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U S RESTAURANT PROPERTIES INC
Form 10-Q
November 14, 2001

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

FORM 10-Q

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

For the quarterly period ended September 30, 2001

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 1-13089

U.S. Restaurant Properties, Inc.
(Exact name of registrant as specified in its charter)

Maryland	75-2687420
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

12240 Inwood Rd., Suite 300, Dallas, Texas 75244
(Address of principal executive offices)
(Zip Code)

(972) 387-1487
(Registrant's telephone number, including area code)

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 ☐
--- ---

As of November 9, 2001, U.S. Restaurant Properties, Inc. had 18,706,033 shares of common stock, \$.001 par value per share, outstanding.

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U.S. RESTAURANT PROPERTIES, INC.

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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

U.S. RESTAURANT PROPERTIES, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

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(IN THOUSANDS, EXCEPT PER SHARE DATA)

	SEPTEMBER 30, ----- 2001 ----- (UNAUDITED)	DECEMBER ----- 2000 -----
ASSETS		
REAL ESTATE		
Property, net		
Land	\$ 185,967	\$ 203,1
Buildings and leasehold improvements	367,013	397,0
Machinery and equipment	10,852	13,6
	-----	-----
	563,832	613,8
Less: accumulated depreciation	(79,204)	(68,1
	-----	-----
	484,628	545,6
Assets held for sale	22,071	
Construction in progress	1,280	8,5
Cash and cash equivalents	25,809	5,5
Restricted cash and marketable securities	3,389	7
Rent and other receivables, net		
(includes \$4,136 and \$4,349 allowance for doubtful accounts		
at September 30, 2001 and December 31, 2000, respectively)	14,454	14,5
Prepaid expenses and other assets	843	3,0
Investments	5,479	2,7
Notes receivable, net		
(includes \$488 and \$2,167 due from related parties		
and \$6,728 and \$4,565 allowance for doubtful accounts		
at September 30, 2001 and December 31, 2000, respectively)	6,319	11,8
Mortgage loans receivable	19,067	22,6
Net investment in direct financing leases	1,497	2,7
Intangibles, net	12,954	6,9
	-----	-----
	597,790	625,0
RETAIL OPERATIONS		
Cash and cash equivalents	471	
Rent and other receivables, net	63	
Inventories	529	
Deposits and other assets	264	
	-----	-----
	1,327	
	-----	-----
TOTAL ASSETS	\$ 599,117	\$ 625,0
	=====	=====

continued on next page

See Notes to Condensed Consolidated Financial Statements.

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U.S. RESTAURANT PROPERTIES, INC. CONDENSED CONSOLIDATED BALANCE SHEETS (CONTINUED) (IN THOUSANDS, EXCEPT PER SHARE DATA)

	SEPTEMBER 30, ----- 2001 ----- (UNAUDITED)	DECEMBER 31, ----- 2000 ----- (UNAUDITED)
LIABILITIES AND STOCKHOLDERS' EQUITY		
REAL ESTATE		
Accounts payable and accrued liabilities	\$ 14,907	\$
Accrued dividends and distributions	3,778	
Unearned contingent rent	1,189	
Deferred gain on sale of property	428	
Line of credit	--	
Interest rate protection agreements at fair value	5,811	
Notes payable		
(includes \$959 due to related parties at December 31, 2000)	365,571	
Mortgage note payable	987	
Capitalized lease obligation	--	
	-----	-----
	392,671	
RETAIL OPERATIONS		
Accounts payable and accrued liabilities	1,045	
	-----	-----
TOTAL LIABILITIES	393,716	
COMMITMENTS AND CONTINGENCIES	--	
MINORITY INTEREST IN OPERATING PARTNERSHIPS	54,418	
STOCKHOLDERS' EQUITY		
Preferred stock, \$.001 par value per share; 50,000 shares authorized, Series A - 3,680 shares issued and outstanding at September 30, 2001 and December 31, 2000 (aggregate liquidation value of \$92,000)	4	
Common stock, \$.001 par value per share; 100,000 shares authorized, 18,034 and 17,417 shares issued and outstanding at September 30, 2001 and December 31, 2000, respectively	18	
Additional paid-in capital	309,174	
Excess stock, \$.001 par value per share 15,000 shares authorized, no shares issued	--	
Accumulated other comprehensive loss	(5,256)	
Loans to stockholders for common stock	(850)	
Distributions in excess of net income	(152,107)	
	-----	-----
TOTAL STOCKHOLDERS' EQUITY	150,983	
	-----	-----
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 599,117	\$
	=====	=====

See Notes to Condensed Consolidated Financial Statements.

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U.S. RESTAURANT PROPERTIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	2001	2000	2001	2000
	-----	-----	-----	-----
REAL ESTATE				
Revenues:				
Rental income	\$ 16,553	\$ 18,637	\$ 51,596	\$ 57,111
Interest income	1,265	1,396	3,946	4,000
Amortization of unearned income on direct financing leases	72	128	249	400
	-----	-----	-----	-----
Total revenues	17,890	20,161	55,791	61,611
Expenses:				
Property	559	531	1,546	1,700
Depreciation and amortization	5,499	5,983	17,361	18,900
General and administrative	1,381	1,560	6,437	6,400
Provision for doubtful accounts	1,964	285	2,914	6,400
Loss on lease resolution	410	--	410	1,300
Interest expense	5,885	7,341	19,426	22,200
Amortization of loan origination fees	637	316	4,739	900
Derivative settlement payments	518	--	1,053	--
Termination of management contract	--	670	--	(3,700)
Impairment of long-lived assets	1,042	1,899	17,091	5,200
Fair value adjustment for interest rate swap	248	--	2,607	--
	-----	-----	-----	-----
Total expenses	18,143	18,585	73,584	59,700
	-----	-----	-----	-----
Income(loss) before retail operations, gain on sale of property, minority interests and extraordinary item	(253)	1,576	(17,793)	1,900
RETAIL OPERATIONS				
Operating revenue	5,490	--	7,476	--
Operating general and administrative	(255)	--	(264)	--
Cost of sales	(4,929)	--	(6,592)	--
	-----	-----	-----	-----
Income from retail operations	306	--	620	--
	-----	-----	-----	-----
Income (loss) before gain on sale of property, minority interests and extraordinary item	53	1,576	(17,173)	1,900
Gain on sale of property	285	978	1,893	1,600
	-----	-----	-----	-----
Income (loss) before minority interests and extraordinary item	338	2,554	(15,280)	3,500
Minority interests	(1,150)	(1,141)	(3,324)	(3,100)
	-----	-----	-----	-----
Net income (loss) before extraordinary item	(812)	1,413	(18,604)	400
Loss on early extinguishment of debt	--	--	(340)	--

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Net income (loss)	(812)	1,413	(18,944)	4
Dividends on preferred stock	(1,776)	(1,776)	(5,327)	(5,327)
Net loss allocable to common stockholders	<u>\$ (2,588)</u>	<u>\$ (363)</u>	<u>\$ (24,271)</u>	<u>\$ (4,954)</u>
Basic and diluted net loss per share:				
Net loss before extraordinary item	\$ (0.14)	\$ (0.02)	\$ (1.34)	\$ (0.02)
Extraordinary item	--	--	(0.02)	--
Net loss	<u>\$ (0.14)</u>	<u>\$ (0.02)</u>	<u>\$ (1.36)</u>	<u>\$ (0.02)</u>
Weighted average shares outstanding				
Basic and diluted	17,964	15,378	17,796	15,378

See Notes to Condensed Consolidated Financial Statements.

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U.S. RESTAURANT PROPERTIES, INC. CONDENSED CONSOLIDATED STATEMENTS OF OTHER COMPREHENSIVE OPERATIONS (IN THOUSANDS) (UNAUDITED)

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	2001	2000	2001	2000
Net income (loss)	\$ (812)	\$ 1,413	\$ (18,944)	\$ 4
Cumulative effect of change in accounting for derivative instrument	--	--	(1,474)	--
Reclassification adjustment - hedge settlement	--	--	1,474	--
Change in derivatives' fair value	(3,205)	--	(3,205)	--
Unrealized gain (loss) on available-for-sale securities	(256)	(46)	(211)	--
Comprehensive income (loss)	<u>\$ (4,273)</u>	<u>\$ 1,367</u>	<u>\$ (22,360)</u>	<u>\$ 4</u>

See Notes to Condensed Consolidated Financial Statements.

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U.S. RESTAURANT PROPERTIES, INC. CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2001 (IN THOUSANDS) (UNAUDITED)

ADDITIONAL LOANS

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	PREFERRED STOCK SHARES	PAR VALUE	COMMON STOCK SHARES	PAR VALUE	PAID-IN CAPITAL	TO SHAREHOLDERS
	-----	-----	-----	-----	-----	-----
Balance at January 1, 2001	3,680	\$ 4	17,417	\$ 17	\$ 302,634	\$ (300)
Net loss						
Loans to shareholders for common stock						(550)
Cumulative effect of change in accounting for derivative instrument						
Reclassification adjustment - hedge settlement						
Proceeds from sale of common stock			469	1	4,837	
Proceeds from exercised stock options			174		2,026	
Common stock repurchased and retired			(26)		(323)	
Changes in derivatives' fair value						
Unrealized loss on available-for-sale securities						
Distributions on common stock and distributions declared						
Distributions on preferred stock						
	-----	-----	-----	-----	-----	-----
Balance at September 30, 2001	3,680	\$ 4	18,034	\$ 18	\$ 309,174	\$ (850)
	=====	=====	=====	=====	=====	=====

	TOTAL

Balance at January 1, 2001	\$ 190,325
Net loss	(18,944)
Loans to shareholders for common stock	(550)
Cumulative effect of change in accounting for derivative instrument	(1,474)
Reclassification adjustment - hedge settlement	1,474
Proceeds from sale of common stock	4,838
Proceeds from exercised stock options	2,026
Common stock repurchased and retired	(323)
Changes in derivatives' fair value	(3,205)
Unrealized loss on available-for-sale securities	(211)
Distributions on common stock and distributions declared	(17,646)
Distributions on preferred stock	(5,327)

Balance at September 30, 2001	\$ 150,983
	=====

See Notes to Condensed Consolidated Financial Statements.

U.S. RESTAURANT PROPERTIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)
(UNAUDITED)

	NINE MONTHS ENDED SEPTEMBER 30,	
	2001	2000
	-----	-----
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	\$ (18,944)	\$ 423
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	17,361	18,983
Extraordinary loss on extinguishment of debt	340	--
Amortization of loan origination fees and discounts	4,815	886
Impairment of long-lived assets	17,091	5,271
Provision for doubtful accounts	2,914	6,455
Realized and unrealized loss on trading securities and accretion of interest income	(454)	(412)
Fair value adjustment for interest rate derivatives	2,607	--
Minority interests	3,324	3,151
Gain on sale of property	(1,893)	(1,649)
Loss on sale of investments	--	816
Termination of management contract	--	(3,752)
Increase in rent and other receivables, net	(920)	(6,271)
Decrease (increase) in prepaid expenses	1,894	(300)
Increase in inventories	(529)	--
Reduction in net investment in direct financing leases	600	1,880
Increase (decrease) in accounts payable and accrued liabilities	(1,323)	961
Increase (decrease) in unearned contingent rent	106	(330)
	-----	-----
	45,933	25,689
	-----	-----
Cash provided by operating activities	26,989	26,112
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sale of property and equipment	17,121	42,319
Purchase of property	(2,547)	(14,614)
Purchase of machinery and equipment	(46)	(192)
Purchase of investments	(2,490)	--
Proceeds from sale of investments	--	259
Distributions received on investments	45	133
Decrease (increase) in restricted cash	(3,347)	12,137
Increase in mortgage notes receivable	(40)	(53)
Reduction of mortgage loans receivable principal	3,593	1,368
Increase in notes receivable	(1,429)	(7,064)
Reduction of notes receivable principal	5,522	2,330
	-----	-----
Cash provided by investing activities	16,382	36,623

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continued on next page
See Notes to Condensed Consolidated Financial Statements.

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U.S. RESTAURANT PROPERTIES, INC. CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED) (IN THOUSANDS) (UNAUDITED)

	NINE MONTHS ENDED SEPTEMBER 30, 2001 2000	
	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from line of credit	\$ --	\$ 32
Payments on line of credit	(119,036)	(72)
Distributions to minority interest	(3,639)	(4)
Cash distributions to stockholders/partners	(17,646)	(12)
Payment of preferred stock dividends	(5,327)	(5)
Increase (decrease) in accrued dividends payable	72	(5)
Proceeds from sale of stock	5,521	
Proceeds from exercised stock options	694	
Payments on notes/mortgage payable	(231,904)	
Proceeds from notes/mortgage payable	360,700	
Loan origination fees	(11,712)	
Payments on capitalized lease obligations	--	
Purchase and retirement of common stock	(323)	
	-----	-----
Cash flows used in financing activities	(22,600)	(69)
	-----	-----
Increase (decrease) in cash and cash equivalents	20,771	(6)
Cash and cash equivalents at beginning of period	5,509	9
	-----	-----
Cash and cash equivalents at end of period	\$ 26,280	\$ 3
	=====	=====
SUPPLEMENTAL DISCLOSURE:		
Interest paid during the period	\$ 19,248	\$ 21
	=====	=====
NON-CASH INVESTING ACTIVITIES:		
Deferred gain of repossessed property	\$ --	\$
Transfer of property from capitalized lease to property and equipment	657	
Unrealized gain (loss) on investments classified as available for sale	(211)	
Notes received on sale of property	1,033	1
Notes written off on repossessed property	563	
Net transfers from construction in progress to property	7,855	30
Security deposit and note receivable transferred	700	
NON-CASH FINANCING ACTIVITIES:		
Decrease in common stock dividends accrued	\$ --	\$ (5)
Fair value of stock received in exchange for investments	--	
OP units converted to common stock	--	
Account receivable conversion to note receivable	124	

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Common stock grant
Loan to shareholder for purchase of common stock

98
550

See Notes to Condensed Consolidated Financial Statements.

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U.S. RESTAURANT PROPERTIES, INC. NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. INTERIM UNAUDITED FINANCIAL INFORMATION

U.S. Restaurant Properties, Inc. (the "Company") is a self-administered and self-managed real estate investment trust ("REIT"), as defined under the Internal Revenue Code of 1986, as amended. As noted in the Company's Annual Report on Form 10-K for the year ended December 31, 2000, the Company became the successor entity to U.S. Restaurant Properties Master L.P. (collectively with its subsidiaries, "USRP"). The business and operations of the Company are conducted primarily through U.S. Restaurant Properties Operating L.P. ("OP"). At September 30, 2001, the Company owned 99.27% of and controlled the OP. As of September 30, 2001, the Company owned 820 properties in 48 states.

The accompanying condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2000, which was filed with the Securities and Exchange Commission (the "SEC"). The results of operations for the three and nine months ended September 30, 2001, are not necessarily indicative of the results to be expected for the year ending December 31, 2001. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America, have been condensed or omitted in this report on Form 10-Q pursuant to the Rules and Regulations of the SEC. In the opinion of management, the disclosures contained in this report are adequate to make the information presented not misleading.

Accounting measurements at interim dates inherently involve greater reliance on estimates than at year end and the results of operations for the interim periods shown in this report are not necessarily indicative of results to be expected for the fiscal year. In the opinion of management, the accompanying unaudited condensed consolidated financial statements include all adjustments (of a normal recurring nature) necessary to present fairly the consolidated financial position of the Company as of September 30, 2001, the consolidated results of its operations, comprehensive operations, stockholders' equity and cash flows for the three and nine months ended September 30, 2001 and 2000.

The Company derives its revenues primarily from the leasing of its properties to operators (primarily restaurants) on a "triple net" basis. Triple net leases typically require the tenants to be responsible for property operating costs, including property taxes, insurance, maintenance and in most cases the ground lease rents where applicable. Accordingly, the accompanying condensed consolidated financial statements do not include costs for property taxes and insurance which are the responsibility of the tenants. Additionally, those amounts associated with ground lease rent expense where the tenant is responsible for the ground lease rents, have been recorded as a reduction to rent revenues with no impact on net income. For the three months ended September 30, 2001 and 2000, the Company has recorded ground lease rent payments of \$873,000 and \$1,019,000, respectively, as reductions to rent revenues. For the nine months ended September 30, 2001 and 2000, the Company has recorded ground lease rent payments of \$2,872,000 and \$3,055,000, respectively, as reductions to

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rent revenues.

The preparation of consolidated financial statements, in conformity with accounting principles generally accepted in the United States of America, requires management to make estimates and assumptions that affect reported amounts of certain assets, liabilities, revenues and expenses as of and for the reporting periods. Actual results may differ from such estimates.

Amounts in previous periods have been reclassified to conform to current period presentation.

Investments in equity securities with readily determinable fair values and debt securities are classified as either available-for-sale or trading, based on the Company's intent with respect to those securities. Such investments are classified as trading securities if those securities are held principally for the purpose of selling them in the near term. All other such investments are classified as available-for-sale. These investments are recorded at fair value on the balance sheet. Changes in fair value during the period are recorded in earnings for trading securities and in other comprehensive income for available-for-sale securities.

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Investments in equity securities that do not have readily determinable fair values are recorded using the cost method since the Company does not have the ability to exercise significant influence over the investees.

As disclosed in the Company's Form 10-K for December 31, 2000, the Company revised its accounting for contingent rent on a prospective basis, effective May 21, 1998, to account for contingent rents in accordance with the initial consensus reached in the Financial Accounting Standards Board's Emerging Issues Task Force ("EITF") Issue No. 98-9, "Accounting for Contingent Rent in Interim Financial Periods." As the Company has already complied with the requirements of accounting for contingent rents, the Company believes it is in compliance with Staff Accounting Bulletin ("SAB") No. 101, "Revenue Recognition in Financial Statements" which was effective October 1, 2000.

Statement of Financial Accounting Standards ("SFAS") No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended, was effective for the Company January 1, 2001. This standard requires that all derivative financial instruments be recognized as either assets or liabilities on the balance sheet at their fair values and that accounting for the changes in the fair values is dependent upon the intended use of the derivatives and their resulting designations. If the derivative is designated as a fair-value hedge, the changes in the fair value of the derivative and the hedged item will be recognized in earnings. If the derivative is designated as a cash flow hedge, changes in fair value of the derivative will be recorded in other comprehensive income and will be recorded in the statement of operations when the hedged item affects earnings. SFAS No. 133 defines new requirements for designation and documentation of hedging relationships as well as ongoing effectiveness assessments in order to use hedge accounting. For a derivative that does not qualify as a hedge, changes in fair value will be recognized in earnings.

The adoption of SFAS No. 133 as of January 1, 2001 resulted in the recognition of a liability of \$1,474,000, with a cumulative effect adjustment to other comprehensive income of \$1,474,000.

SFAS No. 141, "Business Combinations" is effective July 1, 2001 and prohibits pooling-of-interests accounting for acquisitions. SFAS No. 142, "Goodwill and Other Intangible Assets" is effective January 1, 2002 and specifies that

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goodwill and some intangible assets will no longer be amortized but instead will be subject to periodic impairment testing. The Company has not yet determined the effect adopting SFAS No. 142 will have on its financial statements.

SFAS No. 143, "Accounting for Asset Retirement Obligations" was issued in June 2001, and will be adopted by the Company on January 1, 2003. This Statement addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. The Company has not yet determined the effect adopting SFAS No. 143 will have on its financial statements.

SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" was issued in August 2001, and will be adopted by the Company on January 1, 2002. This Statement supersedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of", and the accounting and reporting provisions of APB Opinion No. 30, "Reporting the Results of Operations--Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions", for the disposal of a segment of a business (as previously defined in that Opinion). This Statement retains the requirements of SFAS No. 121 to (a) recognize an impairment loss only if the carrying amount of a long-lived asset is not recoverable from its undiscounted cash flows and (b) measure an impairment loss as the difference between the carrying amount and fair value of the asset. This Statement requires that a long-lived asset to be abandoned, exchanged for a similar productive asset, or distributed to owners in a spinoff be considered held and used until it is disposed of. The accounting model for long-lived assets to be disposed of by sale is used for all long-lived assets, whether previously held and used or newly acquired. That accounting model retains the requirement of SFAS No. 121 to measure a long-lived asset classified as held for sale at the lower of its carrying amount or fair value less cost to sell and to cease depreciation. Discontinued operations are no longer measured on a net realizable value basis, and future operating losses are no longer recognized before they occur. The Company has not yet determined the effect adopting SFAS No. 144 will have on its financial statements.

The Company had 18,033,756 and 17,416,672 shares of common stock outstanding as of September 30, 2001 and December 31, 2000, respectively.

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2. NET LOSS PER SHARE OF COMMON STOCK

A reconciliation of net loss per share and the weighted average shares outstanding for calculating basic and diluted net loss per share for the periods ended September 30, 2001 and 2000 is as follows:

(In thousands, except per share amounts)	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	2001	2000	2001	2000
Net income (loss) before extraordinary item	\$ (812)	\$ 1,413	\$ (18,604)	\$ 423
Dividends on preferred stock	(1,776)	(1,776)	(5,327)	(5,327)
Net loss before extraordinary item allocable to common stockholders	(2,588)	(363)	(23,931)	(4,904)
Loss on early extinguishment of debt	--	--	(340)	--

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Net loss allocable to common stockholders	\$ (2,588)	\$ (363)	\$ (24,271)	\$ (4,904)
	=====	=====	=====	=====
Basic and diluted net loss per share:				
Loss from continuing operations	\$ (0.14)	\$ (0.02)	\$ (1.34)	\$ (0.32)
Extraordinary item	--	--	(0.02)	--
	-----	-----	-----	-----
Net loss per share	\$ (0.14)	\$ (0.02)	\$ (1.36)	\$ (0.32)
	=====	=====	=====	=====
Weighted average shares outstanding				
Basic and diluted (a)	17,964	15,378	17,796	15,380
	=====	=====	=====	=====
Antidilutive securities:				
Stock options	59	--	26	4
Contingent shares	--	825	--	825
OP units	134	1,293	134	1,294
Guaranteed stock	94	226	94	226
Convertible preferred stock	3,453	3,453	3,453	3,453

(a) Basic loss per share is computed based upon the weighted average number of shares of common stock outstanding. Diluted loss per share typically reflects the dilutive effect of stock options, contingent shares, OP units, OP units and shares on which the price is guaranteed and convertible preferred stock.

3. PROPERTY

During the nine months ended September 30, 2001, the Company completed the sale and disposal of 29 properties for net cash proceeds of \$17,121,000, net of closing costs, and \$1,033,000 of notes. During the nine months ended September 30, 2001, the Company transferred \$7,855,000 of construction costs and costs associated with land on which no further development work is intended to be performed, from construction in progress to land, building and equipment.

During the three months ended March 31, 2001, the Company acquired one building from a tenant who defaulted on a land-only lease. The building was recorded at the carrying value of the receivable due from the tenant which was less than the fair market value of the building.

During the three months ended March 31, 2001, BC Oil Ventures LLC, the tenant leasing the Company's service stations and fuel terminal in Hawaii, defaulted on its monthly rent payments. After careful assessment of various factors relevant to these properties, management determined it was appropriate to sell these properties. Accordingly, the Company has classified these properties as Assets Held for Sale in the amount of \$22,071,000, and an impairment charge of \$7,743,000 was recorded to write these assets down to the estimated proceeds from the anticipated disposal of these properties net of estimated costs to sell. It is anticipated that the sale of these properties will be completed within one year. During the nine months ended September 30, 2001, the Company recognized an operating loss of \$331,000 related to these properties. In order to ensure the subtenants in these service stations

receive fuel on a regular basis, in April 2001 the Company formed a subsidiary, Fuel Supply Inc. ("FSI"), for the purpose of supplying the service stations with fuel.

Also during the first quarter of 2001, management analyzed service stations in

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Missouri, Illinois and Texas which were late paying rent and defaulting on certain lease terms for possible impairment. It was determined that 16 of these properties had carrying values in excess of their fair value. The Company recorded an impairment charge of \$7,567,000 to revalue these assets to their estimated fair value. The estimated fair values of these assets were determined by discounting the estimated cash flows of each asset. As a result of the Company's regular analysis of its investments to determine if circumstances indicate that the carrying amount of an asset may not be recoverable, additional impairment charges of \$1,781,000 for the nine months ended September 30, 2001 were recorded in order to revalue 17 other assets to their estimated fair value.

4. INVESTMENTS

The aggregate cost basis and net unrealized loss for investments classified as available-for-sale or trading at September 30, 2001 were \$6,884,000 and \$2,051,000, respectively. The net change in the unrealized fair value of available-for-sale securities is recorded as other comprehensive loss was \$211,000 for the nine months ended September 30, 2001. In addition to these investments, the Company has other investments carried at a cost basis of approximately \$646,000.

5. LINES OF CREDIT, BRIDGE LOAN AND NOTES PAYABLE

In August 2001, the Company completed a \$180,000,000 offering of Triple Net Lease Mortgage Certificates (the "Certificates") through its subsidiary U.S. Restaurant Properties, Inc. Funding 2001-A, L.P. Proceeds from the offering were primarily used to repay approximately \$156,997,000 outstanding under the Company's secured bridge facility with Bank of America and the balance of the net proceeds were used for general corporate purposes including the prepayment of the \$27,500,000 Senior B Secured Guaranteed Notes in October 2001. The Certificates amortize over 15 years, bear interest at the 30 - day LIBOR plus 48 basis points and other associated fees of approximately 52.6 basis points, and have an assumed final distribution or maturity date of August 28, 2006. At September 30, 2001, there was \$179,776,000 outstanding on the Certificates.

In January 2001, the Company entered into an Indenture agreement with Bank of America for a secured bridge facility of \$175,000,000. Proceeds from this bridge facility were used to pay-off the outstanding balance of the \$175,000,000 revolving credit line and the \$50,000,000 unsecured term loan from Credit Lyonnais. The initial term of the bridge loan matured in July 2001, and the Company entered into options to extend the facility through August 31, 2001. In August 2001, the Company paid the outstanding balance of this bridge facility with the proceeds from the offering of the Certificates.

Simultaneously with the closing of the Bank of America Indenture, the Company entered into a Credit Agreement with Bank of America for an unsecured revolving credit facility in the amount of \$7,000,000. The Credit Agreement has a term of up to two years and bears interest in tranches of 30, 60, 90 or 180 - day LIBOR contracts plus 225 basis points. The Credit Agreement also provides that up to \$3,500,000 of the facility may be used for letters of credit. Effective January 9, 2001, Bank of America issued a letter of credit in the amount of \$1,775,000 on behalf of the Company for the benefit of the preferred stockholders. There is a 2.25% fee per annum on the outstanding letter of credit. Amounts available under this facility are further reduced by the market value of the Bank of America Derivatives (as defined below) in excess of a \$2,000,000 threshold. At September 30, 2001, the availability under this facility was \$2,397,000.

On February 26, 1997, the Company issued \$40,000,000 in privately placed debt which consisted of \$12,500,000 Series A Senior Secured Guaranteed Notes with a 8.06% interest rate, which were due January 31, 2000, and \$27,500,000 Series B Senior Secured Guaranteed Notes with a 8.30% interest rate, due January 31, 2002. In January 2000, the Company paid the \$12,500,000 Series A Senior Secured

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Guaranteed Notes in full as scheduled. In October 2001, the Company prepaid the \$27,500,000 Series B Senior Secured Guaranteed Notes in full. In connection with this prepayment, the Company paid \$389,000 of make-whole fees and wrote-off \$216,000 worth of unamortized loan origination fees associated with this facility in October 2001.

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On May 12, 1998, the Company issued \$111,000,000 of seven year fixed rate senior unsecured notes payable in a private placement. The notes bear interest at the rate of 7.15% per annum and are due May 1, 2005. The net proceeds of the notes were used to repay a portion of the Company's previous revolving credit agreement and for general corporate purposes. In conjunction with the notes payable agreement, the underwriters and the Company entered into a rate lock agreement for the purpose of setting the interest rate on these notes payable. The fee paid to lock in the rate on these notes payable was approximately \$424,000 and is being amortized over the term of the notes as an adjustment to interest expense. As a result of the Bank of America Credit Agreement and certain guarantees required by it, the subsidiaries of the Company executed a Subsidiary Guaranty for the benefit of these noteholders.

On November 13, 1998, the Company issued \$47,500,000 in senior notes payable in a private placement. The notes bear interest at the rate of 8.22% per annum and are due August 1, 2003. The net proceeds were used to repay a portion of the Company's previous revolving credit agreement and for general corporate purposes. In conjunction with the notes payable agreement, the underwriters and the Company entered into a rate lock agreement for the purpose of setting the interest rate of these notes payable. The fee paid to lock in the rate on these notes payable was approximately \$406,000 and is being amortized over the term of the notes as an adjustment to interest expense. As a result of the Bank of America Credit Agreement and certain guarantees required by it, the subsidiaries of the Company executed a Subsidiary Guaranty for the benefit of these noteholders.

In April 1999, the OP entered into a credit agreement with Credit Lyonnais for an unsecured term loan of \$50,000,000. This credit facility was scheduled to mature in April 2002. On January 9, 2001, the Company paid the outstanding balance under this facility with proceeds from a bridge loan issued by Bank of America. In connection with this pay-off, the Company wrote-off \$340,000 worth of unamortized loan origination fees associated with this facility in January 2001.

6. DERIVATIVE INSTRUMENTS

Derivative financial instruments are utilized by the Company to reduce its exposure to market risks from changes in interest rates. Derivative financial instruments include interest rate swaps, and interest rate collars. During the three months ended September 30, 2001, the Company recognized \$36,000 in expense related to the ineffective portion of the interest rate swap with Credit Lyonnais. From the date of hedge designation until September 30, 2001, derivative valuation adjustments representing the effective portion of the cash flow hedges, and totaling \$3,205,000, were recognized in other comprehensive operations.

In conjunction with the completion of the Certificates offering, the Company entered into derivative instruments with Bank of America (the "Bank of America Derivatives"): an interest rate swap at a fixed rate of 3.825% for one year on a notional amount of \$50,000,000; and an interest rate collar with a floor of 4.42% and a ceiling of 6.00% for four years on a notional amount of \$80,000,000. These derivatives effectively lock in \$50,000,000 at 4.8310% (3.825% plus

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1.006%) for one year and lock in \$80,000,000 at between 5.4260% (4.42% plus 1.006%) and 7.006% (6.0% plus 1.006%) for four years.

Effective July 3, 2000, the Company entered into an interest rate swap with Credit Lyonnais for a notional amount of \$50,000,000 on which the Company pays a fixed rate of 7.05% and receives a variable rate based upon LIBOR. The interest rate swap agreement terminates in May 2003 but may be terminated earlier subject to certain restrictions. The agreement calls for the net expense or income to be paid or received quarterly. This swap was secured by six properties with an aggregate net book value of \$3,198,000 on February 23, 2001. The adoption of SFAS No. 133 as of January 1, 2001 resulted in the recognition of a liability of \$1,474,000 with a cumulative effect adjustment to other comprehensive income of \$1,474,000. The interest rate swap was designated as a cash flow hedge of the variable rate interest payments related to the Company's term loan with Credit Lyonnais. As previously discussed, during January 2001, the Company repaid the Credit Lyonnais term loan in full with proceeds from a bridge loan. Accordingly, the cash flow hedge relationship was terminated, and the \$1,474,000 in accumulated other comprehensive operations was re-classified to earnings over a six-month period, which was the anticipated term of the bridge loan. From January 2001 until August 2001, this interest rate swap was not designated as a hedge, and accordingly all changes in value, which amounted to an expense of \$1,097,000, were recorded directly to earnings. In connection with the completion of the Certificate offering, the Company designated this interest rate swap as a cash flow hedge of the variable interest rate payments on \$50,000,000 of the Certificates. The Company reduced the notional amount of this interest rate swap by \$20,000,000 in November 2001 for a cost of approximately \$1,400,000.

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7. RELATED PARTY TRANSACTIONS

In connection with Mr. Robert Stetson's resignation as Chief Executive Officer and President of the Company, the Company entered into a Settlement Agreement and Consulting Agreement with Mr. Stetson as of October 6, 1999. Pursuant to the terms of the Settlement Agreement, the Company agreed to provide Mr. Stetson one or more loans, up to the aggregate of \$800,000, for the sole purpose of acquiring shares of the Company's common stock from time to time in the open market. In March 2000, the Company advanced \$400,000 to Mr. Stetson for the purchase of the common stock of the Company. The promissory note provides for an interest rate of 7.0% per annum and quarterly payments of interest only through December 2005, with a final payment of principal and interest due in March 2006. Pursuant to the note agreement, Mr. Stetson has pledged the common stock purchased with the note proceeds as collateral for the loans. This \$400,000 note is classified as a note receivable on the balance sheet.

Effective September 22, 2000, the Company and Mr. Stetson entered into an Amendment to the Settlement Agreement that provided for two changes to the original Settlement Agreement that were completed in October 2000. First, Mr. Stetson executed a second promissory note in the amount of \$300,000 in exchange for which he received 35,037 restricted shares of USRP common stock (calculated based on a value of \$8.5625 per share). Second, the Company advanced Mr. Stetson \$75,000 under a third promissory note to be used for the sole purpose of acquiring shares of the Company's common stock in the open market. Both notes bear interest at 7.0% per annum and provide for quarterly payments of interest only through July 2006, with a final payment of principal and interest due in October 2006. In addition, both notes are secured by the restricted common stock and stock purchased with the proceeds of the notes. The \$300,000 note is classified as a loan to shareholders for common stock on the balance sheet and

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the note for \$75,000 is classified as a note receivable on the balance sheet.

On December 20, 2000, USRP/HCI Partnership 1, L.P., a subsidiary of the Company, ("HJV") made an advance to the preferred interest holder in the amount of \$700,000. Under the terms of the Advance Agreement dated December 1, 2000, the \$700,000 advance bears interest at an annual interest rate of 9.0%. This advance was paid in full as scheduled in April 2001.

In conjunction with the merger between the Company and QSV, the Company assumed a note receivable from Mr. Stetson in the amount of \$959,000 due on January 22, 2001 with an interest rate of 10.00%, as well as a note payable to Mr. Darrel L. Rolph, who was then a Director of the Company, for \$959,000 due on January 22, 2001 with an interest rate of 10.00%. Both the note receivable and note payable were paid in full on their scheduled due dates.

In connection with their resignations, Messrs. Margolin, Rolph and Rolph entered into Noncompetition and Release Agreements with the Company pursuant to which each of them agreed not to (a) submit or cause the submission of any proposals or nominations of candidates for election as directors of the Company or (b) solicit proxies from any of the Company's stockholders, in each case prior to December 31, 2003. Additionally, Mr. Margolin agreed not to directly or indirectly own, manage, control, participate in, invest in or provide consulting services to any entity or business organization that engages in or owns, invests in, manages or controls any venture engaged in the ownership, management, acquisition or development of restaurant, gasoline and convenience store properties similar to those of the Company and its affiliates for a one-year period ending March 9, 2002. As consideration under such agreement and in connection with the termination of Mr. Margolin's Employment Agreement with the Company, the Company paid Mr. Margolin \$800,000 in severance compensation which was expensed during the quarter ended March 31, 2001. Similarly, each of the Rolphs agreed not to directly or indirectly compete with the Company, other than through the restaurant operations of the Rolphs in existence as of the initial closing of the Lone Star Transaction (as defined below).

On August 27, 2001, as part of the employment arrangement with the Company's new Chief Financial Officer and Chief Operating Officer, H.G. Carrington, Jr., the Company advanced Mr. Carrington \$550,000 for the purpose of acquiring shares of the Company's common stock. The promissory note provides for an interest rate of 5.0% per annum and quarterly payments of interest only through May 2006, with a final payment of principal and interest due in August 2006. This \$550,000 note is classified as a loan to shareholders for common stock on the balance sheet.

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8. STOCKHOLDERS' EQUITY AND MINORITY INTERESTS

On January 17, 2001, the Company entered into an agreement with two affiliates of Lone Star Fund III (U.S.), L.P. ("Lone Star") providing for the sale of 1,877,935 shares of Common Stock at a price of \$10.65 per share, for aggregate consideration of \$20,000,000 (the "Lone Star Transaction"). The Lone Star Transaction will involve three or more closings: an initial closing, that occurred on March 9, 2001, at which Lone Star paid \$5,000,000 in exchange for 469,484 shares; a closing on October 30, 2001 at which Lone Star paid \$7,000,000 in exchange for 657,277 shares, and one or more subsequent closings, to occur on or before December 31, 2001, at which up to an additional 751,174 shares will be purchased. After completion of the entire Lone Star Transaction and including Lone Star's purchase of 1,856,330 shares from Fred H. Margolin, Darrel L. Rolph, David K. Rolph and their affiliates, Lone Star will be a beneficial owner of approximately 19.19% of the Company's outstanding common stock.

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The Company and each of Messrs. Margolin, Rolph and Rolph entered into a Registration Rights Agreement, dated March 9, 2001, permitting the holders thereto to request a shelf registration on Form S-3 to be filed with the Securities and Exchange Commission ("SEC") by the Company. Additionally, as a component of the Lone Star Transaction, the Company and Lone Star entered into a Registration Rights Agreement, dated March 9, 2001, granting Lone Star the ability to request a shelf registration on Form S-3.

DISTRIBUTIONS TO COMMON AND PREFERRED STOCKHOLDERS

During the nine months ended September 30, 2001, the Company declared dividends of \$17,646,000 to its common stockholders (or \$.11 per month per share of common stock) and \$5,327,000 to its preferred stockholders (or \$0.4825 per quarter per share of preferred stock).

MINORITY INTERESTS

As reported in the Company's Annual Report on Form 10-K for the year ended December 31, 2000, each OP unit represents a minority interest in the OP of the Company. Each OP unit participates in any income (loss) of the OP based on the percent ownership in the OP and receives a cash dividend in an amount equivalent to a share of common stock. Each OP unit may be exchanged at any time by the holder thereof for one share of common stock of the Company. With each exchange of outstanding OP units for common stock, the Company's percentage ownership interest in the OP, directly or indirectly, will increase. As of September 30, 2001, there were 134,344 OP units outstanding.

During 1999, the Company issued \$55,000,000 of 8.5% preferred limited partnership interests in HJV to a third party for net proceeds of \$52,793,000. Under the terms of this transaction, the preferred interest holder receives annual distributions equal to \$4,675,000, payable monthly from the cash flows of HJV. Income is allocated to the preferred interest holder equal to the amount of their distribution. The Company may be required from time to time to exchange properties that do not meet specified criteria set forth in the HJV partnership agreement.

The 134,344 OP units outstanding at September 30, 2001 and December 31, 2000 and the preferred partnership interests represent the only minority interests in subsidiaries of the Company.

Minority interest in the OP and the preferred limited partnership consist of the following at September 30, 2001 (in thousands):

Balance at January 1, 2001	\$ 54,733
Distributions paid and accrued in the period	(3,639)
Income allocated to minority interest	3,324

Balance at September 30, 2001	\$ 54,418
	=====

9. SEGMENT INFORMATION

Effective April 2001, with the formation of Fuel Supply Inc. and the commencement of retail operations, the Company now has two operating segments, real estate and retail. Operating segments are defined as components of an enterprise for which separate financial information is available that is evaluated by the chief operating decision maker(s) in deciding how to allocate resources and in assessing performance.

Real Estate. Real estate activities are comprised of property management, acquisition and development operations and related business objectives. The Company derives its revenues primarily from rental income received on its 820 restaurant and service station properties located throughout 48 states.

Retail. Commencing in April 2001, the Company formed FSI, which began retail sales. At September 30, 2001, FSI was operating ten service stations in Hawaii, thirteen service stations in Texas, seven service stations in Illinois, and two service stations in Missouri. Revenues from this segment are generated from the gasoline and convenience store sales at these 32 service stations. Intersegment revenues paid to the real estate segment from the retail segment included approximately \$41,000 of rental revenue on two service stations.

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

RESULTS OF OPERATIONS

The Company derives its revenue primarily from the leasing of its properties (primarily restaurants) to operators on a "triple net" basis. Triple net leases typically require the tenants to be responsible for property operating costs, including property taxes, insurance, maintenance, and in most cases, the ground lease rents where applicable. Approximately 50% of the Company's leases provide for a base rent plus a percentage of the sales in excess of a threshold amount. As a result, portions of the Company's revenues are a function of the number of properties in operation and their level of sales. Sales at individual properties are influenced by local market conditions, the efforts of specific operators, marketing, new product programs, support of the franchisor and the general state of the economy.

The following discussion considers the specific impact of such factors on the results of operations of the Company for the following periods.

Comparison of the three months ended September 30, 2001 to the three months ended September 30, 2000

Total revenues, including interest income, income earned on direct financing leases, and income from retail operations, in the three months ended September 30, 2001, totaled \$23,380,000, up 16.0% from the \$20,161,000 recorded for the three months ended September 30, 2000. The 11.2% decrease in rental revenues from \$18,637,000 in 2000 to \$16,553,000 in 2001 is primarily due to decreases in the number of properties owned during 2001 as compared to the same period in 2000. For the three months ended September 30, 2001, approximately 6.0% of the Company's rental revenues resulted from percentage rents (rents determined as a percentage of tenant sales), compared with 7.6% for the three months ended September 30, 2000. The decrease of 9.4% in interest income from \$1,396,000 in 2000 to \$1,265,000 in 2001 is primarily due to reduced amounts of notes and mortgages receivable and a general decline in short-term interest rates.

Retail operations commenced in April 2001. Retail income, which is comprised of revenue from operating activities, was \$5,490,000 in the three months ended September 30, 2001. Cost of sales associated with this revenue totaled \$4,929,000 and general and administrative costs associated with this revenue totaled \$255,000 in the three months ended September 30, 2001.

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Property expense for the three months ended September 30, 2001 totaled \$559,000, an increase of 5.3% when compared to the three months ended September 30, 2000. Depreciation and amortization expenses in the three months ended September 30, 2001 totaled \$5,499,000, a decrease of 8.1% when compared to the three months ended September 30, 2000. This decrease relates directly to the decrease in the number of properties owned during 2001 as compared to the same period in 2000, and properties classified as held for sale during the first quarter of 2001.

General and administrative expenses for the three months ended September 30, 2001 totaled \$1,381,000, a decrease of 11.5% when compared to the three months ended September 30, 2000. This decrease is primarily due to a reduction in legal costs associated with tenant litigation matters and reduced infrastructure costs as a result of the decrease in the number of properties managed.

Provisions for doubtful accounts for the three months ended September 30, 2001 totaled \$1,964,000 compared to \$285,000 for the three months ended September 30, 2000. During the three months ended September 30, 2001, one the Company's borrowers, Lyon's of California, Inc., filed for bankruptcy. The Company increased its reserve by \$2,225,000 to bring the total reserve for the Lyon's notes to \$2,500,000. The outstanding balance owed to the Company by Lyon's is approximately \$11,600,000. During the three months ended September 30, 2001, increased collection efforts resulted in the collection of several accounts that had previously been fully reserved. These recoveries partially offset the increase in the Lyon's reserve.

Loss on lease resolution for the three months ended September 30, 2001 totaled \$410,000. This charge relates to the resolution of leases with one tenant that involved 26 service stations in Missouri, Illinois, California and Texas. The Company, through its operating subsidiary, Fuel Supply Inc., has commenced operating and supplying fuel to 20 of these locations.

Interest expense for the three months ended September 30, 2001 totaled \$5,885,000, a decrease of 19.8% when compared to the three months ended September 30, 2000. This decrease is primarily due to lower interest rates and

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lower debt levels. Amortization of loan origination fees increased to \$637,000 in 2001 as compared to \$316,000 in 2000. This increase is due to the fees associated with the Bank of America bridge facility extensions which were expensed during the three months ended September 30, 2001. Derivative settlement payments related to the interest rate instruments with Credit Lyonnais and Bank of America increased to \$518,000.

As of December 29, 2000, all of the 825,000 contingent shares of common stock relating to the termination of the management contract with QSV had been earned and issued. As the liability had been settled in full, no amounts were recorded in the three months ended September 30, 2001. For the three months ended September 30, 2000, a non-cash accounting charge of \$670,000 was recorded. This charge represented the increase in market value of a share of common stock at September 30, 2000 compared to June 30, 2000 on the maximum total of 825,000 contingent OP units issuable to QSV pursuant to the termination agreement.

During the three months ended September 30, 2001, the Company recorded asset impairment charges of \$1,042,000 compared to a charge of \$1,899,000 in the three months ended September 30, 2000. During 2001, as part of the Company's regular analysis, the Company determined that seven properties had carrying amounts in excess of their net realizable value.

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Fair value adjustment for the interest rate swap agreement that was entered into in 2000 to hedge the variable rate interest payments related to the Company's previous term loan with Credit Lyonnais, totaled \$248,000 for the three months ended September 30, 2001. Prior to August 2001, the Company had not redesignated this interest rate swap as a hedge subsequent to the repayment of the Credit Lyonnais term loan. As a result, all changes in the fair value of the interest rate swap agreement subsequent to the Credit Lyonnais repayment and prior to August 2001 were recognized in earnings immediately. In conjunction with the closing of the Certificates, the Company redesignated this swap as a cash flow hedge of the Certificates' variable interest rate payments.

The gain on sale of properties of \$285,000 for the three months ended September 30, 2001 relates to the sale of four properties for cash of \$2,628,000 and notes of \$155,000. The gain on sale of properties of \$978,000 for the three months ended September 30, 2000 relates to the sale of 43 properties for cash of \$31,333,000 and notes of \$728,000.

Minority interest in net income was \$1,150,000 for the three months ended September 30, 2001 compared to \$1,141,000 for the three months ended September 30, 2000.

Comparison of the nine months ended September 30, 2001 to the nine months ended September 30, 2000

Total revenues, including interest income, income earned on direct financing leases, and income from retail operations, in the nine months ended September 30, 2001 totaled \$63,267,000, up 2.6% from the \$61,650,000 recorded for the nine months ended September 30, 2000. The 9.7% decrease in rental revenues from \$57,166,000 in the nine months ended September 30, 2000 to \$51,596,000 in 2001 is primarily due to decreases in the number of properties owned during 2001 as compared to the same period in 2000. For the nine months ended September 30, 2001, approximately 6.9% of the Company's rental revenues resulted from percentage rents (rents determined as a percentage of tenant sales), compared with 7.7% for the nine months ended September 30, 2000. The decrease of 1.8% in interest income from \$4,019,000 in the nine months ended September 30, 2000 to \$3,946,000 in 2001 is primarily due to reduced amounts of notes and mortgages receivable, partially offset by higher average cash balances available for short-term investment.

Retail operations commenced in April 2001. Retail income, which is comprised of revenue from operating activities, was \$7,476,000 in the nine months ended September 30, 2001. Cost of sales associated with this revenue totaled \$6,592,000 and general and administrative costs associated with this revenue totaled \$264,000 in the nine months ended September 30, 2001.

Property expense for the nine months ended September 30, 2001 totaled \$1,546,000, a decrease of 10.6% when compared to the nine months ended September 30, 2000. Depreciation and amortization expenses in the nine months ended September 30, 2001 totaled \$17,361,000, a decrease of 8.5% when compared to the nine months ended September 30, 2000. This decrease relates directly to the decrease in the number of properties owned during 2001 as compared to the same period in 2000.

General and administrative expenses for the nine months ended September 30, 2001 totaled \$6,437,000, compared to \$6,466,000 for the nine months ended September 30, 2000. During the nine months ended September 30, 2001, the

Company incurred costs of \$813,000 for severance related to the Company's former Chief Executive Officer, a provision of \$350,000 for severance related to the

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Company's former Chief Financial Officer and \$230,000 for costs associated with hiring the Company's new Chief Operating Officer/Chief Financial Officer. These costs are partially offset by decreased legal costs associated with tenant litigation matters and reduced infrastructure costs as a result of the decrease in the number of properties managed.

Provisions for doubtful accounts for the nine months ended September 30, 2001 totaled \$2,914,000 compared to \$6,455,000 for the nine months ended September 30, 2000. During the nine months ended September 30, 2001, one of the Company's borrowers, Lyon's of California, Inc. filed for bankruptcy. The Company reserved \$2,500,000 of the approximately \$11,600,000 owed to the Company by Lyon's. During the nine months ended September 30, 2000, the Company fully provided for all outstanding notes and accounts receivable due from BC Oil Ventures LLC in the amount of \$3,138,000. Additional provisions during the nine months ended September 30, 2001 and 2000 resulted from the Company's regular analysis of its receivables to determine if circumstances indicate that the carrying value of the receivable may not be recovered.

Loss on lease resolution for the nine months ended September 30, 2001 totaled \$410,000 compared to \$1,367,000 for the nine months ended September 30, 2000. The charge in 2001 relates to the resolution of leases with one tenant that involved 26 service stations in Missouri, Illinois, California and Texas. The Company, through its operating subsidiary, FSI, has commenced operating and supplying fuel to 20 of these locations. The charges in 2000 resulted in costs of \$867,000 associated with terminating the lease with an operator of 37 fast food properties. Costs of \$500,000 were incurred in the resolution of a lease with an operator of service stations in Georgia.

Interest expense for the nine months ended September 30, 2001 totaled \$19,426,000, a decrease of 12.7% when compared to the nine months ended September 30, 2000. This decrease is primarily due to lower interest rates and lower debt levels. Amortization of loan origination fees increased to \$4,739,000 in 2001 as compared to \$964,000 in 2000. This increase is due to the fees associated with the Bank of America bridge facility which were expensed over the first eight months of 2001. Derivative settlement payments related to the interest rate instruments with Credit Lyonnais and Bank of America increased to \$1,053,000.

As of December 29, 2000, all of the 825,000 contingent shares of common stock relating to the termination of the management contract with QSV had been earned and issued. As the liability had been settled in full, no amounts were recorded in the nine months ended September 30, 2001. For the nine months ended September 30, 2000, a non-cash accounting credit of \$3,752,000 was recorded. This credit represents the decline in market value of a share of common stock at September 30, 2000 compared to December 31, 1999 on the maximum total of 825,000 contingent OP units issuable to QSV pursuant to the termination agreement.

During the nine months ended September 30, 2001, the Company recorded an asset impairment charge of \$17,091,000, as compared to \$5,271,000 recorded during the nine months ended September 30, 2000. During the nine months ended September 30, 2001, BC Oil Ventures LLC, the tenant leasing the service stations and fuel terminal in Hawaii, defaulted on its monthly rent payments. After careful assessment of various factors relevant to these properties, management determined it was appropriate to sell these properties. Accordingly, the Company has classified these properties as Assets Held for Sale, and an impairment charge of \$7,743,000 was recorded to write these assets down to the estimated proceeds anticipated from the disposal of these properties net of estimated costs to sell. Also during this period, management analyzed service stations in Missouri, Illinois and Texas which were late paying rent and defaulting on certain lease terms for possible impairment. It was determined that 16 of these properties had carrying values in excess of fair value. The Company recorded an impairment charge of \$7,567,000 to revalue these assets to estimated fair value.

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The estimated fair value of these assets was determined by discounting the estimated cash flows of each asset. As a result of the Company's regular analysis of its investments to determine if circumstances indicate that the carrying amount of an asset may not be recoverable, additional impairment charges of \$1,781,000 were recorded from the revaluing of 17 other assets to their estimated fair value.

Fair value adjustment for the interest rate swap agreement for the nine months ended September 30, 2001 totaled \$2,607,000. The adoption of SFAS No. 133, as of January 1, 2001 resulted in the recognition of a liability of \$1,474,000, with a cumulative effect adjustment to other comprehensive income of \$1,474,000. The interest rate swap agreement was entered into in 2000 to hedge the variable rate interest payments related to the Company's previous term loan with Credit Lyonnais. During January 2001, the Company repaid the Credit Lyonnais term loan in full with proceeds from an eight month bridge loan. The unrealized loss on the interest rate swap included in other comprehensive income upon adoption of SFAS No. 133 was reclassified to earnings over the period of the bridge

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loan. Prior to August 2001, the Company had not redesignated this interest rate swap as a hedge subsequent to the repayment of the Credit Lyonnais term loan. As a result, all changes in the fair value of the interest rate swap agreement subsequent to the Credit Lyonnais repayment and prior to August 2001 were recognized in earnings immediately. In conjunction with the closing of the Certificates, the Company redesignated this swap as a hedge against the Certificates. Of the \$2,607,000 recorded, \$1,474,000 represents reclassification of the January 1, 2001 adjustment from other comprehensive income and \$1,133,000 represents the change in the fair value of the interest rate swap.

The gain on sale of properties of \$1,893,000 for the nine months ended September 30, 2001 relates to the sale of 26 properties for cash of \$17,121,000, net of closing costs, and notes of \$1,033,000. The gain on sale of properties of \$1,649,000 for the nine months ended September 30, 2000 relates to the sale of 62 properties for cash of \$42,319,000 and notes of \$1,233,000, and the non-renewal of ground leases.

Minority interest in net income was \$3,324,000 for the nine months ended September 30, 2001, compared to \$3,151,000 for the nine months ended September 30, 2000.

Loss on early extinguishment of debt was \$340,000 for the nine months ended September 30, 2001. On January 9, 2001, the Company paid the outstanding balance under the Credit Lyonnais facility with proceeds from a bridge loan issued by Bank of America. In connection with this pay-off, the Company wrote-off \$340,000 in unamortized loan origination fees associated with this facility.

LIQUIDITY AND CAPITAL RESOURCES

The Company's principal source of cash to meet its short-term cash requirements is rental revenues generated by the Company's properties. Cash generated by the portfolio in excess of operating and dividend payment needs is generally used to reduce amounts outstanding under the Company's credit agreements or make new property acquisitions. The Company currently has three letters of intent for acquisitions outstanding worth approximately \$19,000,000. The terms of the Company's leases ("triple net leases") generally require that the tenant is responsible for maintenance and improvements to the property. The Company is generally not required to expend funds for remodels and renovations. However, the Company expects to spend approximately \$145,000 during the remainder of this year to renovate and remodel currently owned properties.

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During the nine months ended September 30, 2001, the Company declared dividends of \$17,646,000 to its common stockholders (or \$.11 per month per share of common stock) and \$5,327,000 to its preferred stockholders (or \$0.4825 per quarter per share of preferred stock).

During the three months ended June 30, 2001, the Company was informed that two of its tenants had filed for protection under Chapter 11 of the Bankruptcy Code of the United States (the "Bankruptcy Code"). Gant Acquisition LLC ("Gant"), which leases 27 service stations in North Carolina, filed on May 21, 2001. Annual rent from these properties is approximately \$1,504,000. Vista DFW Locs, LLC (formerly VISTA Stores LLC) ("Vista"), which leases 53 FINA branded convenience stores/service stations in Texas, filed on June 29, 2001. Annual rent from these properties is approximately \$2,236,000. The rents from these properties are not delinquent and the Company does not anticipate any adverse impairment of values associated with these properties.

During the three months ended September 30, 2001, the Company was informed that one of its tenants leasing 19 casual dining restaurant properties was experiencing financial difficulties. Annual rent from these properties is approximately \$3,058,000. The Company has received only a portion of the rent from this tenant for October and November. Based on current information, the Company does not anticipate any material adverse impairment of values associated with these properties, but expects interruption of a significant portion of the rent payments for an extended period.

During October 2001, the Company was informed that one of its borrowers, Lyon's of California, Inc., had filed for protection under Chapter 11 of the Bankruptcy Code. At September 30, 2001 there was approximately \$11,600,000 due from Lyon's for which \$2,500,000 had been reserved. Interest revenue associated with these notes is approximately \$123,000 per month.

In August 2001, the Company completed a \$180,000,000 offering of Triple Net Lease Mortgage Certificates (the "Certificates") through its subsidiary U.S. Restaurant Properties, Inc. Funding 2001-A, L.P. Proceeds from the

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offering were primarily used to repay approximately \$156,997,000 outstanding under the Company's secured bridge facility with Bank of America and the balance of the net proceeds were used for general corporate purposes including the prepayment of the \$27,500,000 Senior B Secured Guaranteed Notes in October 2001. The Certificates amortize over 15 years, bear interest at the 30 - day LIBOR plus 48 basis points and other associated fees of approximately 52.6 basis points, and have an assumed final distribution or maturity date of August 28, 2006. At September 30, 2001 there was \$179,776,000 outstanding on the Certificates.

In conjunction with the completion of the offering of the Certificates, the Company entered into the Bank of America Derivatives: an interest rate swap at a fixed rate of 3.825% for one year on a notional amount of \$50,000,000 and an interest rate collar with a floor of 4.42% and a ceiling of 6.00% for four years on a notional amount of \$80,000,000. These derivatives effectively lock in \$50,000,000 at 4.8310% (3.825% plus 1.006%) for one year and lock in \$80,000,000 at between 5.4260% (4.42% plus 1.006%) and 7.006% (6.0% plus 1.006%) for four years.

In January 2001, the Company entered into a Credit Agreement with Bank of America for an unsecured revolving credit facility in the amount of \$7,000,000. The Credit Agreement has a term of up to two years and bears interest in tranches of 30, 60, 90 or 180 - day LIBOR contracts plus 225 basis points. The Credit Agreement also provides that up to \$3,500,000 of the facility may be used

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for letters of credit. Effective January 9, 2001, Bank of America issued a letter of credit in the amount of \$1,775,000 on behalf of the Company for the benefit of the preferred stockholders. There is a 2.25% fee per annum on the outstanding letter of credit. Amounts available under this facility are further reduced by the market value of the Bank of America Derivatives in excess of a \$2,000,000 threshold. At September 30, 2001, the availability under this facility was \$2,397,000.

On January 17, 2001, the Company entered into an agreement with two affiliates of Lone Star Fund III (U.S.), L.P. ("Lone Star") providing for the sale of 1,877,935 shares of Common Stock at a price of \$10.65 per share, for aggregate consideration of \$20,000,000 (the "Lone Star Transaction"). The Lone Star Transaction will involve three or more closings: an initial closing, that occurred on March 9, 2001, at which Lone Star paid \$5,000,000 in exchange for 469,484 shares; a closing on October 30, 2001 at which Lone Star paid \$7,000,000 in exchange for 657,277 shares, and one or more subsequent closings, to occur on or before December 31, 2001, at which up to an additional 751,174 shares will be purchased.

Management believes that cash flow from operations, along with the Company's ability to raise additional equity through joint ventures and anticipated sales of properties, additional proceeds from the sale of the remaining shares of common stock to Lone Star, funds available under the revolving credit facility and the Company's anticipated ability to obtain financing will provide the Company with sufficient liquidity to meet its foreseeable capital needs. However, there can be no assurance that the terms of anticipated financing will be as favorable to the Company as under the existing facilities.

FUNDS FROM OPERATIONS (FFO)

The Company believes that it computes FFO in accordance with the standards established by the National Association of Real Estate Investment Trusts ("NAREIT") in their National Policy Bulletin dated November 8, 1999, which may differ from the methodology for calculating FFO utilized by other equity REITs, and, accordingly, may not be comparable to such other REITs. The Company's FFO is computed as net income (loss) available to common stockholders (computed in accordance with accounting principles generally accepted in the United States of America), excluding real estate related depreciation and amortization, gains (or losses) from sales of property, impairment of long-lived assets, extraordinary items and items of a similar nature that are allocable to minority interest holders. The Company believes FFO is helpful to investors as a measure of the performance of an equity REIT because, along with the Company's statements of financial condition, results of operations and cash flows, it provides investors with an understanding of the ability of the Company to incur and service debt and make capital expenditures. In evaluating FFO and the trends it depicts, investors should consider the major factors affecting FFO. Growth in FFO will result from increases in revenue or decreases in related operating expenses. Conversely, FFO will decline if revenues decline or related operating expenses increase. FFO does not represent amounts available for management's discretionary use because of needed capital replacement or expansion, debt service obligation, or other commitments and uncertainties. FFO should not be considered as an alternative to net income (determined in accordance with accounting principles generally accepted in the United States of America), as an indication of the Company's financial performance, to cash flows from operating activities (determined in accordance with accounting principles generally accepted in the United States of America) or as a measure of the Company's liquidity, nor is it indicative of funds available to fund the Company's cash needs, including its ability to make distributions.

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The following table sets forth, for the three and nine months ended September 30, 2001 and 2000, the calculation of funds from operations.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2001	2000	2001	2000
	-----	-----	-----	-----
(in thousands)				
Net loss allocable to common stockholders	\$ (2,588)	\$ (363)	\$ (24,271)	\$ (4,904)
Depreciation and amortization	5,474	5,955	17,274	18,890
Gain on sale of property	(285)	(978)	(1,893)	(1,649)
Impairment of long-lived assets	1,042	1,899	17,091	5,271
Extraordinary loss	--	--	340	--
Income allocable to minority interests	(19)	(27)	(182)	(355)
	-----	-----	-----	-----
Funds from operations	\$ 3,624	\$ 6,486	\$ 8,359	\$ 17,253
	=====	=====	=====	=====

INFLATION

Some of the Company's leases are subject to adjustments for increases in the Consumer Price Index, which reduces the risk to the Company of the adverse effects of inflation. Additionally, to the extent inflation increases sales volume, percentage rents may tend to offset the effects of inflation on the Company. Because triple net leases also require the property operator to pay for some or all operating expenses, property taxes, property repair and maintenance costs and insurance, some or all of the inflationary impact of these expenses will be borne by the property operator and not by the Company.

SEASONALITY

Fast food restaurant operations historically have been seasonal in nature, reflecting higher unit sales during the second and third quarters due to warmer weather and increase leisure travel. This seasonality can be expected to cause fluctuations in the Company's quarterly revenue to the extent it earns percentage rent.

RECENTLY ISSUED ACCOUNTING STANDARDS

SFAS No. 141, "Business Combinations" is effective July 1, 2001 and prohibits pooling-of-interests accounting for acquisitions. SFAS No. 142, "Goodwill and Other Intangible Assets" is effective January 1, 2002 and specifies that goodwill and some intangible assets will no longer be amortized but instead will be subject to periodic impairment testing. The Company has not yet determined the effect adopting SFAS No. 142 will have on its financial statements.

SFAS No. 143, "Accounting for Asset Retirement Obligations" was issued in June 2001, and will be adopted by the Company on January 1, 2003. This Statement addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. The Company has not yet determined the effect adopting SFAS No. 143 will have on its financial statements.

SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" was issued in August 2001, and will be adopted by the Company on January 1, 2002. This Statement supersedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of", and the

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accounting and reporting provisions of APB Opinion No. 30, "Reporting the Results of Operations--Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions", for the disposal of a segment of a business (as previously defined in that Opinion). This Statement retains the requirements of SFAS No. 121 to (a) recognize an impairment loss only if the carrying amount of a long-lived asset is not recoverable from its undiscounted cash flows and (b) measure an impairment loss as the difference between the carrying amount and fair value of the asset. This Statement requires that a long-lived asset to be abandoned, exchanged for a similar productive asset, or distributed to owners in a spinoff be considered held and used until it is disposed of. The accounting model for long-lived assets to be disposed of by sale is used for all long-lived assets,

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whether previously held and used or newly acquired. That accounting model retains the requirement of SFAS No. 121 to measure a long-lived asset classified as held for sale at the lower of its carrying amount or fair value less cost to sell and to cease depreciation. Discontinued operations are no longer measured on a net realizable value basis, and future operating losses are no longer recognized before they occur. The Company has not yet determined the effect adopting SFAS No. 144 will have on its financial statements.

RISKS ASSOCIATED WITH FORWARD-LOOKING STATEMENTS INCLUDED IN THIS FORM 10-Q

Certain statements contained in this Form 10-Q, including without limitation statements regarding the objectives of management for future operations and statements containing the words "believe," "may," "will," "estimate," "continue," "anticipate," "intend," "expect" and similar expressions, are forward-looking statements within the meaning of the federal securities laws. Such forward-looking statements are subject to known and unknown risks, uncertainties and assumptions which may cause the Company's actual results, performance or achievements to differ materially from those anticipated or implied by the forward-looking statements. The Company disclaims any obligation to update any such statements or publicly announce any updates or revisions to any of the forward-looking statements contained herein to reflect any change in the Company's expectation with regard thereto or any change in events, conditions, circumstances or assumptions underlying such statements. Reference is hereby made to the disclosures contained in the Company's filings with the Securities and Exchange Commission, including, but not limited to, the disclosures under the heading "Risk Factors" in "Item 1. Business" of the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission on April 2, 2001.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company has limited exposure to financial market risks, including changes in interest rates and other relevant market prices, except as noted below. The Company does not have any foreign operations and thus is not exposed to foreign currency fluctuations.

An increase or decrease in interest rates would affect interest costs relating to the Company's variable rate Certificates. At September 30, 2001 there was \$179,776,000 of variable rate debt outstanding on these Certificates. The Certificates bear interest at the 30 - day LIBOR plus 100.6 basis points.

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The Company has entered into an interest rate swap effective July 3, 2000 with a notional amount of \$50,000,000. The Company will pay a fixed rate of 7.05% and receive a variable rate based upon LIBOR under this swap agreement. In August 2001, in conjunction with the completion of the Certificates offering, the Company entered into the Bank of America Derivatives: an interest rate swap at a fixed rate of 3.825% for one year on a notional amount of \$50,000,000 and an interest rate collar with a floor of 4.42% and a ceiling of 6.00% for four years on a notional amount of \$80,000,000. These derivatives effectively lock in \$50,000,000 at 4.8310% (3.825% plus 1.006%) for one year and lock in \$80,000,000 at between 5.4260% (4.42% plus 1.006%) and 7.006% (6.0% plus 1.006%) for four years. Based on the Company's variable rate debt and the derivatives designated as cash flow hedges against this debt, a 10% increase or decrease in interest rates would result in an increase or decrease in interest charges of approximately \$48,000.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

None

ITEM 2. CHANGES IN 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

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

a) Exhibits

Exhibit 2.1 - Certificate of Merger of QSV Properties, Inc. with and into U.S. Restaurant Properties, Inc. (incorporated by reference to Exhibit 2.1 to the Company's Annual Report on Form 10-K for the year ended December 31, 2000)

Exhibit 2.2 - Articles of Merger between QSV Properties, Inc. a Delaware corporation and U.S. Restaurant Properties, Inc., a Maryland corporation (incorporated by reference to Exhibit 2.2 to the Company's Annual Report on Form 10-K for the year ended December 31, 2000)

Exhibit 2.3 - Agreement of Plan of Merger (incorporated by reference to Exhibit 2.3 to the Company's Annual Report on Form 10-K for the year ended December 31, 2000)

Exhibit 3.1 - Amended and Restated Articles of Incorporation of the Company (incorporated by reference to Exhibit 3.1 to the Company's Registration Statement of Form S-3 (File No.

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333-34263))

Exhibit 3.2 - Bylaws of the Company (incorporated by reference to Exhibit 3.2 to the Company's Registration Statement on Form S-4 (File No. 333-21403))

Exhibit 4.1 - Specimen of Common Stock Certificate (incorporated by reference to Exhibit 4.1 to the Company's Registration Statement on Form S-4 (File No. 333-21403))

Exhibit 10.1 - Amended and Restated Property Management Agreement dated August 1, 2001.

Exhibit 10.2 - Amended and Restated Indenture dated August 1, 2001.

Exhibit 11.1 - Earnings per Share Computation

b) Reports on Form 8-K

No reports on Form 8-K were filed during the quarter ended September 30, 2001.

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SIGNATURE

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.

U.S. Restaurant Properties, Inc.

Dated: November 14, 2001

By: /s/ H.G. Carrington, Jr.

H.G. Carrington, Jr.
Chief Financial Officer
Chief Operating Officer
(Principal Financial Officer)

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INDEX TO EXHIBITS

EXHIBIT
NUMBER

DESCRIPTION

10.1	Amended and Restated Property Management Agreement dated August 1, 2001.
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10.2	Amended and Restated Indenture dated August 1, 2001.
11.1	Earnings per Share Computation