10 months) | (6<br>months) |
|---|----|---------------------|---------------|
|   |    | -----               | -----         |
|   |    | (000's)             |               |
| Apartment rental income                             | \$ | 1,493               |               |
| Apartment operations expense                        |    | (740)               |               |
| Interest  |    | (360)               |               |
| Depreciation  |    | (259)               |               |
| Amortization of deferred loan costs                 |    | (14)                |               |
| Write-off of deferred loan costs at debt retirement |    | (33)                |               |
|   |    | -----               | -----         |
|   | \$ | 88                  |               |
|   |    | =====               | =====         |

### Note 4. Real estate investments

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Real estate investments consist of the following:

|  |    | December 31<br>2005 |
|--|----|---------------------|
|  |    | -----<br>(000's)    |
| Apartment properties - owned                             |    |                     |
| Land   | \$ | 59,089              |
| Buildings and improvements                               |    | 449,274             |
| Computer and support equipment                           |    | 1,416               |
| Less accumulated depreciation                            |    | (67,341)            |
|  |    | -----<br>442,437    |
| Apartment properties - consolidated limited partnerships |    |                     |
| Land   |    | 3,214               |
| Buildings and improvements                               |    | 46,567              |
| Less accumulated depreciation                            |    | (7,712)             |
|  |    | -----<br>42,069     |

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|                               |  | December 31<br>2005 |
|-------------------------------|--|---------------------|
|                               |  | -----<br>(000's)    |
| Restaurant properties         |  |                     |
| Land                          |  | 10,445              |
| Buildings and improvements    |  | 26,961              |
| Less accumulated depreciation |  | (12,615)            |
|                               |  | -----<br>24,791     |
|                               |  | -----<br>\$ 509,297 |
|                               |  | =====               |

For federal and state income tax purposes, we will report real estate investments with a total cost basis of \$512 million and accumulated depreciation of \$112 million as of December 31, 2005.

During the three years ended December 31, 2005, we acquired the apartment communities listed below. The results of operations of these apartment communities are included in the financial statements from the dates of acquisition.

2005 acquisitions:

- o Timbers Apartments, acquired October 2005, for a total cost of \$22.5 million, paid in cash.

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- o Hamptons Apartments, acquired October 2005, for a total cost of \$17.5 million, paid in cash.
- o Paces Watch Apartments, acquired May 2005, for a total cost of \$20.5 million, paid in cash.
- o Waverly Place Apartments, acquired April 2005, for a total cost of \$13.2 million, paid in cash.
- o Portfolio of four apartment communities (Canterbury Apartments, Laurel Springs Apartments, Laurel Springs II Apartments, and Salem Ridge Apartments), acquired March 2005, for an aggregate purchase price of \$52.1 million (including \$0.3 million in net operating assets acquired), paid by assumption or refinancing of \$42.8 million in debt obligations and issuance of operating partnership units with an imputed value of \$9.3 million. Under the terms of the exchange agreements, we issued 689,000 operating partnership units at closing, and we will issue an additional 74,000 units in March 2006. We operate Laurel Springs and Laurel Springs II Apartments as one community.

### 2004 acquisitions:

- o Bridges at Southpoint Apartments, acquired September 2004, for a total cost of \$10.2 million, paid in cash.
- o Savannah Shores Apartments, acquired July 2004 - see discussion at Note 3.
- o The Fairington Apartments, acquired August 2004, for a total cost of \$18.6 million, paid in cash.
- o Carriage Club Apartments, acquired June 2004, for a total cost of \$19.7 million, paid in cash.
- o Bridges at Wind River Apartments, acquired May 2004, for a total cost of \$25.1 million (including \$0.2 million in net operating assets acquired), including assumption of \$24.6 million in debt obligations and issuance of 42,000 operating partnership units with an imputed value of \$0.5 million.

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### 2003 acquisitions:

- o The Harrington Apartments, acquired August 2003, for a total cost of \$17.9 million, paid in cash.
- o The Place Apartments, acquired March 2003, for a total cost of \$5.6 million, paid in cash.

We present the following unaudited pro forma summary information as if we had owned the properties acquired in 2005 and 2004 throughout all of both years. These pro forma amounts may not represent how we would have performed if these acquisitions had really occurred prior to 2004. In addition, they do not purport to project our results of operations for any future period.

2005

2004

-----

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(000's) (000's)

|  |          |          |
|--|----------|----------|
| Total revenue                          | \$79,197 | \$75,723 |
| (Loss) income from                     |          |          |
| - Continuing operations                | (8,456)  | (586)    |
| - Discontinued operations              | 6,482    | 72       |
| Net loss                               | (1,974)  | (514)    |
| Loss attributed to common shareholders | (2,807)  | (1,514)  |
|  |          |          |
| Basic and diluted earnings per share:  |          |          |
| (Loss) income from                     |          |          |
| - Continuing operations                | \$(0.91) | \$(0.07) |
| - Discontinued operations              | 0.70     | 0.01     |
| Net loss                               | (0.21)   | (0.06)   |
| Loss attributed to common shareholders | (0.30)   | (0.19)   |

During 2003, we sold two restaurant properties to the lessee for their net carrying values, totaling \$1.2 million. We applied the proceeds from these sales to improvements at apartment communities and to reduce our line of credit secured by the restaurant properties.

### Note 5. Notes Payable

Notes payable consist of the following:

| December 31 |         |
|-------------|---------|
| 2005        | 2004    |
| -----       | -----   |
| (000's)     | (000's) |

#### Owned properties - Lines of credit with a bank:

Principal sum of up to \$14.6 million through January 2007, then \$13.8 million, due January 2008 (as modified June 2005), secured by deeds of trust and assignments of rents of 40 restaurant properties. Interest-only payments on the outstanding balance due monthly at a variable interest rate of 30-day LIBOR plus 1.80% (6.27% at December 31, 2005).

|           |           |
|-----------|-----------|
| \$ 14,650 | \$ 16,316 |
|-----------|-----------|

Revolving line of credit for principal sum of up to \$40.0 million, due January 2009 (as modified November 2005), secured by a deed of trust and assignment of rents of Latitudes Apartments. Interest-only payments on the outstanding balance due monthly at a

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| December 31 |         |
|-------------|---------|
| 2005        | 2004    |
| -----       | -----   |
| (000's)     | (000's) |

variable interest rate of 30-day LIBOR plus 1.65 % (6.12% at December 31, 2005).

|     |        |
|-----|--------|
| -0- | 10,166 |
|-----|--------|

#### Owned properties - Variable rate notes payable:

Notes payable to banks, assumed in conjunction with 2005 acquisitions of one

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apartment community and a parcel of land adjacent to another community. Payments of \$7,000 principal plus interest due monthly at interest rates of 30-day LIBOR plus 1.90% and 1.98% (6.45% at December 31, 2005).

Maturities in 2006 with balloon payments totaling \$7.9 million.

7,923 -

Note payable to a bank in the principal amount of \$10.5 million (as modified December 2004), secured by a deed of trust and assignment of rents of an apartment community. Payable in monthly installments of \$56,000 including principal and interest at 30-day LIBOR plus 1.85% (6.32% at December 31, 2005). Maturity in December 2007, with an estimated balloon payment of \$8.0 million.

8,294 10,453

Note payable to a bank, secured by a deed of trust and assignment of rents of an apartment community, with available balance up to \$13.0 million. Interest-only payments due monthly at 30-day LIBOR plus 1.65% (6.12% at December 31, 2005), with maturity in November 2008.

9,392 -

Note payable to a bank, secured by a deed of trust and assignment of rents of one apartment property. (Two additional notes payable were outstanding at December 31, 2004, and were retired in 2005.)

Interest-only payments on the outstanding principal balance due monthly at an interest rate of 30-day LIBOR plus 1.75% (6.22% at December 31, 2005); beginning September 2007, monthly payments of principal estimated at \$25,000 plus interest. Maturity in August 2009, with an estimated balloon payment of \$12.9 million.

13,400 33,900

Owned properties - Fixed rate notes payable:

Notes payable comprised of 21 loans (11 loans in 2004), payable in monthly installments totaling \$1,564,000 including principal and interest at rates ranging from 4.98% to 7.09% with maturities in 2009 through 2016. Secured by deeds of trust and assignments of rents of apartment communities.

278,461 131,225

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| December 31 |         |
|-------------|---------|
| 2005        | 2004    |
| -----       | -----   |
| (000's)     | (000's) |

Notes payable comprised of 7 loans (10 loans in 2004), interest rates ranging from 5.53% to 6.76%, payable in interest-only monthly installments totaling \$296,000, with maturities totaling \$39.1 million in 2008 and \$17.3 million in 2015. Secured by deeds of

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|  |         |         |
|--|---------|---------|
| trust and assignments of rents of apartment communities. | 56,455  | 84,366  |
|  | -----   | -----   |
|  | 388,576 | 286,425 |

Consolidated limited partnerships - Fixed rate notes payable:

|   |           |           |
|---|-----------|-----------|
| Notes payable comprised of three loans, payable in monthly installments totaling \$279,000 including principal and interest at rates ranging from 5.15% to 7.39% with maturities totaling \$12.7 million in 2011 and \$28.0 million in 2015. Secured by deeds of trust and assignments of rents of apartment communities. The carrying amount at December 31, 2005, includes \$1.0 million premium recorded in consolidation to reduce the effective interest rates of above-market loans from 7.39% to approximately 5.3%. | 48,136    | -         |
|   | -----     | -----     |
|   | \$436,712 | \$286,425 |
|   | =====     | =====     |

During the three years ended December 31, 2005, we executed or assumed the following notes payable in conjunction with acquisitions of apartment communities:

- o \$17.3 million fixed-rate note payable, October 2005, secured by a deed of trust and assignment of rents of Timbers Apartments. This loan provides for interest at 5.45% (5.53% effective rate), payable in interest-only monthly installments of \$80,000, with a balloon payment of \$17.3 million at maturity in November 2015. We paid and recorded deferred loan costs of \$120,000 related to this loan.
  
- o \$13.0 million variable-rate note payable, initial draw of \$9.4 million October 2005, secured by a deed of trust and assignment of rents of Hamptons Apartments. This loan provides for interest at 30-day LIBOR plus 1.65%, payable monthly, with principal due November 2008. We paid and recorded deferred loan costs of \$78,000 related to this loan.
  
- o \$14.9 million fixed-rate note payable, May 2005, secured by a mortgage and assignment of rents of Paces Watch Apartments. This loan provides for interest at 5.31% (5.38% effective rate), with interest-only payments of \$67,000 through June 2008. Beginning July 2008, scheduled monthly installments of principal and interest will be \$83,000, with a balloon payment of \$13.3 million at maturity in June 2015. We paid and recorded deferred loan costs of \$90,000 related to this loan.
  
- o \$10.2 million fixed-rate note payable, April 2005, secured by a mortgage and assignment of rents of Waverly Place Apartments. This loan provides for interest at 5.31% (5.38% effective rate), with interest-only monthly payments of \$46,000 through May 2008. Beginning June 2008, scheduled monthly installments of principal and interest will be \$56,000 with a balloon payment of \$9.1 million at maturity in June 2015. We paid and recorded deferred loan costs of \$66,000 related to this loan.
  
- o \$21.5 million balance, fixed-rate note payable assumed March 2005, secured by a mortgage and assignment of rents of Canterbury Apartments. This loan provides for interest at 5.40% (5.48% effective rate), payable in monthly installments of principal and interest of \$124,000 through July 2013, with a balloon payment of \$18.4 million at maturity in August 2013. We paid and

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recorded

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deferred loan costs of \$26,000 related to this loan.

- o \$1.5 million variable-rate unsecured note related to Canterbury Apartments, assumed March 2005 and immediately retired.
- o \$11.3 million balance, fixed-rate note payable assumed March 2005, secured by a deed of trust and assignment of rents of Laurel Springs Apartments. This loan provides for interest at 4.91% (4.98% effective rate), payable in monthly installments of principal and interest of \$62,000 through June 2013, with a balloon payment of \$9.6 million at maturity in July 2013. We paid and recorded deferred loan costs of \$28,000 related to this loan.
- o \$5.9 million variable-rate note payable assumed March 2005, secured by a deed of trust and assignment of rents of Laurel Springs II Apartments. This loan provides for interest at 30-day LIBOR plus 1.90%, payable monthly. Beginning July 2005, principal payments of \$7,000 are due monthly in addition to interest, with a balloon payment of \$5.8 million at maturity in June 2006. At our option, we may extend the loan maturity to June 2008. We paid and recorded deferred loan costs of \$2,000 related to this loan.
- o \$2.6 million fixed-rate note payable assumed March 2005, secured by a deed of trust and assignment of rents of Salem Ridge Apartments. This loan provides for interest at 6.76%, with interest-only monthly payments of \$15,000, and principal due September 2008. We paid and recorded deferred loan costs of \$12,000 related to this loan.
- o \$8.2 million fixed-rate note payable, September 2004, secured by a deed of trust and assignment of rents of Bridges at Southpoint Apartments. This loan provides for interest at 4.93% (5.00% effective rate), payable in monthly installments of \$34,000 through October 2007, then principal and interest payable in monthly installments of \$44,000 through September 2014, with a balloon payment of \$7.3 million at maturity in October 2014. We paid and recorded deferred loan costs of \$61,000 related to this loan.
- o \$13.4 million variable-rate note payable, August 2004, secured by a deed of trust and assignment of rents of Fairington Apartments. This loan provides for interest at 30-day LIBOR plus 1.75%, payable monthly, with principal due August 2007, subject to an optional 24-month extension. If the loan is extended, principal payments of \$31,000 will be payable monthly beginning September 2007, with the remaining principal balance of \$12.7 million due August 2009. We paid and recorded deferred loan costs of \$76,000 related to this loan.
- o \$9.0 million variable-rate note payable, July 2004, secured by a deed of trust and assignment of rents of Savannah Shores Apartments. We subsequently retired this loan in conjunction with the sale of Savannah Shores Apartments in October 2005. We paid and recorded deferred loan costs of \$56,000 related to this loan in 2004; we wrote off unamortized loan costs of \$33,000 related to this loan in 2005. .
- o \$14.9 million fixed-rate note payable, June 2004, secured by a deed of trust and assignment of rents of Carriage Club Apartments. This loan provides for interest at 5.15% (5.22% effective rate), payable in monthly installments of \$65,000 through July 2005, then principal and interest payable in monthly installments of \$81,000 through June 2009, with a balloon payment of \$14.0 million at maturity in July 2009. We paid and recorded deferred loan costs of \$90,000 related to this loan.

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- o \$19.7 million fixed-rate note payable, May 2004, secured by a deed of trust and assignment of rents of Bridges at Wind River Apartments. This loan provides for interest at 5.57% (5.65% effective rate) and monthly payments of principal and interest of \$113,000, with a balloon payment of \$16.5 million at maturity in June 2014, subject to an optional extension for one year with interest at a variable rate. We applied the proceeds of this note, along with additional funds drawn on our revolving line of

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credit, to retire the existing \$24.6 million loan obligations related to Bridges at Wind River. We paid and recorded deferred loan costs of \$157,000 related to this loan.

- o \$14.4 million variable-rate note payable, August 2003, secured by a deed of trust and assignment of rents of Mallard Creek Phase 2 Apartments (formerly Harrington Apartments). This loan provided for interest at 30-day LIBOR plus 1.75%, payable monthly. We subsequently retired this loan in July 2004 (see refinancing transactions below).
- o \$4.6 million fixed-rate note payable, March 2003, secured by a deed of trust and assignment of rents of Bridges at Pelham Apartments (formerly The Place Apartments). This loan provides for interest at 5.06% (5.13% effective rate) and monthly payments including principal and interest of \$25,000, with a balloon payment of \$3.8 million at maturity in March 2013. We paid and recorded deferred loan costs of \$63,000 related to this loan.

During this three-year period, we executed the following notes payable in refinancing transactions:

- o \$5.7 million fixed-rate note payable, December 2005, secured by a deed of trust and assignment of rents of Pepperstone Apartments. This loan provides for interest at 5.58% (5.66% effective rate), with interest-only monthly payments of \$27,000 through January 2012. Beginning February 2012, scheduled monthly installments of principal and interest will be \$33,000, with a balloon payment of \$5.4 million at maturity in January 2016. We applied the proceeds to retire an existing 6.97% fixed-rate note payable with a balance of \$3.9 million, along with \$133,000 in prepayment penalties, and reduce the outstanding balance of our line of credit secured by Latitudes Apartments. Through December 31, 2005, we paid and recorded deferred loan costs of \$25,000 related to this loan. In addition, we wrote off unamortized loan costs of \$9,000 related to the debt retired.
- o \$20.3 million fixed-rate note payable, December 2005, secured by a deed of trust and assignment of rents of Waterford Place Apartments. This loan provides for interest at 5.58% (5.66% effective rate), with interest-only monthly payments of \$96,000 through January 2012. Beginning February 2012, scheduled monthly installments of principal and interest will be \$116,000, with a balloon payment of \$19.2 million at maturity in January 2016. We applied the proceeds to retire an existing 6.97% fixed-rate note payable with a balance of \$11.1 million, along with \$379,000 in prepayment penalties, and reduce the outstanding balance of our line of credit secured by Latitudes Apartments. Through December 31, 2005, we paid and recorded deferred loan costs of \$32,000 related to this loan. In addition, we wrote off unamortized loan costs of \$20,000 related to the debt retired.
- o \$23.7 million fixed-rate note payable, December 2005, secured by a deed of trust and assignment of rents of Abbington Place Apartments. This loan provides for interest at 5.50% (5.57% effective rate), with interest-only



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monthly payments of \$110,000 through January 2013. Beginning February 2013, scheduled monthly installments of principal and interest will be \$135,000, with a balloon payment of \$22.8 million at maturity in January 2016. We applied the proceeds to retire an existing 6.97% fixed-rate note payable with a balance of \$15.8 million, along with \$539,000 in prepayment penalties, and reduce the outstanding balance of our line of credit secured by the Latitudes Apartments. Through December 31, 2005, we paid and recorded deferred loan costs of \$48,000 related to this loan. In addition, we wrote off unamortized loan costs of \$28,000 related to the debt retired.

- o \$10.2 million fixed-rate note payable, December 2005, secured by a deed of trust and assignment of rents of Savannah Place Apartments. This loan provides for interest at 5.50% (5.57% effective rate), with interest-only monthly payments of \$47,000 through January 2013. Beginning February 2013, scheduled monthly installments of principal and interest will be \$58,000, with a balloon payment of \$9.8 million at maturity in January 2016. We applied the proceeds to retire an existing 6.97% fixed-rate note payable with a balance of \$7.3 million, along with \$250,000 in prepayment penalties, and reduce the outstanding balance of our line of credit secured by Latitudes Apartments. Through December 31, 2005, we paid and recorded deferred loan costs of \$41,000 related to this loan. In

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addition, we wrote off unamortized loan costs of \$14,000 related to the debt retired.

- o \$14.0 million fixed-rate note payable, December 2005, secured by a deed of trust and assignment of rents of Woods Edge Apartments. This loan provides for interest at 5.50% (5.57% effective rate), with interest-only monthly payments of \$65,000 through January 2013. Beginning February 2013, schedule monthly installments of principal and interest will be \$79,000, with a balloon payment of \$13.4 million at maturity in January 2016. We applied the proceeds to retire an existing 6.95% fixed-rate note payable with a balance of \$9.8 million, along with \$326,000 in prepayment penalties, and reduce the outstanding balance of our line of credit secured by Latitudes Apartments. Through December 31, 2005, we paid and recorded deferred loan costs of \$44,000 related to this loan.
- o \$15.5 million fixed-rate note payable, May 2005, secured by a deed of trust and assignment of rents of Chason Ridge Apartments. This loan provides for interest at 5.21% (5.28% effective rate), with interest-only monthly payments of \$68,000 through June 2008. Beginning July 2008, scheduled monthly installments of principal and interest will be \$85,000, with a balloon payment of \$13.9 million at maturity in June 2015. We applied the proceeds to retire an existing \$11.5 million variable-rate note payable and reduce the outstanding balance of our line of credit secured by Latitudes Apartments. We paid and recorded deferred loan costs of \$124,000 related to this loan. In addition, we wrote off unamortized loan costs of \$63,000 related to the debt retired.
- o \$7.1 million fixed-rate note payable, June 2005, secured by a deed of trust and assignment of rents of Mallard Creek Phase 1 Apartments (formerly Harris Hill Apartments). This loan provides for interest at 5.21% (5.28% effective rate), with interest-only monthly payments of \$31,000 through June 2008. Beginning July 2008, scheduled monthly installments of principal and interest will be \$39,000, with a balloon payment of \$6.4 million at maturity in June 2015. We applied the proceeds to retire an existing 8.55% fixed-rate note payable with a balance of \$5.5 million and reduce our line of credit secured by Latitudes Apartments. We paid and recorded deferred loan costs of \$76,000 related to this loan.

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- o \$33.9 million fixed-rate note payable, February 2005, secured by a deed of trust and assignment of rents of Marina Shores Apartments (in which we have a 50% interest through our general partner interest in the Marina Shores Partnership, which we include in our consolidated financial statements). This loan provides for interest at 5.08% (5.15% effective rate), payable in monthly installments of principal and interest of \$184,000, with a balloon payment of \$28.2 million in February 2015. The Marina Shores Partnership first applied proceeds of this loan to retire the existing \$20.7 million deed of trust loan balance along with \$1.2 million in interest and prepayment penalties, then distributed \$6.8 million to the minority limited partner and \$3.7 million to the operating partnership.
- o \$15.0 million fixed-rate note payable, July 2004, secured by a deed of trust and assignment of rents of Mallard Creek Phase 2 Apartments (formerly Harrington Apartments). This loan provides for interest at 5.15% (5.22% effective rate), payable in monthly installments of \$65,000 through August 2005, then principal and interest payable in monthly installments of \$82,000, with a balloon payment of \$14.1 million at maturity in August 2009. We applied the proceeds to retire a \$14.4 million variable-rate note payable. We paid and recorded deferred loan costs of \$92,000 related to this loan. In addition, we wrote off unamortized loan costs of \$85,000 related to the debt retired.
- o \$11.5 million variable-rate note payable, April 2004, secured by a deed of trust and assignment of rents of Chason Ridge Apartments. This loan provided for interest at 30-day LIBOR plus 1.75%, payable monthly. We subsequently retired this loan in May 2005 (discussed above).

In November 2005, we modified our revolving line of credit with a bank secured by Latitudes Apartments to increase our maximum loan amount to \$40.0 million and extend the term of the loan through January 2009 (previously November 2007). In conjunction with this modification we paid and recorded deferred loan costs of \$110,000. We also paid and recorded deferred loan costs of \$184,000 in 2004 and \$32,000

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in 2003 in conjunction with previous modifications. As of December 31, 2005, \$40.0 million was available for draw under our Latitudes line of credit.

In June 2005, we modified and extended our line of credit with a bank secured by our restaurant properties to extend the maturity date of this loan to January 2008 (previously January 2006). In conjunction with this modification, we paid and recorded deferred loan costs of \$21,000. We also paid and recorded deferred loan costs of \$41,000 in 2004 in conjunction with a previous modification.

Interest payments totaled \$23.4 million (including \$2.5 million paid by consolidated limited partnerships) in 2005, \$14.5 million in 2004, and \$13.2 million in 2003.

The loan agreements related to the lines of credit include covenants and restrictions relating to, among other things, specified levels of debt service coverage, leverage and net worth. To date, we have met all applicable requirements.

As of December 31, 2005, we estimate future scheduled principal payments will be as follows (in thousands):

|      |           |      |           |
|------|-----------|------|-----------|
| 2006 | \$ 10,978 | 2009 | \$ 45,235 |
| 2007 | 11,338    | 2010 | 21,884    |

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2008                      67,122                      Thereafter                      280,155

### Note 6. Shareholders' equity

#### Authorized capital stock

Our bylaws and certificate of incorporation allow the Board of Directors to authorize the issuance of up to 100 million shares of common stock and 10 million shares of preferred stock, issuable in series whose characteristics would be set by the Board of Directors.

Approximately 4.3 million authorized shares of common stock are reserved for future issuance under the company's Stock Option and Incentive Plan, Dividend Reinvestment and Stock Purchase Plan, and for conversion of Operating Partnership units.

#### Issue of common stock for acquisition of BIC

In conjunction with the January 2005 acquisition by merger of BIC, we issued 509,000 shares of our common stock valued at \$8.2 million, and cancelled 72,000 shares of common stock that BIC held immediately before the merger.

#### Conversion of preferred shares to common shares

We issued 909,000 shares of the Company's Series B Cumulative Convertible Preferred stock with total liquidation value of \$10.0 million to a single accredited investor during 2001 through 2003, for total net proceeds of \$9.6 million. We redeemed these preferred shares in November 2005 on a one-for-one basis through issuance of 909,000 shares of our common stock.

#### Dividend Reinvestment and Stock Purchase Plan

Our Dividend Reinvestment and Stock Purchase Plan ("DRIP Plan") allows the company, at its option, to issue shares directly to Plan participants. We issued 52,000 shares in 2005, 66,000 shares in 2004, and 73,000 shares in 2003 through the Plan.

#### Redemption of operating partnership units

We redeemed operating partnership units from former minority unitholders by issuing shares of the company's common stock on a one-for-one basis in the following amounts: 78,000 shares in 2005, 25,000 shares in 2004, and 3,000 shares in 2003.

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### Earnings per common share

We calculated basic and diluted earnings per share using the following amounts:

|   | 2005       | 2004    |    |
|---|------------|---------|----|
|   | (000's)    | (000's) |    |
| <b>Numerators:</b>                              |            |         |    |
| Numerator for basic earnings per share -        |            |         |    |
| (Loss) income from                              |            |         |    |
| - Continuing operations                         | \$ (8,052) | \$ 962  | \$ |
| - Discontinued operations                       | 6,563      | 77      |    |
| Net (loss) income                               | (1,488)    | 1,039   | \$ |
| Cumulative preferred dividend                   | (833)      | (1,000) |    |
| (Loss) income attributed to common shareholders | \$ (2,322) | \$ 39   | \$ |

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|   |            |          |    |
|---|------------|----------|----|
| Numerator for diluted earnings per share (1) -                  |            |          |    |
| (Loss) income from  |            |          |    |
| - Continuing operations   | \$ (8,052) | \$ 960   | \$ |
| - Discontinued operations                                       | 6,563      | 95       |    |
|   |            |          |    |
| Net (loss) income   | (1,488)    | \$ 1,055 | \$ |
| Cumulative preferred dividend                                   | (833)      | (1,000)  |    |
|   |            |          |    |
| (Loss) income attributed to common shareholders                 | \$ (2,322) | \$ 55    | \$ |
|   |            |          |    |
| Denominators:   |            |          |    |
| Denominator for basic earnings per share -                      |            |          |    |
| Weighted average common shares outstanding                      | 9,389      | 7,617    |    |
| Less weighted average nonvested common shares outstanding       | (84)       | -        |    |
|   |            |          |    |
| Weighted average common shares - basic                          | 9,305      | 7,617    |    |
| Effect of dilutive securities:                                  |            |          |    |
| Convertible operating partnership units (1)                     | -          | 1,856    |    |
| Weighted average nonvested common shares (2)                    | -          | -        |    |
| Stock options (3)   | -          | 31       |    |
|   |            |          |    |
| Dilutive potential common stock                                 | -          | 1,887    |    |
|   |            |          |    |
| Denominator for diluted earnings per share -                    |            |          |    |
| Adjusted weighted average common shares and assumed conversions | 9,305      | 9,504    |    |
|   |            |          |    |

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### Note 7. Stock-based compensation

The company has one employee Stock Option and Incentive Plan in place. The plan, as amended May 2005, provides for issuance of up to 1,260,000 shares, with a 630,000-share limit on restricted stock, phantom stock and other full-value stock-based awards combined. At December 31, 2005, we have reserved 903,000 shares of common stock for issuance under this plan.

#### Nonvested common stock

Effective August 1, 2005, the Board of Directors granted and the company issued 200,000 restricted shares of the company's common stock to four of our executive officers. All of the shares were nonvested at the date of grant, and will vest 10% per year beginning on July 1, 2006, and on each July 1 thereafter until fully vested. Once vested, the shares will be fully transferable without restriction. All shares carry dividend and voting rights.

Because grantees fully participate in dividends, the fair value of the nonvested shares is equal to the market value at the grant date, \$15.70 per share, or a total of \$3,140,000. Because the grantee group is limited to four key executives, we estimate that 100% of these shares will vest. We will recognize the cost of these awards on a straight-line basis for each annual vesting period ending June 30 through 2015.

During 2005, we recorded \$143,000 in service cost related to nonvested common stock, included in corporate administration expense in our statement of operations and as an increase to additional paid-in capital. As of December 31, 2005, unrecognized service cost related to nonvested common stock totaled \$3.0

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million.

### Options

Options have been granted to employees at prices equal to the fair market value of the stock on the dates the options were granted or repriced. We calculated the fair value of each option grant on the date of grant using the Black-Scholes option-pricing model. Options are generally exercisable in four annual installments beginning one year after the date of grant, and expire ten years after the date of grant.

The following table summarizes information about stock options outstanding at December 31, 2005.

|                                   | Weighted Average<br>Remaining<br>Contractual<br>Life (Years) | Number of<br>Options<br>Outstanding | Nu<br>O<br>Exe |
|-----------------------------------|--|-------------------------------------|----------------|
|                                   |  |                                     |                |
| Exercise price \$9.25 per share   | 4.15   | 30,000                              |                |
| Exercise price \$11.25 per share  | 2.83   | 60,000                              |                |
| Exercise price \$13.125 per share | 2.50   | 120,000                             |                |
| Exercise price \$12.25 per share  | 1.33   | 60,000                              |                |
| All options outstanding           | 2.50   | 270,000                             |                |

There were no grants of options during 2005, 2004, or 2003. As of December 31, 2005, all outstanding options were fully vested. Changes in outstanding stock options were as follows:

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|                                       | 2005     |  | 2004     |  | 2003    |
|---------------------------------------|----------|--|----------|--|---------|
|                                       | Shares   | Weighted<br>Average<br>Exercise<br>Price | Shares   | Weighted<br>Average<br>Exercise<br>Price | Shares  |
| Beginning balance                     | 327,500  | \$12.04                                  | 477,500  | \$12.12                                  | 477,500 |
| Granted                               | -        | -  | -        | -  | -       |
| Exercised                             | (57,500) | 11.86                                    | (99,844) | 12.50                                    | -       |
| Repurchased                           | -        | -  | -        | -  | -       |
| Forfeited                             | -        | -  | (50,156) | 11.85                                    | -       |
| Ending balance                        | 270,000  | \$12.08                                  | 327,500  | \$12.04                                  | 477,500 |
| Exercisable at the end of<br>the year | 270,000  | \$12.08                                  | 327,500  | \$12.04                                  | 465,625 |

During 2005, we issued 57,500 shares of our common stock upon exercise of

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options by two employees for cash proceeds totaling \$682,000. During 2004, we issued 99,844 shares of our common stock, net of 40,071 shares exchanged, upon exercise of options by three employees, for cash proceeds of \$700,000.

### Note 8. Rental operations

#### Apartment properties

We lease our residential apartments under operating leases with monthly payments due in advance. Terms of the apartment leases are generally one year or less, with none longer than two years.

#### Restaurant properties - master lease agreement

The lease agreement with Boddie-Noell Enterprises ("Enterprises") has a primary term expiring in December 2007, but grants Enterprises three five-year renewal options. Enterprises pays annual rent equal to the greater of the specified minimum rent or 9.875% of food sales from the restaurants. Under certain conditions as defined in the agreement, both Enterprises and the company have the right to substitute another restaurant property for a property covered by the lease. Assuming renewal of the lease, after December 31, 2007, Enterprises has the right to terminate the lease on up to five restaurant properties per year by offering to purchase them under specified terms.

In addition, we entered into a separate agreement with Enterprises that, after December 31, 1997, allowed Enterprises to purchase, under specified terms, up to seven restaurant properties deemed non-economic. During 2003 we sold two restaurants to Enterprises, the lessee, under this agreement. We sold five restaurants in previous years to Enterprises under this clause.

The lease requires Enterprises to pay monthly installments of minimum rent and quarterly payments calculated based on the percentage rent, subject to an annual calculation of the greater of minimum or percentage rent. We received the minimum rent in 2005, 2004, and 2003. We expect annual minimum rent will be \$3.8 million in years 2006 and 2007.

#### Casualty gains

During 2005, we recorded casualty gains totaling \$668,000 related to fires that resulted in substantial damages to one building each at two of our apartment communities. We received insurance proceeds totaling \$533,000 for a fire that occurred in April 2005, against which we identified and wrote off \$365,000 net carrying value of assets destroyed. We expect to receive insurance proceeds totaling approximately \$1.0 million in early 2006 for a fire that occurred in September 2005, against which we have tentatively identified and written off \$530,000 net carrying value of assets destroyed.

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During 2004, we recorded casualty gains totaling \$269,000 related to fires that resulted in substantial damage to one building each at two of our apartment communities. We received insurance proceeds totaling \$895,000, against which we identified and wrote off \$626,000 net carrying value of assets destroyed.

We are insured for these losses, including rent continuation insurance covering 100% of lost rental income. We recorded \$150,000 in 2005 and \$131,000 in 2004 in recovery of lost rents, included in apartment rental income in our statements of operations.

### Note 9. Income taxes

We operate as, and elect to be taxed as, a REIT under the Internal Revenue Code. To qualify as a REIT, we must meet a number of organizational and operational requirements, including a requirement that we currently distribute at least 90%

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of our adjusted taxable income to our common shareholders. We intend to adhere to these requirements and maintain the company's REIT status. As a REIT, we generally will not be subject to corporate level federal or state income tax on taxable income we distribute currently to our shareholders. If we fail to qualify as a REIT in any taxable year, we will be subject to federal and state income taxes at regular corporate rates (including any applicable alternative minimum tax) and may not be able to qualify as a REIT for four subsequent taxable years. Even if we qualify for taxation as a REIT, we may be subject to certain state and local taxes on income and property, and to federal income and excise taxes on undistributed taxable income. In addition, taxable income from non-REIT activities managed through taxable REIT subsidiaries would be subject to federal, state and local income taxes.

The following table reconciles our income as reflected in our financial statements to REIT taxable income. Taxable income differs from income for financial statement purposes, primarily due to differences for tax purposes in the estimated useful lives and methods used to compute depreciation and the carrying value (basis) of the investment in properties.

|   | 2005<br>Estimate | 2004<br>Actual |
|---|------------------|----------------|
|   | -----            | -----          |
|   | (000's)          | (000's)        |
| (Loss) income before minority interests                           | \$ (2,155)       | \$ 1,055       |
| (Income) loss attributed to consolidated limited partnerships     | 8,335            | -              |
|   | -----            | -----          |
| Income (loss) subject to income tax - owned properties            | 6,180            | 1,055          |
| Reconciling items:  |                  |                |
| Depreciation differences  | 1,225            | 375            |
| GAAP gain on sale of apartment community in tax-free exchange     | (8,130)          | -              |
| One-time deduction allocated to Wind River Apartments contributor | -                | (1746)         |
| Other book/tax differences, net                                   | 270              | (70)           |
|   | -----            | -----          |
| Adjusted taxable (loss) income - Operating Partnership            | (455)            | (386)          |
| Minority share of taxable (income) loss                           | 255              | 1,010          |
|   | -----            | -----          |
| Taxable income (loss) subject to dividend requirement             | \$ (200)         | \$ 624         |
|   | =====            | =====          |
| Minimum dividend required (90% of taxable income)                 | \$ -             | \$ 561         |
|   | =====            | =====          |

The actual tax deduction for dividends that we take, and the taxability of dividends to shareholders, is based on a measurement of "earnings and profits" as defined by the Internal Revenue Code. Earnings and profits differ from regular taxable income, primarily due to further differences in the estimated useful lives and methods used to compute depreciation. The following table reconciles the dividends paid deduction taken by the company (the portion of dividends paid that are taxable as ordinary income to shareholders) on its tax

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returns to cash dividends paid.

|  | 2005<br>Estimate | 2004<br>Actual |
|--|------------------|----------------|
|  | (000's)          | (000's)        |
| Dividends paid deduction for   |                  |                |
| Preferred dividends paid   | \$ 300           | \$ 1,000       |
| Common dividends paid  | -                | 742            |
|  | 300              | 1,742          |
| Dividends on nonvested common stock, treated<br>as compensation expense for tax purposes | 100              | -              |
| Portion of dividends<br>designated as return of capital                                  | 9,990            | 6,809          |
|  | \$ 10,390        | \$ 8,551       |

We paid dividend distributions totaling \$1.00 per share to common shareholders in 2005, 2004 and 2003. In early January following each year end, we must make an estimate of earnings and profits, and publish an allocation between ordinary dividend income and non-taxable return of capital to common shareholders. The allocation between ordinary dividend income and non-taxable return of capital to common shareholders was as follows:

|                   | 2005   |        | 2004   |        | 2003   |
|-------------------|--------|--------|--------|--------|--------|
|                   | \$     | %      | \$     | %      | \$     |
| Ordinary income   | \$0.00 | 00.0%  | \$0.12 | 12.0%  | \$0.17 |
| Return of capital | 1.00   | 100.0% | 0.88   | 88.0%  | 0.83   |
|                   | \$1.00 | 100.0% | \$1.00 | 100.0% | \$1.00 |

### Note 10. Related party transactions

In 2005 and 2004, we issued 138,000 operating partnership units to acquire Savannah Shores Apartments from a group of investors to whom we refer as the "Chrysson Parties." Previously, between 1997 and 2002, we issued 1.5 million operating partnership units to acquire eight apartment communities from this group. Certain current directors of the company were shareholders and officers in the Chrysson Parties.

In February 1997, we entered into a participating loan agreement with The Villages Partnership, which we now include in our consolidated financial statements effective January 2005. We record minimum interest on a \$100,000 note payable at the greater of 12.5% or the 30-day LIBOR rate plus 6.125%, and we are entitled to 25% participation in increased rental revenue and 25% participation in the increase in value of the property. In July 2001, we modified the participating loan agreement to establish a \$950,000 "fixed portion" of our participation in the increase in value of the property and extend the period for our 25% participation in increased rental revenue and increase in value of the property to the earlier of July 2011 or sale or refinance of the property. We



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received \$383,000 of the fixed portion during 2002 and 2001. Required payment of the fixed portion is subject to cash flow from the Villages property, as defined in the agreement. Interest on the outstanding fixed portion accrues at the greater of a prime rate or 8%, payable monthly.

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During 2005, the operating partnership recorded interest income related to the participating loan agreement of \$59,000, along with interest income related to notes and other receivables acquired in our acquisition of BIC of \$70,000, which have been eliminated in consolidation. At December 31, 2005, we have eliminated amounts receivable for loans and advances to the Villages Partnership totaling \$2.3 million in consolidation. We received interest and participation income of \$59,000, along with guarantee fees of \$12,000, in each of 2004 and 2003 related to the participating loan agreement.

In 1996 through 1999, we made loans totaling \$140,000, on an interest-free basis, to certain officers of the company. The loans are secured by shares of the company's common stock and are payable in full six months after termination of employment. These loans are included in our balance sheets in other assets.

### Note 11. Profit sharing plan

The employees of the company are participants in a profit sharing plan pursuant to Section 401 of the Internal Revenue Code. We make limited matching contributions based on the level of employee participation as defined in the plan. We made contributions to the plan totaling \$107,000 in 2005, \$82,000 in 2004, and \$57,000 in 2003.

### Note 12. Commitments and contingencies

We expect to spend approximately \$1.3 million in early 2006 for reconstruction of an apartment building damaged by fire and \$1.2 million for other significant improvements projects at our apartment communities. (We expect to receive insurance proceeds of approximately \$1.1 million in early 2006, which we plan to apply toward the cost of the reconstruction.)

We currently lease 10,000 square feet of office space in downtown Charlotte, North Carolina, for our corporate and administrative offices. Rent expense totaled \$178,000 in 2005, and \$163,000 in 2004 and 2003. The lease agreements for the office space provide for monthly rental of \$19,000 and expire in January and June 2008.

We have agreements with four of our executive officers that provide for cash compensation and other benefits if we terminate them without cause or if a change in control of the company occurs.

The company is a party to a variety of legal proceedings arising in the ordinary course of its business. We believe that such matters will not have a material effect on the financial position or results of operations of the company.

### Note 13. Quarterly financial data (unaudited)

We present below selected financial data (unaudited) for the years ended December 31, 2005 and 2004.

|               | Net Income (Loss) |           |
|---------------|-------------------|-----------|
| Revenues from | -----             | Per Share |

|               | Net Income (Loss) |           |
|---------------|-------------------|-----------|
| Revenues from | -----             | Per Share |

Income (Attribution) Comm

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|                | Continuine<br>Operations | Total      | Basic     | Diluted   | Sharehol<br>Per Share, |
|----------------|--------------------------|------------|-----------|-----------|------------------------|
|                | (000's)                  | (000's)    |           |           |                        |
| 2005           |                          |            |           |           |                        |
| First quarter  | \$ 15,035                | \$ (5,970) | \$ (0.66) | \$ (0.66) | \$ (0.                 |
| Second quarter | 18,166                   | (409)      | (0.04)    | (0.04)    | (0.                    |

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|                | Revenues from<br>Continuine<br>Operations | Net Income (Loss) |           | Income (   |        |
|----------------|---|-------------------|-----------|------------|--------|
|                | (000's)                                   | Total             | Per Share | Attribut   |        |
|                | (000's)                                   | (000's)           | Basic     | Comm       |        |
|                |   |                   | Diluted   | Sharehol   |        |
|                |   |                   |           | Per Share, |        |
| Third quarter  | 18,892                                    | (150)             | (0.01)    | (0.01)     | (0.    |
| Fourth quarter | 19,919                                    | 5,040             | 0.55      | 0.55       | 0.     |
|                | \$ 72,012                                 | \$ (1,488)        | \$ (0.16) | \$ (0.16)  | \$ (0. |
| 2004           |   |                   |           |            |        |
| First quarter  | \$ 11,231                                 | \$ 373            | \$ 0.06   | \$ 0.05    | \$ 0.  |
| Second quarter | 11,858                                    | 217               | 0.03      | 0.02       | (0.    |
| Third quarter  | 13,268                                    | 299               | 0.03      | 0.03       | 0.     |
| Fourth quarter | 13,630                                    | 150               | 0.02      | 0.01       | (0.    |
|                | \$ 49,986                                 | \$ 1,039          | \$ 0.14   | \$ 0.11    | \$ 0.  |

Note 14. Subsequent events

The Board of Directors declared a regular quarterly dividend of \$0.26 per common share on January 19, 2006, payable on February 15, 2006, to shareholders of record on February 1, 2006.

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Report of Independent Auditors

Board of Directors and Stockholders  
BNP Residential Properties, Inc.

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We have audited the accompanying statement of revenues and certain operating expenses of the Hamptons Apartments ("the Apartments") for the year ended December 31, 2004. This statement is the responsibility of Company management. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Apartments' internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

The accompanying statement of revenues and certain operating expenses was prepared for the purpose of complying with the rules and regulations of the Securities and Exchange Commission, as described in Note 1, and is not intended to be a complete presentation of the Hamptons Apartments' revenues and expenses.

In our opinion, the statement of revenues and certain operating expenses referred to above presents fairly, in all material respects, the revenues and certain operating expenses described in Note 1 of the Hamptons Apartments for the year ended December 31, 2004 in conformity with accounting principles generally accepted in the United States of America.

/s/ Grant Thornton LLP

Charlotte, North Carolina  
March 6, 2006

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Hamptons Apartments  
Statements of Revenue and Certain Operating Expenses

|                             | Year ended<br>December 31,<br>2004 | Nine<br>Sept |
|-----------------------------|------------------------------------|--------------|
|                             | -----                              | -----        |
| Rental income               | \$ 1,852,940                       |              |
| Certain operating expenses: |                                    |              |
| Property operations expense | 604,066                            |              |

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|   |              |       |
|---|--------------|-------|
| Property insurance                              | 62,847       |       |
| Property taxes                                  | 155,241      |       |
|   | -----        | ----- |
|   | 822,154      | ----- |
|   | -----        | ----- |
| Revenue in excess of certain operating expenses | \$ 1,030,786 | ===== |
|   | =====        | ===== |

See accompanying notes.

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Hamptons Apartments  
Notes to Statements of Revenue and Certain Operating Expenses  
For the year ended December 31, 2004, and  
For the nine months ended September 30, 2005 (Unaudited)

### 1. Summary of Significant Accounting Policies

#### Basis of presentation

These statements of revenue and certain operating expenses reflect the operations of an apartment property located in Charlotte, North Carolina. Hamptons Apartments is not a legal entity; it is an apartment property acquired by BNP Residential Properties, Inc. in October 2005. The 232-unit apartment property was built in 1986.

We prepared these statements in accordance with Rule 3-14 of Regulation S-X. Accordingly, these statements exclude items such as interest, depreciation and amortization, and general and administrative expenses that are not comparable to the anticipated future on-site operations of the apartment property.

#### Revenue recognition

Hamptons Apartments leased its residential apartments under operating leases with monthly payments due in advance. The majority of the apartment leases were for terms of one year or less. Rental and other revenues were recorded as earned.

#### Advertising expense

Hamptons Apartments charged advertising costs to property operations expense as incurred. Advertising expense included in property operations expense totaled approximately \$45,000 for the year ended December 31, 2004 and approximately \$29,000 for the nine months ended September 30, 2005.

#### Use of estimates

We are required to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes in order to prepare them in accordance with generally accepted accounting principles. Actual results could differ from those amounts.

#### Interim financial data

The financial statements for the period ended September 30, 2005, include all adjustments that are, in management's opinion, necessary for a fair presentation of the revenues and certain operating expenses for this interim period. Operating results for the period ended September 30, 2005, are not necessarily indicative of the results to be expected for the entire year ending December 31,

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2005.

### 2. Environmental matters

Hamptons Apartments has been subjected to Phase I environmental reviews. These reviews did not reveal, nor is management aware of, any environmental liability that management believes would have a material adverse effect on the accompanying financial statements.

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### Report of Independent Auditors

Board of Directors and Stockholders  
BNP Residential Properties, Inc.

We have audited the accompanying statement of revenues and certain operating expenses of the Timbers Apartments ("the Apartments") for the year ended December 31, 2004. This statement is the responsibility of Company management. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Apartments' internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

The accompanying statement of revenues and certain operating expenses was prepared for the purpose of complying with the rules and regulations of the Securities and Exchange Commission, as described in Note 1, and is not intended to be a complete presentation of the Timbers Apartments' revenues and expenses.

In our opinion, the statement of revenues and certain operating expenses referred to above presents fairly, in all material respects, the revenues and certain operating expenses described in Note 1 of the Timbers Apartments for the year ended December 31, 2004 in conformity with accounting principles generally accepted in the United States of America.

/s/ Grant Thornton LLP

Charlotte, North Carolina

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March 6, 2006

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Timbers Apartments  
Statements of Revenue and Certain Operating Expenses

|   | Year ended<br>December 31,<br>2004 | Nine<br>Sept |
|---|------------------------------------|--------------|
|   | -----                              | -----        |
| Rental income                                   | \$ 2,122,183                       |              |
| Certain operating expenses:                     |                                    |              |
| Property operations expense                     | 521,399                            |              |
| Property insurance                              | 51,178                             |              |
| Property taxes                                  | 161,482                            |              |
|   | -----                              | -----        |
|   | 734,059                            |              |
|   | -----                              | -----        |
| Revenue in excess of certain operating expenses | \$ 1,388,124                       |              |
|   | =====                              | =====        |

See accompanying notes.

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Timbers Apartments  
Notes to Statements of Revenue and Certain Operating Expenses  
For the year ended December 31, 2004 and  
For the nine months ended September 30, 2005 (Unaudited)

3. Summary of Significant Accounting Policies

Basis of presentation

These statements of revenue and certain operating expenses reflect the operations of an apartment property located in Richmond, Virginia. Timbers Apartments is not a legal entity; it is an apartment property acquired by BNP Residential Properties, Inc. in October 2005. The 240-unit apartment property was built in 1989.

We prepared these statements in accordance with Rule 3-14 of Regulation S-X. Accordingly, these statements exclude items such as interest, depreciation and amortization, and general and administrative expenses that are not comparable to the anticipated future on-site operations of the apartment property.

Revenue recognition

Timbers Apartments leased its residential apartments under operating leases with monthly payments due in advance. The majority of the apartment leases were for

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terms of one year or less. Rental and other revenues were recorded as earned.

### Advertising expense

Timbers Apartments charged advertising costs to property operations expense as incurred. Advertising expense included in property operations expense totaled approximately \$41,700 for the year ended December, 2004 and approximately \$31,000 for the nine months ended September, 2005.

### Use of estimates

We are required to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes in order to prepare them in accordance with generally accepted accounting principles. Actual results could differ from those amounts.

### Interim financial data

The financial statements for the period ended September 30, 2005, include all adjustments that are, in management's opinion, necessary for a fair presentation of the revenues and certain operating expenses for this interim period. Operating results for the period ended September 30, 2005, are not necessarily indicative of the results to be expected for the entire year ending December 31, 2005.

### 4. Environmental matters

Timbers Apartments has been subjected to Phase I environmental reviews. These reviews did not reveal, nor is management aware of, any environmental liability that management believes would have a material adverse effect on the accompanying financial statements.

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### BNP RESIDENTIAL PROPERTIES, INC.

-----  
 Schedule III - Real Estate and Accumulated Depreciation  
 Year ended December 31, 2005

| Description<br>-----              | Encumb.<br>----- | Initial Costs<br>----- |                            | Costs<br>Capitalized<br>Subsequent<br>to Acquisition | Gros                     |
|-----------------------------------|------------------|------------------------|----------------------------|--|--------------------------|
|                                   |                  | Land                   | Buildings &<br>Improvem'ts |  | Carried<br>-----<br>Land |
| Owned apartment properties:       |                  |                        |                            |  |                          |
| North Carolina:                   |                  |                        |                            |  |                          |
| Abbington Place, Greensboro       | \$ 23,700,000    | \$ 2,302,000           | \$ 23,598,676              | 292,265  | \$ 2,302,000             |
| Allerton Place, Greensboro        | 10,270,000       | 1,384,000              | 14,650,428                 | 276,737  | 1,384,000                |
| Barrington Place, Charlotte       | 19,509,835       | 2,604,000              | 24,002,687                 | 357,253  | 2,604,000                |
| Brookford Place, Greensboro       | 4,689,887        | 465,000                | 5,157,507                  | 108,891  | 465,000                  |
| Carriage Club, Mooresville        | 14,818,648       | 1,984,000              | 17,714,261                 | 150,158  | 1,984,000                |
| Chason Ridge, Fayetteville        | 15,500,000       | 624,000                | 11,790,472                 | 1,003,908  | 994,606                  |
| Fairington, Charlotte             | 13,400,000       | 4,257,200              | 14,322,231                 | 751,069  | 4,257,200                |
| Hamptons, Charlotte               | 9,392,418        | 3,561,700              | 13,945,831                 | 32,229   | 3,561,700                |
| Laurel Springs, High Point        | 11,187,808       | 1,303,800              | 13,256,894                 | 80,981   | 1,303,800                |
| Laurel Springs - Ph 2, High Point | 5,808,720        | 455,000                | 6,663,904                  | 8,693  | 455,000                  |
| Mallard Creek 1, Charlotte        | 7,120,000        | 1,003,298              | 7,867,857                  | 1,837,691  | 1,003,298                |
| Mallard Creek 2, Charlotte        | 14,933,759       | 1,790,000              | 16,113,942                 | 635,634  | 1,790,000                |
| Madison Hall, Clemmons            | 4,245,000        | 303,000                | 6,054,307                  | 288,039  | 303,000                  |
| Marina Sh. Waterfront, Cornelius  | 15,271,926       | 4,144,000              | 15,062,322                 | 1,097,464  | 4,144,000                |
| Oak Hollow, Cary                  | 8,385,000        | 1,480,000              | 10,808,689                 | 2,212,183  | 1,480,000                |
| Oak Hollow - Phase 2, Cary        | 8,294,088        | 1,914,000              | 10,485,239                 | 2,242,013  | 1,914,000                |
| Oakbrook, Charlotte               | 7,562,276        | 848,835                | 8,523,384                  | 1,218,969  | 848,835                  |

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|                                |            |           |            |           |           |
|--------------------------------|------------|-----------|------------|-----------|-----------|
| Paces Commons, Charlotte       | 15,728,414 | 1,430,158 | 12,871,424 | 1,831,588 | 1,448,184 |
| Paces Village, Greensboro      | 7,000,000  | 1,250,000 | 9,416,580  | 714,422   | 1,250,000 |
| Pepperstone, Greensboro        | 5,720,000  | 552,000   | 5,015,153  | 380,652   | 552,000   |
| Salem Ridge, Winston-Salem     | 2,610,000  | 402,000   | 3,952,533  | 267,864   | 402,000   |
| Savannah Place, Winston-Salem  | 10,150,000 | 790,000   | 10,032,721 | 491,797   | 790,000   |
| Southpoint, Durham             | 8,200,000  | 1,610,500 | 8,620,734  | 257,330   | 1,610,500 |
| Summerlyn Place, Burlington    | 6,645,000  | 837,000   | 9,559,115  | 211,317   | 837,000   |
| Waterford Place, Greensboro    | 20,293,000 | 1,686,000 | 16,745,972 | 64,809    | 1,686,000 |
| Wind River, Morrisville        | 19,341,343 | 3,170,000 | 21,922,771 | 684,230   | 3,170,000 |
| Woods Edge, Durham             | 13,950,000 | 994,000   | 13,061,195 | 1,837,678 | 994,000   |
| Computer and support equipment | -          | -         | -          | 1,415,716 | -         |

---

|  |             |            |             |            |            |
|--|-------------|------------|-------------|------------|------------|
|  | 303,727,122 | 43,145,491 | 331,216,829 | 20,751,580 | 43,534,123 |
|--|-------------|------------|-------------|------------|------------|

South Carolina:

|                          |            |           |            |           |           |
|--------------------------|------------|-----------|------------|-----------|-----------|
| Canterbury, Myrtle Beach | 23,429,077 | 2,000,000 | 23,755,561 | 2,848,703 | 4,705,838 |
| Paces Watch, Charleston  | 14,925,000 | 2,848,000 | 17,621,918 | 263,057   | 2,848,000 |
| Pelham, Greenville       | 4,384,899  | 630,000   | 4,991,397  | 416,505   | 630,000   |
| Waverly, Charleston      | 10,160,000 | 1,800,000 | 11,304,741 | 392,402   | 1,800,000 |

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|  |            |           |            |           |           |
|--|------------|-----------|------------|-----------|-----------|
|  | 52,898,976 | 7,278,000 | 57,673,617 | 3,920,667 | 9,983,838 |
|--|------------|-----------|------------|-----------|-----------|

Description

-----

|              |                 |         |
|--------------|-----------------|---------|
| Accumulated  | Date of Date    | Life    |
| Depreciation | Constr.Acquired | (Years) |

Owned apartment properties:

North Carolina:

|                                   |              |      |        |    |
|-----------------------------------|--------------|------|--------|----|
| Abbingtion Place, Greensboro      | \$ 6,677,691 | 1997 | Dec-97 | 40 |
| Allerton Place, Greensboro        | 3,594,146    | 1998 | Sep-98 | 40 |
| Barrington Place, Charlotte       | 2,509,399    | 1999 | May-02 | 60 |
| Brookford Place, Greensboro       | 641,715      | 1998 | May-02 | 60 |
| Carriage Club, Mooresville        | 914,213      | 2000 | Jun-04 | 60 |
| Chason Ridge, Fayetteville        | 2,679,879    | 1994 | Jan-99 | 40 |
| Fairington, Charlotte             | 854,052      | 1981 | Aug-04 | 40 |
| Hamptons, Charlotte               | 79,723       | 1986 | Oct-05 | 40 |
| Laurel Springs, High Point        | 363,194      | 2002 | Mar-05 | 60 |
| Laurel Springs - Ph 2, High Point | 155,876      | 2004 | Mar-05 | 60 |
| Mallard Creek 1, Charlotte        | 2,854,625    | 1988 | Dec-94 | 40 |
| Mallard Creek 2, Charlotte        | 1,072,575    | 1997 | Aug-03 | 60 |
| Madison Hall, Clemmons            | 1,468,026    | 1997 | Aug-98 | 40 |
| Marina Sh. Waterfront, Cornelius  | 1,724,002    | 1994 | Sep-02 | 60 |
| Oak Hollow, Cary                  | 2,679,297    | 1983 | Jul-98 | 40 |
| Oak Hollow - Phase 2, Cary        | 2,410,682    | 1986 | Dec-00 | 40 |
| Oakbrook, Charlotte               | 3,063,997    | 1985 | Jun-94 | 40 |
| Paces Commons, Charlotte          | 5,043,085    | 1988 | Jun-93 | 40 |
| Paces Village, Greensboro         | 2,990,135    | 1988 | Apr-96 | 40 |
| Pepperstone, Greensboro           | 1,468,994    | 1992 | Dec-97 | 40 |
| Salem Ridge, Winston-Salem        | 151,582      | 1984 | Mar-05 | 40 |
| Savannah Place, Winston-Salem     | 2,875,932    | 1991 | Dec-97 | 40 |
| Southpoint, Durham                | 468,286      | 1987 | Sep-04 | 43 |
| Summerlyn Place, Burlington       | 2,148,524    | 1998 | Sep-98 | 40 |
| Waterford Place, Greensboro       | 4,715,414    | 1997 | Dec-97 | 40 |
| Wind River, Morrisville           | 1,187,485    | 2000 | May-04 | 60 |
| Woods Edge, Durham                | 3,450,534    | 1985 | Jun-98 | 40 |
| Computer and support equipment    | 794,634      |      |        |    |

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59,037,698

South Carolina:

|                          |         |      |        |    |
|--------------------------|---------|------|--------|----|
| Canterbury, Myrtle Beach | 668,551 | 1999 | Mar-05 | 60 |
| Paces Watch, Charleston  | 413,641 | 1987 | May-05 | 55 |
| Pelham, Greenville       | 634,078 | 1985 | Mar-03 | 45 |
| Waverly, Charleston      | 354,893 | 1986 | Apr-05 | 45 |

-----  
2,071,164

99

| Description<br>-----             | Encumb.<br>----- | Initial Costs<br>----- |                            | Costs<br>Capitalized<br>Subsequent<br>to Acquisition | Gros<br>Carried<br>----- |
|----------------------------------|------------------|------------------------|----------------------------|--|--------------------------|
|                                  |                  | Land                   | Buildings &<br>Improvem'ts |  | Land                     |
| Virginia:                        |                  |                        |                            |  |                          |
| Latitudes, Virginia Beach        | -                | 3,360,000              | 18,606,667                 | 1,343,214  | 3,358,558                |
| Timbers, Richmond                | 17,300,000       | 2,212,000              | 20,231,558                 | 38,982   | 2,212,000                |
|                                  | 17,300,000       | 5,572,000              | 38,838,225                 | 1,382,196  | 5,570,558                |
| -----                            |                  |                        |                            |  |                          |
| Total owned apartment properties | 373,926,098      | 55,995,491             | 427,728,671                | 26,054,443   | 59,088,518               |
| Owned restaurant properties:     |                  |                        |                            |  |                          |
| North Carolina:                  |                  |                        |                            |  |                          |
| Burlington                       | (1)              | 162,411                | 417,629                    | -  | 162,411                  |
| Denver                           | (1)              | 275,484                | 708,387                    | -  | 275,484                  |
| Eden                             | (1)              | 253,282                | 651,296                    | -  | 253,282                  |
| Fayetteville (Ramsey)            | (1)              | 260,135                | 668,919                    | -  | 260,135                  |
| Fayetteville (N.Eastern)         | (1)              | 308,271                | 792,696                    | -  | 308,271                  |
| Hillsborough                     | (1)              | 290,868                | 747,948                    | -  | 290,868                  |
| Kinston (W. Vernon)              | (1)              | 237,135                | 609,777                    | -  | 237,135                  |
| Kinston (Richlands)              | (1)              | 231,678                | 595,743                    | -  | 231,678                  |
| Newton                           | (1)              | 223,453                | 574,594                    | -  | 223,453                  |
| Siler City                       | (1)              | 268,312                | 689,945                    | -  | 268,312                  |
| Spring Lake                      | (1)              | 218,925                | 562,949                    | -  | 218,925                  |
| Thomasville (E. Main)            | (1)              | 253,716                | 652,411                    | -  | 253,716                  |
| Thomasville (Randolph)           | (1)              | 327,727                | 842,726                    | -  | 327,727                  |
|                                  |                  | 3,311,397              | 8,515,020                  | -  | 3,311,397                |
| -----                            |                  |                        |                            |  |                          |
| Virginia:                        |                  |                        |                            |  |                          |
| Ashland                          | (1)              | 296,509                | 762,452                    | -  | 296,509                  |
| Blackstone                       | (1)              | 275,565                | 708,596                    | -  | 275,565                  |
| Bluefield                        | (1)              | 205,700                | 528,947                    | -  | 205,700                  |
| Chester                          | (1)              | 300,165                | 771,852                    | -  | 300,165                  |
| Clarksville                      | (1)              | 211,545                | 543,972                    | -  | 211,545                  |
| Clintwood                        | (1)              | 222,673                | 572,588                    | -  | 222,673                  |
| Dublin                           | (1)              | 364,065                | 936,168                    | -  | 364,065                  |
| Franklin                         | (1)              | 287,867                | 740,230                    | -  | 287,867                  |
| Galax                            | (1)              | 309,578                | 796,057                    | -  | 309,578                  |
| Hopewell                         | (1)              | 263,939                | 678,701                    | -  | 263,939                  |
| Lebanon                          | (1)              | 266,340                | 684,876                    | -  | 266,340                  |

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|                        |     |         |         |   |         |
|------------------------|-----|---------|---------|---|---------|
| Lynchburg (Langhorne)  | (1) | 249,865 | 642,509 | - | 249,865 |
| Lynchburg (Timberlake) | (1) | 276,153 | 710,107 | - | 276,153 |
| Norfolk                | (1) | 325,822 | 837,829 | - | 325,822 |

| Description<br>-----                          | Accumulated<br>Depreciation | Date of<br>Constr. | Date<br>Acquired | Life<br>(Years) |
|---|-----------------------------|--------------------|------------------|-----------------|
| Virginia:                                     |                             |                    |                  |                 |
| Latitudes, Virginia Beach                     | 6,130,764                   | 1989               | Oct-94           | 38              |
| Timbers, Richmond                             | 101,698                     | Jun-05             | Oct-05           | 50              |
|   | -----                       |                    |                  |                 |
|   | 6,232,463                   |                    |                  |                 |
|   | -----                       |                    |                  |                 |
| Total owned apartment properties <sup>3</sup> | 67,341,324                  |                    |                  |                 |
| Owned restaurant properties:                  |                             |                    |                  |                 |
| North Carolina:                               |                             |                    |                  |                 |
| Burlington                                    | 195,404                     | Oct-85             | Apr-87           | 40              |
| Denver  | 331,447                     | Jul-83             | Apr-87           | 40              |
| Eden  | 304,734                     | Jun-73             | Apr-87           | 40              |
| Fayetteville (Ramsey)                         | 312,980                     | Oct-73             | Apr-87           | 40              |
| Fayetteville (N.Eastern)                      | 370,894                     | Sep-83             | Apr-87           | 40              |
| Hillsborough                                  | 349,957                     | Mar-78             | Apr-87           | 40              |
| Kinston (W. Vernon)                           | 285,308                     | Jul-62             | Apr-87           | 40              |
| Kinston (Richlands)                           | 278,742                     | Dec-81             | Apr-87           | 40              |
| Newton  | 268,847                     | Mar-76             | Apr-87           | 40              |
| Siler City                                    | 322,818                     | May-79             | Apr-87           | 40              |
| Spring Lake                                   | 263,398                     | Mar-76             | Apr-87           | 40              |
| Thomasville (E. Main)                         | 305,256                     | Feb-66             | Apr-87           | 40              |
| Thomasville (Randolph)                        | 394,302                     | Apr-74             | Apr-87           | 40              |
|   | -----                       |                    |                  |                 |
|   | 3,984,087                   |                    |                  |                 |
| Virginia:                                     |                             |                    |                  |                 |
| Ashland                                       | 356,744                     | Apr-87             | Apr-87           | 40              |
| Blackstone                                    | 331,545                     | Sep-79             | Apr-87           | 40              |
| Bluefield                                     | 247,489                     | Feb-85             | Apr-87           | 40              |
| Chester                                       | 361,141                     | May-73             | Apr-87           | 40              |
| Clarksville                                   | 254,519                     | Oct-85             | Apr-87           | 40              |
| Clintwood                                     | 267,908                     | Jan-81             | Apr-87           | 40              |
| Dublin  | 438,023                     | Jul-83             | Apr-87           | 40              |
| Franklin                                      | 346,346                     | Feb-75             | Apr-87           | 40              |
| Galax   | 372,466                     | Jun-74             | Apr-87           | 40              |
| Hopewell                                      | 317,557                     | Jun-78             | Apr-87           | 40              |
| Lebanon                                       | 320,447                     | Jun-83             | Apr-87           | 40              |
| Lynchburg (Langhorne)                         | 300,623                     | Sep-82             | Apr-87           | 40              |
| Lynchburg (Timberlake)                        | 332,251                     | Aug-83             | Apr-87           | 40              |
| Norfolk                                       | 392,011                     | Aug-84             | Apr-87           | 40              |

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| Description<br>-----   | Encumb.<br>----- | Initial Costs<br>----- |                            | Costs<br>Capitalized<br>Subsequent<br>to Acquisition | Gros<br>Carried<br>-----<br>Land |
|--|------------------|------------------------|----------------------------|--|----------------------------------|
|  |                  | Land                   | Buildings &<br>Improvem'ts |  |                                  |
| Orange   | (1)              | 244,883                | 629,699                    | -  | 244,883                          |
| Petersburg   | (1)              | 357,984                | 920,531                    | -  | 357,984                          |
| Richmond (Forest Hill)   | (1)              | 196,084                | 504,216                    | -  | 196,084                          |
| Richmond (Midlothian)  | (1)              | 270,736                | 696,179                    | -  | 270,736                          |
| Richmond (Myers)   | (1)              | 321,946                | 827,861                    | -  | 321,946                          |
| Roanoke (Hollins)  | (1)              | 257,863                | 663,076                    | -  | 257,863                          |
| Roanoke (Abenham)  | (1)              | 235,864                | 606,507                    | -  | 235,864                          |
| Rocky Mount  | (1)              | 248,434                | 638,829                    | -  | 248,434                          |
| Smithfield   | (1)              | 223,070                | 573,608                    | -  | 223,070                          |
| Verona   | (1)              | 191,631                | 492,765                    | -  | 191,631                          |
| Virginia Beach (Lynnhaven)                                       | (1)              | 271,570                | 698,322                    | -  | 231,731                          |
| Virginia Beach (Holland)   | (1)              | 277,943                | 714,710                    | -  | 277,943                          |
| Wise   | (1)              | 219,471                | 564,355                    | -  | 219,471                          |
|  |                  | 7,173,265              | 18,445,542                 | -  | 7,133,426                        |
| -----  |                  |                        |                            |  |                                  |
| Total owned restaurant properties                                | 14,649,857       | 10,484,662             | 26,960,562                 | -  | 10,444,823                       |
| -----  |                  |                        |                            |  |                                  |
| Total owned real estate  | 388,575,955      | 66,480,153             | 454,689,233                | 26,054,443   | 69,533,341                       |
| -----  |                  |                        |                            |  |                                  |
| Equity interests in consolidated limited partnership properties: |                  |                        |                            |  |                                  |
| Marina Shores, Virginia Beach VA                                 | 33,504,843       | 2,440,000              | 29,991,385                 | 195,315  | 2,440,000                        |
| Villages of Ch. Hill, Carrboro NC                                | 11,828,541       | 547,000                | 13,643,468                 | 26,816   | 547,000                          |
| Villages - Phase 5, Carrboro NC                                  | 2,802,772        | 226,950                | 2,712,761                  | (2,270)  | 226,950                          |
|  | 48,136,156       | 3,213,950              | 46,347,614                 | 219,861  | 3,213,950                        |
| -----  |                  |                        |                            |  |                                  |
| Total real estate, consolidated                                  | \$ 436,712,111   | \$ 69,694,103          | \$ 501,036,847             | \$ 26,274,304  | \$ 72,747,291                    |
| =====  |                  |                        |                            |  |                                  |

Description  
-----

Accumulated Date of Date Life  
Depreciation Constr.Acquired(Years)

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|                            |         |        |        |    |
|----------------------------|---------|--------|--------|----|
| Orange                     | 294,629 | Aug-74 | Apr-87 | 40 |
| Petersburg                 | 430,707 | Mar-74 | Apr-87 | 40 |
| Richmond (Forest Hill)     | 235,917 | Nov-74 | Apr-87 | 40 |
| Richmond (Midlothian)      | 325,734 | Jan-74 | Apr-87 | 40 |
| Richmond (Myers)           | 387,348 | Apr-83 | Apr-87 | 40 |
| Roanoke (Hollins)          | 310,247 | Feb-73 | Apr-87 | 40 |
| Roanoke (Abenham)          | 283,779 | Nov-82 | Apr-87 | 40 |
| Rocky Mount                | 298,901 | May-80 | Apr-87 | 40 |
| Smithfield                 | 268,385 | Apr-77 | Apr-87 | 40 |
| Verona                     | 230,559 | Jan-85 | Apr-87 | 40 |
| Virginia Beach (Lynnhaven) | 326,738 | Jun-80 | Apr-87 | 40 |
| Virginia Beach (Holland)   | 334,405 | Aug-83 | Apr-87 | 40 |
| Wise                       | 264,055 | Jun-80 | Apr-87 | 40 |

-----  
8,630,474

-----  
Total owned restaurant properties 12,614,561  
-----

Total owned real estate 79,955,885

Equity interests in consolidated limited partnership properties:

|                                   |           |      |        |    |
|-----------------------------------|-----------|------|--------|----|
| Marina Shores, Virginia Beach VA  | 6,796,894 | 1981 | Jan-05 | 35 |
| Villages of Ch. Hill, Carrboro NC | 500,254   | 1975 | Jan-05 | 25 |
| Villages - Phase 5, Carrboro NC   | 415,079   | 1987 | Jan-05 | 30 |

-----  
7,712,227  
-----

-----  
Total real estate, consolidated\$ \$ 87,668,112  
=====

(1) Indicates the restaurants encumbered by a line of credit with a bank for up to \$14,649,857 outstanding at 12/31/05.

(2) Aggregate cost basis at December 31, 2005, for federal income tax purposes was approximately \$512 million.

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BNP RESIDENTIAL PROPERTIES, INC.

-----  
Schedule III - Real Estate and Accumulated Depreciation

|                              | 2005           | 2004           | 2003     |
|------------------------------|----------------|----------------|----------|
|                              | -----          | -----          | -----    |
| Real estate investments:     |                |                |          |
| Balance at beginning of year | \$ 426,524,525 | \$ 337,066,609 | \$ 314,8 |

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|                                |                |                |          |
|--------------------------------|----------------|----------------|----------|
| Additions during year          |                |                |          |
| Limited partnership properties |                |                |          |
| consolidated effective Jan05   | 49,561,564     |                |          |
| Acquisitions                   | 129,721,278    | 86,148,336     | 23,5     |
| Improvements, etc.             | 8,299,159      | 5,231,775      | 3,3      |
| Deductions during year         |                |                |          |
| Apartment property sold        | (14,500,619)   | -              |          |
| Other deductions               | (2,640,492)    | (1,922,195)    | (4,6     |
| Balance at close of year       | \$ 596,965,415 | \$ 426,524,525 | \$ 337,0 |
| Accumulated depreciation:      |                |                |          |
| Balance at beginning of year   | \$ 66,453,731  | \$ 56,052,569  | \$ 49,4  |
| Limited partnership properties |                |                |          |
| consolidated effective Jan05   | 6,404,930      |                |          |
| Provision for depreciation     | 16,978,664     | 11,660,219     | 10,0     |
| Deductions during year         |                |                |          |
| Apartment property sold        | (425,819)      | -              |          |
| Other deductions               | (1,743,394)    | (1,259,057)    | (3,4     |
| Balance at close of year       | \$ 87,668,112  | \$ 66,453,731  | \$ 56,0  |

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### INDEX TO EXHIBITS

Exhibit No.

- 2.1\* Master Agreement of Merger and Acquisition by and among BNP Residential Properties, Inc., BNP Residential Properties Limited Partnership, Paul G. Chrysson, James G. Chrysson, W. Michael Gilley, Matthew G. Gallins, James D. Yopp and the partnerships and limited liability companies listed therein, dated September 22, 1997 (filed as Exhibit 2.1 to Registration Statement No. 333-39803 on Form S-2, December 16, 1997, and incorporated herein by reference)
- 2.2\* Amendment to Master Agreement of Merger and Acquisition dated September 22, 1997, by and among BNP Residential Properties, Inc., BNP Residential Properties Limited Partnership, Paul G. Chrysson, James G. Chrysson, W. Michael Gilley, Matthew G. Gallins, James D. Yopp, and the partnerships and limited liability companies listed therein, dated November 3, 1997 (filed as Exhibit 2.3 to BNP Residential Properties, Inc. Current Report on Form 8-K dated December 1, 1997, and incorporated herein by reference)
- 3.1\* Articles of Incorporation (filed as Exhibit 3.1 to BNP Residential Properties, Inc., Current Report on Form 8-K dated March 17, 1999, and incorporated herein by reference)
- 3.2\* Articles Supplementary, Classifying and Designating 909,090 Shares of Series B Cumulative Convertible Preferred Stock, dated December 28, 2001 (filed as Exhibit 3.1 to BNP Residential Properties, Inc. Current Report on Form 8-K dated December 28, 2001, and incorporated herein by reference)
- 3.3\* Amended and Restated By-Laws adopted May 20, 2004 (filed as Exhibit 3.1 to BNP Residential Properties, Inc., Current Report on Form 8-K dated July 14, 2004, and incorporated herein by reference)
- 4.1\* Rights Agreement, dated March 18, 1999, between the Company and First Union National Bank (filed as Exhibit 4 to BNP Residential Properties, Inc. Current

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- 4.2\* Report on Form 8-K dated March 17, 1999, and incorporated herein by reference)  
Registration Rights Agreement By and Among BNP Residential Properties, Inc. and Preferred Investment I, LLC, dated December 28, 2001 (filed as Exhibit 4 to BNP Residential Properties, Inc. Current Report on Form 8-K dated December 28, 2001, and incorporated herein by reference)
- 10.1 Employment Agreement dated August 1, 2005, between BNP Residential Properties, Inc. and Philip S. Payne
- 10.2 Employment Agreement dated August 1, 2005, between BNP Residential Properties, Inc. and D. Scott Wilkerson
- 10.3 Employment Agreement dated August 1, 2005, between BNP Residential Properties, Inc. and Pamela B. Bruno
- 10.4 Employment Agreement dated August 1, 2005, between BNP Residential Properties, Inc. and Eric S. Rohm
- 10.5\* Second Amended and Restated Agreement of Limited Partnership of BNP Residential Properties Limited Partnership dated as of March 17, 1999 (filed as Exhibit 10.1 to the company's Annual Report on Form 10-K for the year ended December 31, 1998, and incorporated herein by reference)
- 10.6\* Amendment to Second Amended and Restated Agreement of Limited Partnership of BNP Residential Properties Limited Partnership, dated December 28, 2001 (filed as Exhibit 10.1 to BNP Residential Properties, Inc. Current Report on Form 8-K dated December 28, 2001, and incorporated herein by reference)
- 10.7\* Investment Agreement By and Between BNP Residential Properties, Inc. and Preferred Investment I, LLC, dated December 28,

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Exhibit No.

- 2001 (filed as Exhibit 10.2 to BNP Residential Properties, Inc. Current Report on Form 8-K dated December 28, 2001, and incorporated herein by reference)
- 10.8\* Amended and Restated Master Lease Agreement dated December 21, 1995, between BNP Residential Properties, Inc. and Boddie-Noell Enterprises, Inc. (filed as Exhibit 10.1 to BNP Residential Properties, Inc. Annual Report on Form 10-K dated December 31, 1995, and incorporated herein by reference)
- 10.9\* Amended and Restated 1994 Stock Option and Incentive Plan (filed as Exhibit 10.1 to BNP Residential Properties, Inc. Current Report on Form 8-K dated May 19, 2005 and incorporated by reference herein)
- 10.10\* Purchase Agreement by and among BNP Residential Properties, Inc. and Purchasers for 1,175,519 shares of common stock, dated as of February 17, 2004 (filed as Exhibit 10.1 to BNP Residential Properties, Inc. Current Report on Form 8-K dated February 23, 2004, and incorporated herein by reference)
- 10.11\* Purchase Agreement by and among BNP Residential Properties, Inc. and Purchasers for 1,420,000 shares of common stock, dated as of July 14, 2004 (filed as Exhibit 10.1 to BNP Residential Properties, Inc. Current Report on Form 8-K dated July 14, 2004, and incorporated herein by reference)
- 10.12\* Exchange Agreement among BNP Residential Properties, Inc., BNP Residential Properties Limited Partnership, and Beach Investment Properties, LLC and members thereof, dated as of December 7, 2004 (filed as Exhibit 10.9 to BNP Residential Properties, Inc. Annual Report on Form 10-K for the year ended December 31, 2004, and incorporated herein by reference)
- 10.13\* Exchange Agreement among BNP Residential Properties, Inc., BNP Residential Properties Limited Partnership, and Timberline Ventures, LLC and members thereof, dated as of December 7, 2004 (filed as Exhibit 10.10 to BNP Residential Properties, Inc. Annual Report on Form 10-K for the year ended December 31, 2004, and incorporated herein by reference)
- 10.14\* Exchange Agreement among BNP Residential Properties, Inc., BNP Residential Properties Limited Partnership, and Laurel Springs II, LLC and members thereof,

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|        |  |
|--------|--|
|        | dated as December 7, 2004 (filed as Exhibit 10.11 to BNP Residential Properties, Inc. Annual Report on Form 10-K for the year ended December 31, 2004, and incorporated herein by reference)   |
| 10.15* | Exchange Agreement among BNP Residential Properties, Inc., BNP Residential Properties Limited Partnership, and Salem Ridge/Shugart, LLC and members thereof, dated as of December 7, 2004 (filed as Exhibit 10.12 to BNP Residential Properties, Inc. Annual Report on Form 10-K for the year ended December 31, 2004, and incorporated herein by reference) |
| 21     | Subsidiaries of the Registrant   |
| 23.1   | Consent of Grant Thornton LLP  |
| 23.2   | Consent of Ernst & Young LLP   |
| 31.1   | Rule 13a-14(a)/15d-14(a) Certification by Chairman   |
| 31.2   | Rule 13a-14(a)/15d-14(a) Certification by Chief Executive Officer  |
| 31.3   | Rule 13a-14(a)/15d-14(a) Certification by Chief Financial Officer  |
| 32.1   | Section 1350 Certification by Chairman, Chief Executive Officer, and Chief Financial Officer   |

\* Incorporated herein by reference