AGREE REALTY CORP
Form 10-Q
November 08, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

Mark One

þ **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the quarterly period ended September 30, 2007

OR

o **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 1-12928
Agree Realty Corporation

(Exact name of registrant as specified in its charter)

Maryland	**38-3148187**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
31850 Northwestern Highway, Farmington Hills, Michigan	**48334**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code: (248) 737-4190

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 þ No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer o Accelerated Filer þ Non-Accelerated Filer o

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

As of November 7, 2007, the Registrant had 7,751,746 shares of common stock, $0.0001 par value, outstanding.

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Agree Realty Corporation
Consolidated Balance Sheets (Unaudited)

	September 30, 2007	December 31, 2006
Assets		
Real Estate Investments		
Land	**$ 81,868,958**	$ 77,536,458
Buildings	**193,827,554**	189,117,421
Property under development	**4,524,364**	1,593,828
	280,220,876	268,247,707
Less accumulated depreciation	**(52,020,712)**	(48,352,753)
Net real estate investments	**228,200,164**	219,894,954
Cash and Cash Equivalents	**146,354**	463,730
Accounts Receivable Tenants, net of allowance of $20,000 for possible losses at September 30, 2007 and December 31, 2006	**337,595**	732,141
Unamortized Deferred Expenses		
Financing costs, net of accumulated amortization of $4,620,272 and $4,482,272 at September 30, 2007 and December 31, 2006	**881,905**	1,019,905
Leasing costs, net of accumulated amortization of $703,053 and $665,811 at September 30, 2007 and December 31, 2006	**404,095**	421,229
Other Assets	**822,517**	982,640
	$ 230,792,630	$ 223,514,599

See accompanying notes to consolidated financial statements.

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Agree Realty Corporation
Consolidated Balance Sheets (Unaudited)

	September 30, 2007	December 31, 2006
Liabilities and Stockholders Equity		
Mortgages Payable	**$ 46,424,292**	$ 48,291,247
Notes Payable	**30,150,000**	20,500,000
Dividends and Distributions Payable	**4,124,455**	4,111,807
Deferred Revenue	**11,586,793**	12,103,954
Accrued Interest Payable	**356,641**	239,318
Accounts Payable		
Capital expenditures	**1,320,612**	766,378
Operating	**353,093**	1,140,617
Tenant Deposits	**64,085**	64,085
Total Liabilities	**94,379,971**	87,217,406
Minority Interest	**5,829,486**	5,878,593
Stockholders Equity		
Common stock, $0.0001 par value; 20,000,000 shares authorized, 7,751,746 and 7,750,496 shares issued and outstanding	**775**	775
Additional paid-in capital	**142,013,723**	141,276,763
Deficit	**(11,431,325)**	(10,858,938)
Total Stockholders Equity	**130,583,173**	130,418,600
	$ 230,792,630	$ 223,514,599

See accompanying notes to consolidated financial statements.

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Agree Realty Corporation
Consolidated Balance Sheets (Unaudited)

	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006
Revenues		
Minimum rents	**$ 7,754,457**	$ 7,452,909
Percentage rents	**13,778**	13,606
Operating cost reimbursements	**681,445**	638,900
Other income	**24**	8,545
Total Revenues	**8,449,704**	8,113,960
Operating Expenses		
Real estate taxes	**467,714**	449,823
Property operating expenses	**380,541**	389,237
Land lease payments	**168,550**	195,465
General and administrative	**965,942**	1,005,902
Depreciation and amortization	**1,259,462**	1,212,660
Total Operating Expenses	**3,242,209**	3,253,087
Income From Operations	**5,207,495**	4,860,873
Other (Expense)		
Interest expense, net	**(1,280,051)**	(1,156,949)
Income Before Minority Interest	**3,927,444**	3,703,924
Minority Interest	**(314,200)**	(297,797)
Net Income	**$ 3,613,244**	$ 3,406,127
Earnings Per Share Basic	**$ 0.47**	$ 0.45
Earnings Per Share Dilutive	**$ 0.47**	$ 0.44
Dividend Declared Per Share	**$ 0.49**	$ 0.49

Weighted Average Number of Common Shares Outstanding Basic	**7,643,708**	7,607,808
Weighted Average Number of Common Shares Outstanding Dilutive	**7,692,118**	7,672,549

See accompanying notes to consolidated financial statements.

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Agree Realty Corporation
Consolidated Statements of Income (Unaudited)

	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
Revenues		
Minimum rents	$ **23,084,371**	$ 22,415,582
Percentage rents	**29,804**	40,891
Operating cost reimbursements	**2,163,902**	2,060,329
Other income	**12,645**	37,026
Total Revenues	**25,290,722**	24,553,828
Operating Expenses		
Real estate taxes	**1,392,222**	1,351,988
Property operating expenses	**1,327,150**	1,317,509
Land lease payments	**507,150**	586,395
General and administrative	**2,937,604**	3,078,733
Depreciation and amortization	**3,756,111**	3,618,495
Total Operating Expenses	**9,920,237**	9,953,120
Income From Operations	**15,370,485**	14,600,708
Other (Expense)		
Interest expense, net	**(3,608,021)**	(3,449,164)
Income Before Minority Interest	**11,762,464**	11,151,544
Minority Interest	**(941,009)**	(896,588)
Net Income	$ **10,821,455**	$ 10,254,956
Earnings Per Share Basic	$ **1.42**	$ 1.35
Earnings Per Share Dilutive	$ **1.41**	$ 1.34
Dividend Declared Per Common Share	$ **1.47**	$ 1.47

Weighted Average Number of Common Shares Outstanding Basic	**7,642,924**	7,603,837
Weighted Average Number of Common Shares Outstanding Dilutive	**7,697,212**	7,666,366

See accompanying notes to consolidated financial statements

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Agree Realty Corporation
Consolidated Statements of Stockholders Equity (Unaudited)

	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Deficit
Balance, January 1, 2007	7,750,496	$775	$141,276,763	$(10,858,938)
Issuance of shares under the Equity Incentive Plan	1,250			
Vesting of restricted stock			736,960	
Dividends declared for the period January 1, 2007 to September 30, 2007				(11,393,842)
Net income for the period January 1, 2007 to September 30, 2007				10,821,455
Balance, September 30, 2007	7,751,746	$775	$142,013,723	$(11,431,325)

See accompanying notes to consolidated financial statements.

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Agree Realty Corporation
Consolidated Statements of Cash Flows (Unaudited)

	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
Cash Flows From Operating Activities		
Net income	$ 10,821,455	$ 10,254,956
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation	3,713,205	3,580,590
Amortization	180,906	130,905
Stock-based compensation	736,960	627,000
Minority interests	941,009	896,588
Decrease in accounts receivable	394,546	325,159
Decrease in other assets	109,213	357,952
Decrease in accounts payable	(787,524)	(1,022,279)
Decrease in deferred revenue	(517,161)	(517,162)
Increase in accrued interest	117,323	20,104
Increase in tenant deposits		6,078
Net Cash Provided By Operating Activities	15,709,932	14,659,891
Cash Flows From Investing Activities		
Acquisition of real estate investments (including capitalized interest of $401,000 in 2007 and $111,000 in 2006)	(10,652,557)	(4,168,937)
Net Cash Used In Investing Activities	(10,652,557)	(4,168,937)
Cash Flows From Financing Activities		
Net proceeds from the issuance of common stock		95,550
Payments of mortgages payable	(1,866,955)	(1,807,899)
Dividends and distributions paid	(12,371,310)	(12,302,459)
Line-of-credit net borrowings (payments)	9,650,000	(1,850,000)
Repayments of capital expenditure payables	(766,378)	(112,687)
Payment of leasing costs	(20,108)	(63,707)
Net Cash Used In Financing Activities	(5,374,751)	(16,041,202)
Net Decrease In Cash and Cash Equivalents	(317,376)	(5,550,248)

Cash and Cash Equivalents, beginning of period		**463,730**		5,714,540
Cash and Cash Equivalents, end of period	**$**	**146,354**	$	164,292

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Agree Realty Corporation
Consolidated Statements of Cash Flows (Unaudited)

	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
Supplemental Disclosure of Cash Flow Information		
Cash paid for interest (net of amounts capitalized)	**$ 3,378,355**	$ 3,337,297
Supplemental Disclosure of Non-Cash Transactions		
Dividends and distributions declared and unpaid	**$ 4,124,455**	$ 4,110,764
Shares issued under Equity Incentive Plan	**$ 40,062**	$ 149,989
Real estate investments financed with accounts payable	**$ 1,320,612**	$ 864,778

See accompanying notes to consolidated financial statements.

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Agree Realty Corporation
Notes to Consolidated Financial Statements

1. Basis of Presentation

The accompanying unaudited consolidated financial statements for the three and nine months ended September 30, 2007 and 2006 have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for audited financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The consolidated balance sheet at December 31, 2006 has been derived from the audited consolidated financial statements at that date. Operating results for the three and nine months ended September 30, 2007 are not necessarily indicative of the results that may be expected for the year ending December 31, 2007 or for any other interim period. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2006.

2. Stock Based Compensation

On January 1, 2006, Agree Realty Corporation (the n Company) adopted the provisions of Statement of Financial Accounting Standards (SFAS) No. 123 (R), *Share-Based Payments* (SFAS 123R), under the modified prospective method. Under the modified prospective method, compensation cost is recognized for all awards granted after the adoption of this standard and for the unvested portion of previously granted awards that are outstanding as of the adoption date. In accordance with SFAS 123R, the Company estimates the fair value of restricted stock and stock option grants at the date of grant and amortize those amounts into expense on a straight line basis or amount vested, if greater, over the appropriate vesting period.

As of September 30, 2007, there was $2,571,447 of total unrecognized compensation costs related to the outstanding restricted shares, which is expected to be recognized over a weighted average period of 2.83 years. The Company used a 0% discount factor and forfeiture rate for determining the fair value of restricted stock. The forfeiture rate was based on historical results and trends and the Company does not consider discount rates to be material.

The holder of a restricted share award is generally entitled at all times on and after the date of issuance of the restricted shares to exercise the rights of a shareholder of the Company, including the right to vote the shares and the right to receive dividends on the shares.

	Shares Outstanding	Weighted Average Grant Date Fair Value
Unvested restricted shares at December 31, 2006	131,120	$ 29.42

Restricted shares granted	1,250		32.05
Restricted shares vested	(24,400)		24.47
Restricted shares forfeited			
Unvested restricted shares at September 30, 2007	107,970	$	30.57

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3. Earnings Per Share

Earnings per share has been computed by dividing the net income by the weighted average number of common shares outstanding. The per share amounts reflected in the consolidated statements of income are presented in accordance with SFAS No. 128 *Earnings per Share*.

The following is a reconciliation of the denominator of the basic net earnings per common share computation to the denominator of the diluted net earnings per common share computation for each of the periods presented:

	Three Months Ended September 30,	
	2007	2006
Weighted average number of common shares outstanding	**7,751,678**	7,712,828
Unvested restricted stock	**(107,970)**	(105,020)
Weighted average number of common shares outstanding used in basic earnings per share	**7,643,708**	7,607,808
Weighted average number of common shares outstanding used in basic earnings per share	**7,643,708**	7,607,808
Effect of dilutive securities:		
Restricted stock	**48,410**	63,394
Common stock options		1,347
Weighted average number of common shares outstanding used in diluted earnings per share	**7,692,118**	7,672,549

	Nine Months Ended September 30,	
	2007	2006
Weighted average number of common shares outstanding	**7,750,894**	7,708,857
Unvested restricted stock	**(107,970)**	(105,020)
Weighted average number of common shares outstanding used in basic earnings per share	**7,642,924**	7,603,837
Weighted average number of common shares outstanding used in basic earnings per share	**7,642,924**	7,603,837
Effect of dilutive securities:		
Restricted stock	**54,288**	61,244
Common stock options		1,285
Weighted average number of common shares outstanding used in diluted earnings per share	**7,697,212**	7,666,366

4. Recent Accounting Pronouncements

In June 2006, the Financial Accounting Standards Board (the FASB) issued FASB Interpretation 48, *Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109* (FIN 48), to clarify the accounting treatment for uncertain income tax positions when applying FASB Statement No. 109, *Accounting for Income Taxes.* This interpretation prescribes a financial statement recognition threshold and measurement attribute for any tax position taken or expected to be taken in a tax return. The interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. Effective January 1, 2007, the Company adopted FIN 48. Upon adoption and as of September 30, 2007, there was no unrecognized income tax benefit and the adoption of FIN 48 had no effect on stockholders equity. The Company expects no significant increase or decrease in unrecognized tax benefits due to changes in tax positions within one year of September 30, 2007. The Company recognizes accrued interest and penalties related to uncertain tax positions in income tax expense. At January 1, 2007 and September 30, 2007, the Company had accrued zero for the payment of tax related interest and penalties and there was no tax interest or penalties recognized in the statements of operations for the three and nine months ended September 30, 2007. The Company s federal, state and local tax returns for fiscal years 2003-2006 remain subject to examination.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (SFAS No. 157). This statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles (GAAP) and expands the disclosures about fair value measurements. SFAS No. 157 applies to other accounting pronouncements that require or permit fair value measurements. The definition focuses on the price that would be received to sell the asset or paid to transfer the liability at the measurement date (an exit price) and not the price that would be paid to acquire the asset or received to assume the liability at the measurement date (an entry price). This statement also emphasizes that fair value is a market-based measurement, not an entity specific measurement, and subsequently a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. The statement also clarifies the market participant assumptions about risk and the effect of a restriction on the sale or use of an asset. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. This statement will be applied prospectively as of the beginning of the fiscal year in which this statement is initially applied. A limited form of retrospective application of SFAS No. 157 is allowed for certain financial instruments. The Company is currently evaluating the provisions of SFAS No. 157 to determine the potential impact, if any, the adoption of SFAS No. 157 will have on the Company s financial position or results of operations.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS No. 159). This statement permits companies and not-for-profit organizations to make a one-time election to carry eligible types of financial assets and liabilities at fair value, even if fair value measurement is not required under GAAP. SFAS 159 is effective for fiscal years beginning after November 15, 2007. The Company is currently evaluating the provisions of SFAS No. 159 to determine the potential impact, if any, the adoption of SFAS No. 159 will have on the Company s financial position or results of operations.

5. Other Taxes

In July 2007, the State of Michigan signed into law the Michigan Business Tax Act, replacing the Michigan single business tax with a business income tax and modified gross receipts tax. These new taxes take effect on January 1, 2008, and, because they are based on or derived from income-based measures, the provisions of SFAS No. 109, *Accounting for Income Taxes*, apply as of the enactment date. In September 2007, the State of Michigan also enacted a new services tax law that takes effect on December 1, 2007. There is substantial uncertainty as to the applicability of the new law to certain of the Company s transactions and services, as well as the treatment of various items in the computation of the tax. The Company is currently evaluating the possible effects, if any, of the new taxes on future results of operations and closely monitoring local efforts aimed at clarifying, amending, and/or repealing the law.

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ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements

Management has included herein certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities and Exchange Act of 1934, as amended (the Exchange Act). These forward-looking statements represent our expectations, plans and beliefs concerning future events and may be identified by terminology such as anticipate, estimate, should, expect, believe, intend and expressions. Although the forward-looking statements made in this report are based on good faith beliefs, reasonable assumptions and our best judgment reflecting current information, certain factors could cause actual results to differ materially from such forward looking statements, including but not limited to; the effect of economic and market conditions; risks that our acquisition and development projects will fail to perform as expected; financing risks, such as the inability to obtain debt or equity financing on favorable terms; the level and volatility of interest rates; loss or bankruptcy of one or more of our major retail tenants; a failure of our properties to generate additional income to offset increases in operating expenses; and other factors discussed elsewhere in this report and our other filings with the Securities and Exchange Commission, including our annual report on Form 10-K for the fiscal year ended December 31, 2006. Given these uncertainties, you should not place undue reliance on our forward-looking statements. Except as required by law, we assume no obligation to update these forward looking statements, even if new information becomes available in the future.

Overview

Agree Realty Corporation is a fully-integrated, self-administered and self-managed real estate investment trust (REIT) focused primarily on the ownership, development and management of retail properties net leased to national tenants. We were formed in December 1993 to continue and expand the business founded in 1971 by our current President and Chairman, Richard Agree. We specialize in developing retail properties for national tenants who have executed long-term net leases prior to the commencement of construction. As of September 30, 2007, approximately 89% of our annualized base rent was derived from national tenants. All of our freestanding property tenants and the majority of our community shopping center tenants have triple-net leases, which require the tenant to be responsible for property operating expenses, including property taxes, insurance and maintenance. We believe this strategy provides a generally consistent source of income and cash for distributions.

As of September 30, 2007, our portfolio consisted of 61 properties, located in 15 states containing an aggregate of approximately 3.4 million square feet of gross leasable area (GLA). As of September 30, 2007, our portfolio included 49 freestanding net leased properties and 12 community shopping centers that were 99.7% leased in aggregate. As of September 30, 2007, approximately 67% of our annualized base rent was derived from our top three tenants: Borders Group, Inc. 32%; Walgreen Co. (Walgreens) 23% and Kmart Corporation 12%.

We expect to continue to grow our asset base primarily through the development of retail properties that are pre-leased on a long-term basis to national tenants. We focus on development because we believe, based on the historical returns we have been able to achieve, it generally provides us a higher return on investment than the acquisition of similarly located properties and does not entail the risks associated with speculative development. Since our initial public offering in 1994, we have developed 48 of our 61 properties, including 36 of our 49 freestanding properties and all 12 of our community shopping centers. As of September 30, 2007, the properties that we developed accounted for 82.8% of our annualized base rent. We expect to continue to expand our tenant relationships and diversify our tenant base to include other quality national tenants.

During October 2007, we announced that we would develop two additional projects located in Marion County, Florida and Shelby Township, Michigan, respectively. Budgeted costs for the Florida and Michigan developments are $3.5 million and $2.5 million, respectively, and the developments are expected to be completed during the 2nd quarter of

2008. During October 2007, we also completed the sale of our interest in a contract to acquire a 14.9 acre parcel of land to a national home improvement superstore. The transaction resulted in a gain of approximately $1.5 million.

Our assets are held by, and all operations are conducted through, Agree Limited Partnership (the Operating Partnership), of which Agree Realty Corporation is the sole general partner and held a 92.01% and 92.00% interest as of September 30, 2007 and December 31, 2006, respectively. We are operating so as to qualify as a REIT for federal income tax purposes.

The following should be read in conjunction with the Consolidated Financial Statements of Agree Realty Corporation, including the respective notes thereto, which are included in this Form 10-Q.

Recent Accounting Pronouncements

In June 2006, the FASB issued FASB Interpretation 48, *Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109* (FIN 48), to clarify the accounting treatment for uncertain income tax positions when applying FASB Statement No. 109, *Accounting for Income Taxes.* This interpretation prescribes a financial statement recognition threshold and measurement attribute for any tax position taken or expected to be taken in a tax return. The interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. Effective January 1, 2007, we adopted FIN 48. Upon adoption and as of September 30, 2007, there was no unrecognized income tax benefit and the adoption of FIN 48 had no effect on stockholders equity. We do not expect any significant increase or decrease in unrecognized tax benefits due to changes in tax positions within one year of September 30, 2007. We recognize accrued interest and penalties related to uncertain tax positions in income tax expense. At January 1, 2007 and September 30, 2007, we had accrued zero for the payment of tax related interest and penalties and there was no tax interest or penalties recognized in the statements of operations for the three and nine months ended September 30, 2007. Our federal, state and local tax returns for fiscal years 2003-2006 remain subject to examination.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (SFAS No. 157). This statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles (GAAP) and expands the disclosures about fair value measurements. SFAS No. 157 applies to other accounting pronouncements that require or permit fair value measurements. The definition focuses on the price that would be received to sell the asset or paid to transfer the liability at the measurement date (an exit price) and not the price that would be paid to acquire the asset or received to assume the liability at the measurement date (an entry price). This statement also emphasizes that fair value is a market-based measurement, not an entity specific measurement, and subsequently a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. The statement also clarifies the market participant assumptions about risk and the effect of a restriction on the sale or use of an asset. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. This statement will be applied prospectively as of the beginning of the fiscal year in which this statement is initially applied. A limited form of retrospective application of SFAS No. 157 is allowed for certain financial instruments. We are currently evaluating the provisions of SFAS No. 157 to determine the potential impact, if any, the adoption of SFAS No. 157 will have on our financial position or results of operations.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS No. 159). This statement permits companies and not-for-profit organizations to make a one-time election to carry eligible types of financial assets and liabilities at fair value, even if fair value measurement is not required under GAAP. SFAS 159 is effective for fiscal years beginning after November 15, 2007. We are currently evaluating the provisions of SFAS No. 159 to determine the potential impact, if any, the adoption of SFAS No. 159 will have on our financial position or results of operations.

Critical Accounting Policies

Critical accounting policies are those that are both significant to the overall presentation of our financial condition and results of operations and require management to make difficult, complex or subjective judgments. For example, significant estimates and assumptions have been made with respect to revenue recognition, capitalization of costs related to real estate investments, potential impairment of real estate investments, operating cost reimbursements, and taxable income.

Minimum rental income attributable to leases is recorded when due from tenants. Certain leases provide for additional percentage rents based on tenants sales volumes. These percentage rents are recognized when determinable by us. In addition, leases for certain tenants contain rent escalations and/or free rent during the first several months of the lease term; however such amounts are generally not material.

Real estate assets are stated at cost less accumulated depreciation. All costs related to planning, development and construction of buildings prior to the date they become operational, including interest and real estate taxes during the construction period, are capitalized for financial reporting purposes and recorded as property under development until construction has been completed. Subsequent to the completion of construction, expenditures for property maintenance are charged to operations as incurred, while significant renovations are capitalized. Depreciation of the buildings is recorded in accordance with the straight-line method using an estimated useful life of 40 years.

In determining the fair value of real estate investments, we consider future cash flow projections on a property by property basis, current interest rates and current market conditions of the geographical location of each property.

Substantially all of our leases contain provisions requiring tenants to pay as additional rent a proportionate share of operating expenses (operating cost reimbursements) such as real estate taxes, repairs and maintenance, insurance, etc. The related revenue from tenant billings is recognized in the same period the expense is recorded.

We have elected to be taxed as a REIT under the Internal Revenue Code of 1986, as amended (the Code), commencing with our 1994 tax year. As a result, we are not subject to federal income taxes to the extent that we distribute annually at least 90% of our REIT taxable income to our stockholders and satisfy certain other requirements defined in the Code. Accordingly, no provision was made for federal income taxes in the accompanying consolidated financial statements.

Comparison of Three Months Ended September 30, 2007 to Three Months Ended September 30, 2006

Minimum rental income increased $301,000, or 4%, to $7,754,000 in 2007, compared to $7,453,000 in 2006. The increase was primarily the result of the development of a Walgreens at our Capital Plaza shopping center in December 2006, the acquisition of a Rite Aid drug store in Summit Township, Michigan in September 2006, and the development of a Walgreens in Livonia, Michigan which opened in June of 2007.

Percentage rental income remained constant at $14,000 in 2007 and 2006.

Operating cost reimbursements increased $42,000, or 7%, to $681,000 in 2007, compared to $639,000 in 2006. Operating cost reimbursements increased due to the increase in property operating expenses as explained below and a higher recovery ratio.

Other income decreased $9,000, to $-0- in 2007.

Real estate taxes increased $18,000, or 4%, to $468,000 in 2007, compared to $450,000 in 2006. The increase was the result of general assessment adjustments.

Property operating expenses (shopping center maintenance, snow removal, insurance and utilities) decreased $8,000, or 2%, to $381,000 in 2007 compared to $389,000 in 2006. The net decrease was the result of: a decrease in shopping

Agree Realty Corporation

center maintenance costs of ($6,000); an increase in utility costs of $4,000; and a decrease in insurance costs of ($6,000) in 2007 versus 2006.

Land lease payments decreased $26,000, or 14%, to $169,000 in 2007 compared to $195,000 in 2006. The decrease was the result of our purchase of the fee interest in the land located at our Lawrence, Kansas property previously leased.

General and administrative expenses decreased by $40,000, or 4%, to $966,000 in 2007, compared to $1,006,000 in 2006. The net decrease was the result of increased compensation related expenses as a result of: an increase in salaries and the value of employee stock awards of $44,000; a decrease in contracted services to investigate development opportunities of ($24,000); a decrease in legal and auditing costs of ($44,000); and a decrease in property related expenses of ($16,000). General and administrative expenses as a percentage of total rental income (minimum and percentage rents) decreased from 13.5% for 2006 to 12.4% for 2007.

Depreciation and amortization increased $46,000, or 4%, to $1,259,000 in 2007, compared to $1,213,000 in 2006. The increase was the result of the development and acquisition of two properties in 2006 and the development of one property in 2007.

Interest expense increased $123,000, or 11%, to $1,280,000 in 2007, from $1,157,000 in 2006. The increase in interest expense resulted from increased borrowings to fund the development and acquisition of the two properties in 2006 and the development of one property in 2007.

Our income before minority interest increased $223,000, or 6%, to $3,927,000 in 2007 from $3,704,000 in 2006 as a result of the foregoing factors.

Comparison of Nine Months Ended September 30, 2007 to Nine Months Ended September 30, 2006

Minimum rental income increased $668,000, or 3%, to $23,084,000 in 2007, compared to $22,416,000 in 2006. The increase was primarily the result of the development of a Walgreens at our Capital Plaza shopping center in December 2006,; the acquisition of a Rite Aid drug store in Summit Township, Michigan in September 2006 and the development of a Walgreens in Livonia, Michigan which opened in June 2007.

Percentage rental income decreased $11,000, to $30,000 in 2007, compared to $41,000 in 2006. The decrease was the result of decreased tenant sales.

Operating cost reimbursements increased $104,000, or 5%, to $2,164,000 in 2007, compared to $2,060,000 in 2006. Operating cost reimbursements increased due to the increase in property operating expenses as explained below and a higher recovery ratio.

Other income decreased $24,000 to $13,000 in 2007, compared to $37,000 in 2006.

Real estate taxes increased $40,000, or 3%, to $1,392,000 in 2007, compared to $1,352,000 in 2006. The increase was the result of general assessment adjustments.

Property operating expenses (shopping center maintenance, snow removal, insurance and utilities) increased $9,000, or 1%, to $1,327,000 in 2007 compared to $1,318,000 in 2006. The net increase was the result of: decreased shopping center maintenance costs of ($6,000); an increase in snow removal costs of $5,000; an increase in utility costs of $12,000; and a decrease in insurance costs of ($2,000) in 2007 versus 2006.

Land lease payments decreased $79,000, or 14%, to $507,000 in 2007 compared to $586,000 in 2006. The decrease was the result of our purchase of the fee interest in the land located at our Lawrence, Kansas property previously leased.

General and administrative expenses decreased by $141,000, or 5%, to $2,938,000 in 2007, compared to $3,079,000 in 2006. The net decrease was the result of increased compensation related expenses as a result of: an increase in salaries and the value of employee stock awards of $144,000; a decrease in contracted services to investigate development opportunities of ($51,000); a decrease in legal and auditing costs of ($157,000); and a decrease in property related expenses of ($77,000). General and administrative expenses as a percentage of total rental income decreased from 13.7% for 2006 to 12.7% for 2007.

Depreciation and amortization increased $138,000, or 4%, to $3,756,000 in 2007, compared to $3,618,000 in 2006. The increase was the result of the development and acquisition of two properties in 2006 and the development of one property in 2007.

Interest expense increased $159,000, or 5%, to $3,608,000 in 2007, from $3,449,000 in 2006. The increase in interest expense resulted from increased borrowings to fund the development and acquisition of the two properties in 2006 and the development of one property in 2007.

Our income before minority interest increased $610,000, or 5%, to $11,762,000 in 2007 from $11,152,000 in 2006 as a result of the foregoing factors.

Liquidity and Capital Resources

Our principal demands for liquidity are distributions to our stockholders, debt repayment, development of new properties, redevelopment of existing properties and future property acquisitions. We intend to meet our short-term liquidity requirements, including capital expenditures related to the leasing and improvement of the properties, through cash flow provided by operations and the Line of Credit and the Credit Facility. We believe that adequate cash flow will be available to fund our operations and pay dividends in accordance with REIT requirements for at least the next 12 months. We may obtain additional funds for future development or acquisitions through other borrowings or the issuance of additional shares of common stock. We intend to incur additional debt in a manner consistent with our policy of maintaining a ratio of total debt (including construction and acquisition financing) to total market capitalization of 65% or less. We believe that these financing sources will enable us to generate funds sufficient to meet both our short-term and long-term capital needs.

During the quarter ended September 30, 2007, we declared a quarterly dividend of $0.49 per share. We paid the dividend on October 11, 2007 to holders of record on September 28, 2007.

As of September 30, 2007, we had total mortgage indebtedness of $46,424,292 with a weighted average interest rate of 6.64%. This mortgage debt is all fixed rate debt.

In addition, the Operating Partnership has in place a $50 million credit facility (the Credit Facility) with LaSalle Bank, as the agent, which is guaranteed by the Company. The Credit Facility matures in November 2009 and can be extended at our option subject to specified conditions, for two additional one-year periods. Advances under the Credit Facility bear interest within a range of one-month to twelve-month LIBOR plus 100 basis points to 150 basis points or the lender s prime rate, at our option, based on certain factors such as the ratio of our indebtedness to the capital value of our properties. The Credit Facility generally is used to fund property acquisitions and development activities. As of September 30, 2007, $26,500,000 was outstanding under the Credit Facility bearing a weighted average interest rate of 6.38%.

We also have in place a $5 million line of credit (the Line of Credit), which matures in November 2009, and can be extended extended at our option subject to specified conditions for two additional one year periods. The Line of Credit bears interest at the lender s prime rate less 75 basis points or 150 basis points in excess of the one-month to twelve-month LIBOR rate, at our option. The purpose of the Line of Credit is generally to provide working capital and fund land options and start-up costs associated with new projects. As of September 30, 2007, $3,650,000 was outstanding under the Line of Credit bearing a weighted average interest rate of 7.00%.

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The following table outlines our contractual obligations for the periods presented below (in thousands).

	Total	Oct. 1, 2007 - Sep. 30, 2008	Oct. 1, 2008 - Sep. 30, 2010	Oct. 1, 2010 - Sep. 30, 2012	Thereafter
Mortgages Payable	$ 46,424	$ 2,709	$ 5,975	$ 6,818	$ 30,922
Notes Payable	30,150		30,150		
Land Lease Obligation	11,272	674	1,305	1,387	7,906
Interest Payments on Mortgages And Notes Payable	25,319	4,834	7,688	4,595	8,202
Other Long-Term Liabilities					
Total	$ 113,165	$ 8,217	$ 45,118	$ 12,800	$ 47,030

At September 30, 2007 we had four development projects under construction that will add an additional 43,290 square feet of GLA to our portfolio. The projects are expected to be completed during the fourth quarter of 2007 and the first quarter of 2008. Additional funding required to complete the projects is estimated to be $4,659,000, which is not reflected in the table above, and will be funded through advances under the Credit Facility.

During October 2007, we announced that we would develop two additional projects located in Marion County, Florida and Shelby Township, Michigan, respectively. Budgeted costs for the Florida and Michigan developments are $3.5 million and $2.5 million, respectively, and the developments are expected to be completed during the second quarter of 2008. These development projects will also be funded through advances under the Credit Facility.

During October 2007, we completed the sale of our interest in a contract to acquire a 14.9 acre parcel of land to a national home improvement superstore. The transaction resulted in a gain of approximately $1.5 million. We established a taxable REIT subsidiary to facilitate this transaction. We expect to elect to defer the recognition of the gain from the transaction for income tax purposes by making an election under Section 1031 of the Code.

We plan to begin construction of additional pre-leased developments and may acquire additional properties, which will initially be financed by the Credit Facility and Line of Credit. We will periodically refinance short-term construction and acquisition financing with long-term debt and/or equity.

Off-Balance Sheet Arrangements

We do not engage in any off-balance sheet arrangements with unconsolidated entities or financial partnerships, such as structured finance or special purpose entities, that have or are reasonably likely to have a material effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditure or capital resources.

Inflation

Our leases generally contain provisions designed to mitigate the adverse impact of inflation on net income. These provisions include clauses enabling the us to pass through to tenants certain operating costs, including real estate taxes, common area maintenance, utilities and insurance, thereby reducing the our exposure to increases in costs and operating expenses resulting from inflation. Certain of our leases contain clauses enabling us to receive percentage rents based on tenants gross sales, which generally increase as prices rise, and, in certain cases, escalation clauses, which generally increase rental rates during the terms of the leases. In addition, expiring tenant leases permit us to seek increased rents upon re-lease at market rates if rents are below the then existing market rates.

Other Taxes

In July 2007, the State of Michigan signed into law the Michigan Business Tax Act, replacing the Michigan single business tax with a business income tax and modified gross receipts tax. These new taxes take effect on January 1, 2008, and, because they are based on or derived from income-based measures, the provisions of SFAS No. 109, *Accounting for Income Taxes*, apply as of the enactment date. In September 2007, the State of Michigan also enacted a new services tax law that takes effect on December 1, 2007. There is substantial uncertainty as to the applicability of the new law to certain of the Company s transactions and services, as well as the treatment of various items in the computation of the tax. The Company is currently evaluating the possible effects, if any, of the new taxes on future results of operations and closely monitoring local efforts aimed at clarifying, amending, and/or repealing the law.

Funds from Operations

Funds from Operations (FFO) is defined by the National Association of Real Estate Investment Trusts, Inc. (NAREIT) to mean net income computed in accordance with GAAP, excluding gains (or losses) from sales of property, plus real estate related depreciation and amortization and after adjustments for unconsolidated partnerships and joint ventures. Management uses FFO as a supplemental measure to conduct and evaluate our business because there are certain limitations associated with using GAAP net income by itself as the primary measure of our operating performance. Historical cost accounting for real estate assets in accordance with GAAP implicitly assumes that the value of real estate assets diminishes predictably over time. Since real estate values instead have historically risen or fallen with market conditions, management believes that the presentation of operating results for real estate companies that use historical cost accounting is insufficient by itself.

FFO should not be considered as an alternative to net income as the primary indicator of our operating performance or as an alternative to cash flow as a measure of liquidity. Further, while we adhere to the NAREIT definition of FFO, our presentation of FFO is not necessarily comparable to similarly titled measures of other REITs due to the fact that not all REITs use the same definition.

The following tables illustrate the calculation of FFO for the three months and nine months ended September 30, 2007 and 2006:

	Three Months Ended September 30,	
	2007	2006
Net income	**$3,613,244**	$3,406,127
Depreciation of real estate assets	**1,229,708**	1,185,432
Amortization of leasing costs	**12,550**	11,751
Minority interest	**314,200**	297,797
Funds from Operations	**$5,169,702**	$4,901,107
Weighted Average Shares and Operating Partnership Units Outstanding Dilutive	**8,365,665**	8,346,096

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	Agree Realty Corporation	
	Nine Months Ended September 30,	
	2007	2006
Net income	**$10,821,455**	$10,254,956
Depreciation of real estate assets	**3,673,623**	3,540,228
Amortization of leasing costs	**37,242**	32,241
Minority interest	**941,009**	896,588
Funds from Operations	**$15,473,329**	$14,724,013
Weighted Average Shares and Operating Partnership Units Outstanding Dilutive	**8,370,759**	8,339,913

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to interest rate risk primarily through borrowing activities. There is inherent roll-over risk for borrowings as they mature and are renewed at current market rates. The extent of this risk is not quantifiable or predictable because of the variability of future interest rates and our future financing requirements.

Our interest rate risk is monitored using a variety of techniques. The table below presents the principal payments (in thousands) and the weighted average interest rates on outstanding debt, by year of expected maturity, to evaluate the expected cash flows and sensitivity to interest rate changes.

	Year Ended September 30,						
	2008	**2009**	**2010**	**2011**	**2012**	**Thereafter**	**Total**
Fixed rate debt	$2,709	$2,889	$ 3,086	$3,297	$3,521	$30,922	$46,424
Average interest rate	6.64%	6.64%	6.64%	6.64%	6.64%	6.64%	
Variable rate debt			$30,150				$30,150
Average interest rate			6.46%				

The fair value (in thousands) is estimated at $46,500 and $30,150 for fixed rate debt and variable rate debt, respectively, as of
September 30, 2007.

The table above incorporates those exposures that exist as of September 30, 2007; it does not consider those exposures or positions, which could arise after that date. As a result, our ultimate realized gain or loss with respect to interest rate fluctuations will depend on the exposures that arise during the period and interest rates.

We do not enter into financial instrument transactions for trading or other speculative purposes or to manage interest rate exposure.

As of September 30, 2007, a 10% adverse change in interest rates on the portion of our debt bearing interest at variable rates would result in an increase in interest expense of approximately $196,000.

Agree Realty Corporation

ITEM 4. CONTROLS AND PROCEDURES

At December 31, 2006, management identified the following material weakness in our internal controls:

> We lack segregation of duties in the period-end financial reporting process. Our chief financial officer is the only employee with any significant knowledge of generally accepted accounting principles. The chief financial officer is also the sole employee in charge of the general ledger (including the preparation of routine and non-routine journal entries and journal entries involving accounting estimates), the preparation of accounting reconciliations, the selection of accounting principles, and the preparation of interim and annual financial statements (including report combinations, consolidation entries and footnote disclosures) in accordance with generally accepted accounting principles.

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, as of the end of the period covered by this report.

Based on this evaluation as of September 30, 2007, and due to the material weaknesses in our internal control over financial reporting as described above, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures were not effective to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified by the SEC. There was no change in our internal control over financial reporting during the most recently completed fiscal quarter that has materially affected or is reasonably likely to materially affect our internal control over financial reporting.

Our audit committee has engaged independent third party consultants to perform periodic reviews of our financial reporting closing process.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are not presently involved in any litigation nor, to our knowledge, is any other litigation threatened against us, except for routine litigation arising in the ordinary course of business which is expected to be covered by our liability insurance.

ITEM 1A. RISK FACTORS

There were no material changes in our risk factors set forth under Item 1A of Part I of our most recently filed Form 10-K.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None

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

None

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ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS

3.1	Articles of Incorporation and Articles of Amendment of the Company (incorporated by reference to Exhibit 3.1 to the Company s Registration Statement on Form S-11 (Registration Statement No. 33-73858, as amended)
3.2	Bylaws of the Company (incorporated by reference to Exhibit 3.2 to the Company s Annual Report on Form 10-K for the year ended December 31, 2006)
*31.1	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, Richard Agree, President and Chief Executive Officer
*31.2	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, Kenneth R. Howe, Vice President and Chief Financial Officer
*32.1	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, Richard Agree, President and Chief Executive Officer
*32.2	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, Kenneth R. Howe, Vice President and Chief Financial Officer

* Filed herewith

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Pursuant to the requirements 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.

Agree Realty Corporation

/s/ RICHARD AGREE

Richard Agree
President and Chief Executive Officer
(Principal Executive Officer)

/s/ KENNETH R. HOWE

Kenneth R. Howe
Vice-President and Financial Officer
(Principal Financial and Accounting Officer)

Date: November 8, 2007