

CHELSEA PROPERTY GROUP INC
Form 10-K
March 03, 2004

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

FORM 10-K

**[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2003**

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 No. 1-12328

CHELSEA PROPERTY GROUP, INC.

(Exact name of registrant as specified in its charter)

Maryland

*(State or other jurisdiction
of incorporation or organization)*

22-3251332

*(I.R.S. Employer
Identification No.)*

103 Eisenhower Parkway, Roseland, New Jersey 07068

(Address of principal executive offices - zip code)

(973) 228-6111

(Registrant's telephone number, including area code)

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

| <u>Title of each class</u> | <u>Name of each exchange on which registered</u> |
|--------------------------------|--|
| Common stock, \$0.01 par value | New York Stock Exchange |

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark if the disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [x]

Indicate by check mark whether the registrant is an accelerated filer.

Yes No

Based on the closing sales price on June 30, 2003 of \$40.31 per share, the aggregate market value of the voting stock held by non-affiliates of the registrant was \$1,714,707,385.

The number of shares outstanding of the registrant's common stock, \$0.01 par value was 43,702,508 at February 17, 2004.

Documents incorporated by reference:

Portions of the registrant's definitive Proxy Statement relating to its 2004 Annual Meeting of Shareholders are incorporated by reference into Part III as set forth herein.

PART I

Item 1. Business

The Company

Chelsea Property Group, Inc. (the "Company") is a self-administered and self-managed real estate investment trust ("REIT"). The Company made its initial public offering of common stock on November 2, 1993 (the "IPO") and simultaneously became the managing general partner of CPG Partners, L.P. (the "Operating Partnership" or "OP"), a partnership that specializes in owning, developing, redeveloping, leasing, marketing and managing upscale and fashion-oriented manufacturers' outlet centers. As of December 31, 2003, the Company wholly or partially owned 60 centers in 31 states and Japan containing approximately 16.1 million square feet of gross leasable area ("GLA"), represented by more than 1,030 tenants in 3,953 stores. As of December 31, 2003, the Company's portfolio is comprised of 30 Premium Outlet centers containing 10.6 million square feet of GLA ("Premium Properties") and 30 other retail centers containing 5.5 million square feet of GLA ("Other Properties") (collectively the "Properties"). The Premium Properties, excluding properties converted to Premium during 2003, generated approximately 75% and 86% of the Company's real estate net operating income for the years ended December 31, 2003 and 2002, respectively. The Premium Properties generally are located near metropolitan areas including New York City, Los Angeles, Chicago, Boston, Washington, D.C., San Francisco, Sacramento, Atlanta, Dallas, Tokyo and Osaka, Japan, which have a population of at least one million people within a 30-mile radius, with average annual household income of greater than \$50,000. Some Premium Properties are also located within 20 miles of major tourist destinations including Palm Springs, Napa Valley, Orlando, Las Vegas and Honolulu. During 2003, the Company's domestic Premium Properties generated weighted average tenant sales of \$399 per square-foot, defined as total sales reported by tenants divided by their gross leasable area, weighted by the number of months in operation.

The Company's executive offices are located at 103 Eisenhower Parkway, Roseland, New Jersey 07068 (telephone 973-228-6111). The Company's website can be accessed at www.cpgi.com. A copy of the Company's Forms 10-K, 10-Q, 8-K and other filings can be obtained free of charge, on the Company's website. These SEC filings are added to the website as soon as reasonably practicable. The Company's Code of Ethics, and other committee charters are also listed on the website and the corporate governance principles will follow shortly. Additionally, the Company was incorporated in Maryland on August 24, 1993.

The Company is taxed as a REIT under the provisions of the Internal Revenue Code. The Company generally will not be taxed at the corporate level on income it currently distributes to its shareholders, provided it distributes at least 90% of its taxable income.

Recent Developments

Acquisitions

In June 2003, the Company purchased The Crossings Factory Stores, a 390,000 square-foot outlet center located in Tannersville, Pennsylvania, for \$111.3 million including closing costs and the assumption of a \$60.7 million 5.85% mortgage loan due 2013. In conjunction with the acquisition, the Company completed an offering of 1.2 million shares of common stock at a price of \$42.10 per share. Net proceeds after expenses of \$49.4 million were used to fund substantially the entire cash portion of the acquisition.

In August 2003, the Company acquired Las Vegas Outlet Center, a 477,000 square-foot outlet center in Las Vegas, Nevada, for \$104.0 million including the assumption of a \$24.4 million 8.12% mortgage loan due 2012. As part of the transaction, the Company also acquired Lakeland Factory Outlet Mall, a 319,000 square-foot outlet center near Memphis, Tennessee for an additional \$3.5 million. The Lakeland property is being marketed for sale. The approximately \$84.0 million cash portion of the overall transaction was financed with a \$100.0 million one-year term loan at an annual interest rate of LIBOR plus 0.80% that is due on July 31, 2004 and extendible for six months until January 31, 2005, at the Company's option. The LIBOR rate spread ranges from 0.70% to 1.35% depending on the Company's Senior Debt rating. Surplus proceeds from the financing of approximately \$16.0 million were used for general corporate purposes.

Recent Developments (continued)

Chelsea Interactive

At December 31, 2002, the Company recognized an impairment loss equal to the net book value of its investment in Chelsea Interactive. The Company believes that it will not be able to recover the net book value of its investment in Chelsea Interactive through future cash flows. A \$2.5 million funding loss was reported for the year ended December 31, 2003. Future funding by the Company will be reported as a loss in the period funding is required. Through December 31, 2003, the Company had funded \$54.9 million and anticipates that Chelsea Interactive will not reach the Company's funding limit of \$60.0 million. On February 17, 2004, the Company announced a joint venture between Chelsea Interactive and a publicly traded third party, GSI Commerce, Inc. ("GSI-Chelsea Solutions"). Under the terms of the agreement, Chelsea Interactive will no longer operate its e-commerce technology, but will retain a minority interest in GSI-Chelsea Solutions. Chelsea Interactive's largest clients have entered into service agreements with GSI-Chelsea Solutions and will transition e-commerce activities to the GSI-Chelsea platform by the second quarter of 2004.

The following table sets forth a summary of the GLA changes from developments, expansions, acquisitions and dispositions from January 1 through December 31, 2003:

| Property ----- | Owned | Date (1) | GLA (Sq. Ft.) | Number of Stores | Tenants (2) |
|---|-------|-------------|-------------------|------------------------|---|
| ----- | | | | | |
| As of January 1, 2003 | | | 14,386,000 | 3,436 | |
| New centers developed: | | | | | |
| Las Vegas Premium Outlets..... Las Vegas, NV | 50% | 08/03 | 435,000 | 123 | A X Armani Exchange Dolce & Gabana, Ken Polo Ralph Lauren |
| Sano Premium Outlets Sano, Japan | 40% | 03/03 | 180,000 | 97 | Bally, Brooks Broth Escada, Nautica, Th Timberland |
| Total Development | | | 615,000 | 220 | |
| Expansions: | | | | | |

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| | | | | | |
|---|------|-------|-------------------|--------------|---|
| Gotemba Premium Outlets..... Gotemba City, Japan | 40% | 07/03 | 170,000 | 73 | Bally, Coach, Diesel, Gucci, L.L. Bean, Nike |
| Albertville Premium Outlets..... Albertville, MN | 100% | 12/03 | 125,000 | 37 | Calvin Klein, Liz Claiborne, Timberland, Tommy Hilf |
| Other (net) | | | (30,000) | (12) | |
| Total expansions | | | 265,000 | 98 | |
| Acquisitions: | | | | | |
| Las Vegas Outlet Center..... Las Vegas, NV | 100% | 08/03 | 477,000 | 130 | Liz Claiborne, Nike, Tommy Hilfiger, VF Outlet |
| The Crossings Factory Stores..... Tannersville, PA | 100% | 06/03 | 390,000 | 108 | Ann Taylor, Coach, Reebok, Tommy Hilfi |
| Lakeland Factory Outlet Mall..... Lakeland, TN | 100% | 08/03 | 319,000 | 45 | Bass, L'eggs Hanes, Playtex, Nike, VF F |
| Total acquisitions | | | 1,186,000 | 283 | |
| Dispositions: | | | | | |
| Factory Stores of America..... Mesa, AZ | 100% | 09/03 | (167,000) | (30) | |
| American Tin Cannery Premium Outlets(3) | 100% | 01/04 | (135,000) | (45) | |
| Pacific Grove, CA | | | | | |
| St. Helena Premium Outlets..... St. Helena, CA (Napa Valley) | 100% | 06/03 | (23,000) | (9) | |
| Total dispositions | | | (325,000) | (84) | |
| Net additions for 2003 | | | 1,741,000 | 517 | |
| Totals as of December 31, 2003 | | | 16,127,000 | 3,953 | |

- 1) Development, expansion, acquisition, disposition or termination date.
- 2) Consists of tenants who lease at least 5,000 square feet of GLA or have estimated sales of more than \$300 per square-foot. Most tenants pay a fixed base rent based on square feet leased and pay percentage rent based on sales.
- 3) The Company terminated its long-term lease agreement, expiring December 2004, effective January 2, 2004.

Recent Developments (continued)

Some of the most recent newly developed, acquired or expanded centers are discussed below:

Las Vegas Premium Outlets, Las Vegas, Nevada Las Vegas Premium Outlets, a 435,000 square-foot center containing 123 stores opened in August 2003. The center is located between Grand Central Parkway and I-15 near the intersection of U.S. Route 95, easily accessible from downtown Las Vegas and the "Strip". This tourist destination attracts over 35 million people annually. The population within a 15-mile radius is 1.1 million. Average household income within a 30-mile radius is approximately \$60,000.

Sano Premium Outlets, Sano, Japan - Sano Premium Outlets, a 180,000 square-foot center containing 97 stores, opened in March 2003. The center is located 40 miles north of Tokyo on Route 50 off the Tohoku Expressway. Sano is near some of Japan's most famous tourist spots, including Nikko and the Nasu-Kogen resort area. The population

within a 20-mile and 30-mile radius is 2.5 million and 8.3 million, respectively.

Gotemba Premium Outlets, Gotemba City, Japan - Gotemba Premium Outlets is a 390,000 square-foot center containing 158 stores. Gotemba opened its initial phase in July 2000 and expanded by 170,000 square feet in July 2003. The center is located on the Tomei Expressway, approximately 60 miles west of Tokyo and midway between Mt. Fuji and the Hakone resort area. These two tourist destinations attract 37 million people annually. The population within a 20-mile, 30-mile and 60-mile radius is approximately 1.5 million, 5.0 million and 31.2 million, respectively.

Albertville Premium Outlets, Albertville, Minnesota - Albertville Premium Outlets, a 430,000 square-foot center containing 104 stores was acquired in November 2002 and expanded in December 2003. The center is located approximately 20 miles northwest of Minneapolis-St. Paul on Interstate 94. The population within a 15-mile, 30-mile, and 60-mile radius is 0.3 million, 1.9 million and 3.3 million, respectively. Average household income within a 30-mile radius is approximately \$68,000.

Las Vegas Outlet Center, Las Vegas, Nevada - Las Vegas Outlet Center, a 477,000 square-foot center containing 130 stores was acquired in August 2003. The center is located at the intersection of Las Vegas Boulevard and Warm Springs Road, easily accessible from the Las Vegas airport and the "Strip". This tourist destination attracts over 35 million people annually. The population within a 15-mile radius is 1.1 million. Average household income within a 30-mile radius is approximately \$60,000.

The Crossings Factory Stores, Tannersville, Pennsylvania - The Crossings Factory Stores, a 390,000 square-foot center containing 108 stores was acquired in June 2003. The center is located in Tannersville approximately 13 miles from the Delaware Water Gap, directly off Interstate 80. The population within a 15-mile, 30-mile, and 60-mile radius is 0.2 million, 1.0 million and 2.7 million, respectively. Average household income within a 30-mile radius is approximately \$60,000.

Strategic Alliances and Joint Ventures

In June 1999, the Company entered into an agreement with Mitsubishi Estate Co., Ltd. and Nissho Iwai Corporation to jointly develop, own and operate Premium Outlet centers in Japan. The joint venture, known as Chelsea Japan Co., Ltd. ("Chelsea Japan"), has three operating centers: Sano Premium Outlets, Gotemba Premium Outlets, and Rinku Premium Outlets. Chelsea Japan is scheduled to open its fourth center, Tosu Premium Outlets, located near Fukuoka, Japan, in March 2004.

During 2002, the Company and Simon Property Group, Inc. ("Simon") agreed to develop two Premium Outlet centers under separate 50/50 joint ventures, the 435,000 square-foot Las Vegas Premium Outlets which opened in August 2003 and the 438,000 square-foot Chicago Premium Outlets scheduled to open in mid-2004 ("Simon-Ventures"). Simon is the largest publicly traded retail real estate company in the United States as measured by market capitalization. At February 2004, Simon was engaged in ownership and management of income-producing properties, primarily regional malls and community centers, and had an interest in and/or managed approximately 190 million square feet of retail and mixed-use properties in 37 states, Canada and Europe.

Strategic Alliances and Joint Ventures (continued)

The Company has a 50/50 joint venture agreement with Sordo Madaleno y Asociados and affiliates to jointly develop, own and operate Premium Outlet centers in Mexico. In July 2003, the first development project broke ground, a 230,000 square-foot first phase of Punta Norte Premium Outlets located near Mexico City and is scheduled to open in late 2004. The Company is responsible for financing its 50% share of project costs of approximately \$15.0 million. As of December 31, 2003, the Company had contributed \$2.5 million.

The Company has made several investments through joint ventures with others. Joint venture investments may involve risks not otherwise present for investments made solely by the Company, including the possibility its co-venturers might become bankrupt, its co-venturers might at any time have different interests or goals than the Company, and that the co-venturers may take action contrary to the Company's instructions, requests, policies or objectives, including its policy with respect to maintaining the qualification of the Company as a REIT. Other risks of joint venture investments include impasse on decisions, such as a sale, because neither its co-venturer nor the Company would have full control over the joint venture. There is no limitation under the Company's organizational documents as to the amount of funds that may be invested in partnerships or joint ventures, however, the Company's loan covenants do contain certain limitations.

Organization of the Company

Virtually all of the Company's assets are held by, and all of its business activities conducted through, the Operating Partnership. The Company (which owned 85.6% of the Operating Partnership as of December 31, 2003) is the sole general partner of the Operating Partnership and has full and complete control over the management of the Operating Partnership and each of the Properties, excluding joint ventures.

The Manufacturers' Outlet Business

Manufacturers' outlets are manufacturer-operated retail stores that sell primarily first-quality branded goods at significant discounts from regular department and specialty store prices. Manufacturers' outlet centers offer numerous advantages to both consumer and manufacturer; by eliminating the third party retailer, manufacturers are often able to sell to customers at lower prices for brand name and designer merchandise; manufacturers benefit from selling first quality in-season, as well as out-of-season, overstocked or discontinued merchandise without compromising their relationships with department stores or the manufacturers' brand name. In addition, outlet stores enable manufacturers to optimize the size of production runs while maintaining control of their distribution channels.

Business Strategy

The Company believes its strong tenant relationships, high-quality property portfolio and managerial expertise give it significant advantages in the manufacturers' outlet business.

Strong Tenant Relationships. The Company maintains strong tenant relationships with high-fashion, upscale manufacturers and retailers that have a selective presence in the outlet industry, such as Giorgio Armani, Banana Republic, Brooks Brothers, Chanel, Coach, ColeHaan, Gucci, Nautica, Polo Ralph Lauren, Tommy Hilfiger and Versace, as well as with national brand-name manufacturers such as Adidas, Carter's, Gap, Nike, Phillips-Van Heusen (Bass, Calvin Klein, Izod, Geoffrey Beene, Van Heusen) and Timberland. The Company believes that its ability to draw from both groups is an important factor in providing broad customer appeal and higher tenant sales.

High Quality Property Portfolio. The Company's domestic Premium Properties generated weighted average reported tenant sales during 2003 of \$399 per square-foot, the highest among the three publicly traded outlet companies. As a result, the Company has been successful in attracting some of the world's most sought-after brand-name designers, manufacturers and retailers and each year has added new names to the outlet business and its centers. The Company believes that the quality of its centers gives it significant advantages in attracting customers and negotiating multi-lease transactions with tenants.

Business Strategy (continued)

Management Expertise. The Company believes it has a competitive advantage in the manufacturers' outlet business as a result of its experience in the business, long-standing relationships with tenants and expertise in the development and operation of manufacturers' outlet centers. Management developed a number of the earliest and most successful

outlet centers in the industry, including Liberty Village Premium Outlets (one of the first manufacturers' outlet centers in the U.S.) in 1981, Woodbury Common Premium Outlets in 1985 and Desert Hills Premium Outlets in 1990. Since its IPO, the Company has added significantly to its senior management in the areas of development, leasing and property management without increasing general and administrative expenses as a percentage of total revenues; additionally, the Company intends to continue to invest in systems and controls to support the planning, coordination and monitoring of its activities.

Growth Strategy

The Company seeks growth through increasing rents in its existing centers; developing new centers and expanding existing centers; international development and acquiring and re-developing centers.

Increasing Rents at Existing Centers. The Company's leasing strategy includes aggressively marketing available space and maintaining a high level of occupancy; providing for inflation-based contractual rent increases or periodic fixed contractual rent increases in substantially all leases; renewing leases at higher base rents per square-foot; re-tenanting space occupied by under performing tenants and continuing to sign leases that provide for percentage rents.

Developing New Centers and Expanding Existing Centers. The Company believes that there continue to be significant opportunities to develop manufacturers' outlet centers across the United States and internationally. The Company intends to undertake such development selectively, and believes that it will have a competitive advantage in doing so as a result of its development expertise, tenant relationships and access to capital. The Company expects that the development of new centers and the expansion of existing centers will continue to be a substantial part of its growth strategy. The Company believes that its development experience and strong tenant relationships enable it to determine site viability on a timely and cost-effective basis. However, there can be no assurance that any development or expansion projects will be commenced or completed as scheduled.

International Development. The Company continues to develop, own and operate Premium Outlet centers in Japan through its joint venture company, Chelsea Japan. In 2003, Chelsea Japan opened the 180,000 square-foot first phase of Sano Premium Outlets, located 40 miles north of Tokyo, Japan and expanded Gotemba Premium Outlets, by 170,000 square-feet. Gotemba Premium Outlets at 390,000 square feet is the Company's largest and most productive outlet center in Japan. The 185,000 square-foot first phase of Tosu Premium Outlets, located near Fukuoka, Japan is scheduled to open in March 2004. During 2003, the Company commenced construction on the 230,000 square-foot first phase of Punta Norte Premium Outlets, located north of Mexico City. The center is scheduled to open in late 2004 and can support an additional phase containing approximately 165,000 square feet. The Company believes that there are significant opportunities to develop additional manufacturers' outlet centers in Japan, Mexico and other countries. The Company intends to pursue these opportunities as viable sites and local partners are identified.

Acquiring and Redeveloping Centers. The Company intends to selectively acquire individual properties and portfolios of properties that meet its strategic investment criteria as suitable opportunities arise. The Company believes that its extensive experience in the outlet center business, access to capital markets, familiarity with real estate markets and advanced management systems will allow it to evaluate and execute its acquisition strategy successfully. Furthermore, management believes that the Company will be able to enhance the operation of acquired properties as a result of its strong tenant relationships with both national and upscale fashion retailers and development, marketing and management expertise as a full-service real estate organization. Additionally, the Company may be able to acquire properties on a tax-advantaged basis through the issuance of Operating Partnership units. However, there can be no assurance that any acquisitions will be consummated or, if consummated, will result in an advantageous return on investment for the Company.

Operating Strategy

The Company's primary business objective is to enhance the value of its properties and operations by increasing cash flow. The Company plans to achieve this objective through continuing efforts to improve tenant sales and profitability, and to enhance the opportunity for higher base and percentage rents.

Operating Strategy (continued)

Leasing. The Company pursues an active leasing strategy through long-standing relationships with a broad range of tenants including manufacturers of men's, women's and children's ready-to-wear, lifestyle apparel, footwear, accessories, tableware, housewares, linens and domestic goods. Key tenants are placed in strategic locations to draw customers into each center and to encourage shopping at more than one store. The Company continually monitors tenant mix, store size, store location and sales performance, and works with tenants to improve each center through re-sizing, re-location and joint promotion.

Market and Site Selection. To ensure a sound long-term customer base, the Company generally seeks to develop sites near densely populated, high-income metropolitan areas, and/or at or near major tourist destinations. While these areas typically impose numerous restrictions on development and require compliance with complex entitlement and regulatory processes, the Company believes that these areas provide the most attractive long-term demographic characteristics. The Company generally seeks to develop sites that can support at least 400,000 square feet of GLA and that offer the long-term opportunity to dominate their respective markets through a critical mass of tenants.

Marketing. The Company pursues an active, property-specific marketing strategy using a variety of media including newspapers, television, radio, billboards, regional magazines, guide books and direct mailings. The centers are marketed to tour groups, conventions and corporations; additionally, each property participates in joint destination marketing efforts with other area attractions and accommodations. Virtually all consumer-marketing expenses incurred by the Company are reimbursable by tenants.

Property Design and Management. The Company believes that effective property design and management are significant factors in the success of its properties and works continually to maintain or enhance each center's physical plant, original architectural theme and high level of on-site services. Each property is designed to be compatible with its environment and is maintained to high standards of aesthetics, ambiance and cleanliness in order to promote longer visits and repeat visits by shoppers. The Company has 645 full-time and 208 part-time employees. Of these employees, 502 full-time and 208 part-time are involved in on-site maintenance, security, administration and marketing. An on-site property manager generally manages centers with oversight from a regional operations director.

Financing

The Company seeks to maintain a strong, flexible financial position by: (i) maintaining a moderate level of leverage, (ii) extending and sequencing debt maturity dates, (iii) managing floating interest rate exposure and (iv) maintaining liquidity. Management believes these strategies will continue to enable the Company to access a broad array of capital sources, including bank or institutional borrowings, secured and unsecured debt and equity financings. See "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Competition

The Properties compete for retail consumer spending on the basis of the diverse mix of retail merchandising and value oriented pricing. Manufacturers' outlet centers have established a niche capitalizing on consumers' desire for value-priced goods. The Properties compete for customer spending with other outlet locations, traditional shopping malls, off-price retailers, and other retail distribution channels. The Company believes that the Premium Properties generally are the leading manufacturers' outlet centers in each market. The Company carefully considers the degree of existing and planned competition in each proposed market before deciding to build a new center.

Environmental Matters

The Company is not aware of any environmental liabilities relating to the Properties that would have a material impact on the Company's financial position and results of operations.

Personnel

As of December 31, 2003, the Company had 645 full-time and 208 part-time employees. None of the employees are subject to any collective bargaining agreements, and the Company believes it has good relations with its employees.

Item 2. Properties

As of December 31, 2003, the Company had 60 centers in 31 states and Japan containing approximately 16.1 million square feet of gross leasable area. Of the 60 centers, 56 are owned 100% (50 in fee and 6 under long-term leases). The Company operated all 57 of its domestic centers and Chelsea Japan managed the three centers in Japan.

The Company's Premium Properties consist of 30 upscale, fashion-oriented manufacturers' outlet centers located in or near New York City, Los Angeles, Chicago, Boston, Washington, D.C., San Francisco, Sacramento, Atlanta, Dallas, Tokyo and Osaka, Japan, or within 20 miles of major tourist destinations including Palm Springs, Napa Valley, Orlando, Las Vegas and Honolulu. The domestic Premium Properties were 99% leased as of December 31, 2003, and contained approximately 2,468 stores with more than 550 different tenants. The Company's Premium Properties in Japan were 100% leased as of December 31, 2003, and contained 375 stores with approximately 190 different tenants. The Company's Other Properties were 93% leased as of December 31, 2003, and contained approximately 1,110 stores with more than 290 different tenants.

The Company believes the Properties are adequately covered by insurance.

The Company does not consider any single store lease to be material; no individual tenant, combining all of its store concepts, accounts for more than 5% of the Company's gross revenues; and only one tenant occupies more than 5% of the Company's total domestic GLA at 8%. As a result, and considering the Company's past success in re-leasing available space, the Company believes the loss of any individual tenant would not have a significant effect on future operations.

For the years ended December 31, 2003, 2002 and 2001, respectively, 13%, 16% and 21% of the Company's total revenues were derived from Woodbury Common Premium Outlets. The loss of this center or a material decrease in revenues from the center for any reason might have a material adverse effect on the Company. In addition, for the years ended December 31, 2003, 2002 and 2001, respectively, 23%, 25% and 28% of the Company's total revenues were derived from the Company's centers in California.

VF Corporation (Vanity Fair) leases approximately 8% of the Company's total domestic GLA as of December 31, 2003, which constitutes approximately 3% of the Company's base rents.

Woodbury Common Premium Outlets contributed more than 10% of the Company's aggregate gross revenues during 2003 and had a book value of more than 5% of the total assets at year-end 2003. No tenant leases more than 5% of the center's GLA. The following chart shows certain information for Woodbury Common.

| Fiscal Year ----- | Occupancy Rate ----- | Avg. Annual Rent Per Sq Ft ----- |
|-------------------------|----------------------------|---|
| 1999 | 99.5% | \$35.61 |
| 2000 | 100.0% | 38.55 |

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| 2001 | 98.8% | 38.63 |
| 2002 | 100.0% | 41.23 |
| 2003 | 100.0% | 44.62 |

Woodbury Common Premium Outlets opened in four phases in 1985, 1993, 1995 and 1998 and contains 844,000 square feet of GLA. As of December 31, 2003, the center's 212 units were fully leased. Woodbury Common is located approximately 50 miles north of New York City at the Harriman exit off the New York State Thruway. The population within a 30-mile, 60-mile and 100-mile radius is approximately 2.5 million, 17.3 million and 25.2 million, respectively. Average household income within the 30-mile radius is approximately \$83,000.

Item 2. Properties (continued)

The following table shows lease expiration data as of December 31, 2003 for Woodbury Common Premium Outlets for the next ten years (assuming that none of the tenants exercise renewal options).

| Expiration Year | GLA | Contractual Base Rents ("CBR") per sq ft | Total | No. of Leases Expiring | Annual "CBR" Represented Expiring Le |
|-----------------|---------|--|-------------|------------------------------|---|
| 2004 | 42,086 | \$30.12 | \$1,268,000 | 11 | 3.8% |
| 2005 | 109,652 | 36.13 | 3,962,000 | 26 | 11.9% |
| 2006 | 33,768 | 43.76 | 1,478,000 | 14 | 4.4% |
| 2007 | 55,722 | 37.94 | 2,114,000 | 14 | 6.3% |
| 2008 | 229,842 | 36.41 | 8,369,000 | 52 | 25.1% |
| 2009 | 52,739 | 47.84 | 2,523,000 | 19 | 7.6% |
| 2010 | 44,661 | 40.62 | 1,814,000 | 12 | 5.4% |
| 2011 | 79,142 | 41.58 | 3,291,000 | 15 | 9.9% |
| 2012 | 70,068 | 51.46 | 3,606,000 | 22 | 10.8% |
| 2013 | 109,636 | 38.67 | 4,240,000 | 23 | 12.7% |

Depreciation on Woodbury Common Premium Outlets is calculated using the straight-line method over the estimated useful life of the real property and land improvements, which ranges from 10 to 40 years. At December 31, 2003, the Federal income tax basis in this center was \$116.0 million.

The real estate tax on Woodbury Common Premium Outlets was \$4.2 million in 2003 and it is estimated to be \$4.7 million in 2004.

Set forth in the table below is certain property information as of December 31, 2003:

| Name/Location | Opened or Acquired | GLA (Sq. Ft.) | No. of Stores | Selected Tenants |
|---|--------------------------|------------------|------------------|--|
| Premium Properties: | | | | |
| Woodbury Common Premium Outlets..... Central Valley, NY (New York City area) | 1985 | 844,000 | 212 | Banana Republic, Brooks Brother Giorgio Armani, Gucci, Neiman M Call, Polo Ralph Lauren, Salvat Ferragamo |
| Wrentham Village Premium Outlets..... Wrentham, MA (Boston/Providence area) | 1997 | 601,000 | 158 | Barneys New York, Burberry, Hug Kenneth Cole, Nike, Polo Ralph Sony, Versace |
| Gilroy Premium Outlets..... | 1990 | 577,000 | 142 | Brooks Brothers, Calvin Klein, |

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| | | | | |
|---|----------|---------|-----|--|
| Gilroy, CA (San Jose area) | | | | Crew, Hugo Boss, Nike, Polo Ralph Lauren, Timberland, Tommy Hilfiger, Vera Wang |
| North Georgia Premium Outlets..... Dawsonville, GA (Atlanta metro area) | 1996 | 537,000 | 132 | Coach, Crate & Barrel, Escada, Polo Ralph Lauren, Tommy Hilfiger, Williams-Sonoma |
| Desert Hills Premium Outlets..... Cabazon, CA (Palm Springs-Los Angeles) | 1990 | 499,000 | 133 | Burberry, Coach, Giorgio Armani, Max Mara, Polo Ralph Lauren, Salvatore Ferragamo, Versace, Yves Saint Laurent, Rive Gauche, Zegna |
| Lighthouse Place Premium Outlets..... Michigan City, IN (Chicago area) | 1987 | 478,000 | 115 | Burberry, Coach, Crate & Barrel, Liz Claiborne, Polo Ralph Lauren, Tommy Hilfiger |
| Leesburg Corner Premium Outlets..... Leesburg, VA (Washington DC area) | 1998 | 463,000 | 103 | Barneys New York, Kenneth Cole, Claiborne, Nike, Polo Ralph Lauren, Williams-Sonoma |
| Camarillo Premium Outlets..... Camarillo, CA (Los Angeles metro area) | 1995 | 454,000 | 122 | Banana Republic, Barneys New York, Coach, Donna Karan, Polo Ralph Lauren, St. John, Versace |
| Carolina Premium Outlets (2)..... Smithfield, NC (Raleigh area) | 2001 | 440,000 | 82 | Brooks Brothers, Gap, Liz Claiborne, Nike, Polo Ralph Lauren, Tommy Hilfiger |
| Las Vegas Premium Outlets..... Las Vegas, NV | 2003 | 435,000 | 123 | A X Armani Exchange, Calvin Klein, Coach, Dolce & Gabbana, Elie Tahari, Polo Ralph Lauren |
| Albertville Premium Outlets..... Albertville, MN (Minneapolis area) | 2002 | 430,000 | 104 | Banana Republic, Calvin Klein, Old Navy, Polo Ralph Lauren, Tommy Hilfiger |
| Orlando Premium Outlets..... Orlando, FL (between Sea World & Epcot) | 2000 | 428,000 | 115 | Barneys New York, Coach, Escada, Armani, Hugo Boss, Max Mara, Nike, Polo Ralph Lauren |
| Waterloo Premium Outlets..... Waterloo, NY (Finger Lakes Region) | 1995 | 392,000 | 99 | Brooks Brothers, Coach, Eddie Bauer, J. Crew, Jones New York, Liz Claiborne, Polo Ralph Lauren |
| Osage Beach Premium Outlets..... Osage Beach, MO | 2002 | 391,000 | 104 | Brooks Brothers, Coach, Gap, Liz Claiborne, Polo Ralph Lauren, Tommy Hilfiger |
| Gotemba Premium Outlets..... Gotemba City, Japan (Tokyo metro area) (2) | 2000 (1) | 390,000 | 158 | Bally, Coach, Diesel, Gap, Guccio Gucci, Stuart, L.L. Bean, Nike, Tod's |
| Allen Premium Outlets..... Allen, TX (Dallas metro area) | 2000 | 349,000 | 84 | Brooks Brothers, Cole-Haan, Crate & Barrel, Kenneth Cole, Liz Claiborne, Polo Ralph Lauren, Tommy Hilfiger |
| St. Augustine Premium Outlets..... St. Augustine, FL | 2002 | 329,000 | 93 | Brooks Brothers, Casual Corner, Gap, Movado, Reebok, Tommy Bahama |
| Folsom Premium Outlets..... Folsom, CA (Sacramento metro area) | 1990 | 299,000 | 80 | Bass, Eddie Bauer, Gap, Kenneth Cole, Liz Claiborne, Nike, Off 5th-Sak |
| Aurora Premium Outlets..... Aurora, OH (Cleveland metro area) | 1987 | 287,000 | 65 | Ann Taylor, Brooks Brothers, Gap, Claiborne, Nautica, Off 5th-Sak |
| Clinton Crossing Premium Outlets..... Clinton, CT (I-95/NY-NewEngland Corridor) | 1996 | 272,000 | 66 | Barneys New York, Calvin Klein, Dooney & Bourke, Gap, Kenneth Cole, Liz Claiborne, Nike, Polo Ralph |

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| Rinku Premium Outlets..... Izumisano, Japan (Osaka metro area) (2) | 2000 (1) | 250,000 | 120 | Bally, Brooks Brothers, Coach, Bauer, Gap, Nautica, Nike, Timb Versace |
| Waikale Premium Outlets..... Waipahu, HI (Honolulu area) | 1997 | 210,000 | 51 | Banana Republic, Barneys New Yo Coach, Guess, Kenneth Cole, Max Polo Ralph Lauren |
| Petaluma Village Premium Outlets..... Petaluma, CA (San Francisco metro area) | 1994 | 196,000 | 51 | Brooks Brothers, Coach, Gap, Jo New York, Liz Claiborne, Off 5t Fifth Avenue, Puma |
| Sano Premium Outlets..... Sano, Japan (Tokyo metro area) (2) | 2003 (1) | 180,000 | 97 | Bally, Brooks Brothers, Coach, New Yorker, Nine West, Timberla |
| Napa Premium Outlets..... Napa, CA (Napa Valley) | 1994 | 179,000 | 51 | Barneys New York, J. Crew, Jone York, Kenneth Cole, Nautica, To Hilfiger, TSE |
| Liberty Village Premium Outlets..... Flemington, NJ (New York-Phila. metro area) | 1981 | 177,000 | 57 | Calvin Klein, Ellen Tracy, Jone New York, L.L. Bean, Polo Ralph Lauren, Tommy Hilfiger, Timberl Waterford Wedgwood |
| Columbia Gorge Premium Outlets..... Troutdale, OR (Portland metro area) | 1991 | 164,000 | 45 | Adidas, Carter's, Gap, Samsonit Van Heusen |
| Kittery Premium Outlets Kittery, ME (Boston area) (2) | 1984 | 150,000 | 32 | Banana Republic, Coach, Crate & Barrel, J. Crew, Polo Ralph Lau Reebok, Tumi |
| Santa Fe Premium Outlets..... Santa Fe, NM | 1993 | 125,000 | 38 | Brooks Brothers, Coach, Johnsto Murphy, Jones New York, Liz Cla Nautica, Van Heusen |
| Patriot Plaza Premium Outlets..... Williamsburg, VA (Norfolk-Richmond area) | 1986 | 77,000 | 11 | Lenox, Polo Ralph Lauren, WestP Stevens |
| Total Premium Properties (3)..... | | ----- 10,603,000 ----- | ----- 2,843 ----- | |
| Other Properties: | | | | |
| Las Vegas Outlet Center..... Las Vegas, NV | 2003 | 477,000 | 130 | Liz Claiborne, Nike, Reebok, To Hilfiger, VF Factory Outlet, Wa Wedgwood |
| Factory Stores at Vacaville..... Vacaville, CA | 2001 | 447,000 | 104 | Adidas, Burberry, Coach, Eddie Gap, Liz Claiborne, Nike, Polo Lauren, Reebok |
| The Crossings Factory Stores..... Tannersville, PA | 2003 | 390,000 | 108 | Ann Taylor, Coach, Liz Claiborn Ralph Lauren, Reebok, Tommy Hil |
| Lakeland Factory Outlet Mall..... Lakeland, TN | 2003 | 319,000 | 45 | Bass, L'eggs Hanes Bali Playtex VF Factory Outlet, Van Heusen |
| Edinburgh Outlet Center..... Edinburgh, IN | 2002 | 305,000 | 72 | Coach, Gap, Nautica, Nike, OshK B'Gosh, Polo Ralph Lauren, Tomm Hilfiger |
| Factory Merchants Branson..... Branson, MO | 2002 | 300,000 | 86 | Carter's, Coach, Izod, Nautica, Pfaltzgraff, Reebok, Van Heusen |
| Jackson Outlet Village..... Jackson, NJ | 2002 | 292,000 | 71 | Brooks Brothers, Calvin Klein, Nike, Reebok, Timberland, Tommy |

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|--|------|---------|----|---|
| The Factory Shoppes at Branson Meadows (2)..... Branson, MO | 2001 | 287,000 | 43 | Dress Barn, Easy Spirit, VF Fac |
| Johnson Creek Outlet Center..... Johnson Creek, WI | 2002 | 278,000 | 62 | Gap, Lands' End, Nike, Old Navy Hilfiger |
| Factory Stores at North Bend North Bend, WA | 2001 | 223,000 | 50 | Adidas, Bass, Carter's, Eddie B OshKosh B'Gosh, Samsonite |
| Factory Stores of America..... Draper, UT | 2001 | 184,000 | 31 | Adidas, Dress Barn, Samsonite, Outlet |
| Factory Stores of America..... Georgetown, KY | 2001 | 177,000 | 27 | Bass, Carolina Pottery, Dress B Van Heusen |
| North Ridge Shopping Center..... Raleigh, NC | 2001 | 166,000 | 33 | Ace Hardware, Kerr Drugs, Winn |
| Factory Stores of America Crossville, TN | 2001 | 151,000 | 30 | Bass, Liz Claiborne, OshKosh B' Reebok, Van Heusen, VF Factory |
| MacGregor Village..... Cary, NC | 2001 | 145,000 | 45 | Spa Health Club, Tuesday Mornin |
| Factory Stores of America -Tri-Cities... Blountville, TN | 2001 | 133,000 | 16 | Carolina Pottery, L'eggs Hanes Playtex, Tri-Cities Cinemas |
| Factory Stores of America..... Tupelo, MS | 2001 | 129,000 | 12 | Banister Shoes, VF Factory Outl Van Heusen |
| Dare Centre (2)..... Kill Devil Hills, NC | 2001 | 115,000 | 15 | Fashion Bug, Food Lion |
| Factory Stores of America..... Story City, IA | 2001 | 112,000 | 17 | Dress Barn, Factory Brand Shoes Factory Outlet, Van Heusen |
| Factory Stores of America (2)..... Boaz, AL | 2001 | 112,000 | 18 | Banister Shoes, Paper Factory, Factory Outlet |
| Factory Stores of America (2)..... Iowa, LA | 2001 | 109,000 | 15 | Easy Spirit, VF Factory Outlet, Van Heusen |
| Factory Stores of America..... West Frankfort, IL | 2001 | 91,000 | 10 | VF Factory Outlet |
| Factory Stores of America..... Arcadia, LA | 2001 | 90,000 | 11 | Bass, Dress Barn, VF Factory Ou Van Heusen |
| Factory Stores of America..... Nebraska City, NE | 2001 | 90,000 | 10 | Bass, Dress Barn, VF Factory Ou |
| Factory Stores of America..... Lebanon, MO | 2001 | 86,000 | 13 | Dress Barn, VF Factory Outlet |
| Factory Stores of America..... Graceville, FL | 2001 | 84,000 | 13 | Factory Brand Shoes, VF Factory Van Heusen |
| Factory Stores of America..... Hanson, KY | 2001 | 64,000 | 4 | Banister Shoes, VF Factory Outl |
| Factory Stores of America..... Hempstead, TX | 2001 | 64,000 | 4 | VF Factory Outlet |
| Factory Stores of America..... Union City, TN | 2001 | 60,000 | 4 | VF Factory Outlet |
| Factory Stores of America..... | 2001 | 44,000 | 11 | Levi's, Sportshoe Center, Carte |

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Lake George, NY

| | | |
|-------------------------------------|------------|-------|
| Total Other Properties | 5,524,000 | 1,110 |
| Grand Total | 16,127,000 | 3,953 |

Notes to Property Data:

- 1) Chelsea Japan properties are 40%-owned through a joint venture with Mitsubishi Estate Co., Ltd. (30% ownership) and Nissho Iwai Corporation (30% ownership).
- 2) Property held under long term land lease expiring as follows: Factory Stores of America at Boaz, January 2007; Kittery Premium Outlets (129,000 sq ft), October 2009; Gotemba Premium Outlets, October 2019; Rinku Premium Outlets, March 2020; Sano Premium Outlets, June 2022; The Shoppes at Branson Meadows, November 2021; Carolina Premium Outlets (87,000 sq ft), January 2029; Dare Centre, September 2058; Factory Stores of America at Iowa, September 2087.
- 3) The Company terminated its American Tin Cannery Premium Outlets long-term lease agreement.

Item 3. Legal Proceedings

The Company is not presently involved in any material litigation other than routine litigation arising in the ordinary course of business and that is either expected to be covered by liability insurance or to have no material impact on the Company's financial position and results of operations.

Item 4. Submission of Matters to a Vote of Security Holders

None

Directors and Executive Officers of the Company

The following table sets forth the directors and executive officers of the Company:

| Name | Age | Position |
|------------------------|-----|--|
| ---- | --- | ----- |
| David C. Bloom | 47 | Chairman of the Board and Chief Executive Officer (term expires in 2005) |
| William D. Bloom | 41 | Vice Chairman and Director (term expires in 2006) |
| Brendan T. Byrne | 79 | Director (term expires in 2004) |
| Robert Frommer | 68 | Director (term expires in 2006) |
| Barry M. Ginsburg | 66 | Director (term expires in 2005) |
| Philip D. Kaltenbacher | 66 | Director (term expires in 2005) |
| Reuben S. Leibowitz | 56 | Director (term expires in 2006) |
| Leslie T. Chao | 47 | President |
| Thomas J. Davis | 48 | Chief Operating Officer, President - U.S. Premium Outlets |
| Michael J. Clarke | 50 | Executive Vice President and Chief Financial Officer |
| Anthony J. Galvin | 44 | Executive Vice President - International |
| John R. Klein | 45 | Senior Vice President-Real Estate |
| Richard N. Lewis | 54 | Senior Vice President- Domestic Leasing |
| Matt Broas | 43 | Vice President - Assistant General Counsel |
| Christina M. Casey | 48 | Vice President-Human Resources |
| Denise M. Elmer | 47 | Vice President - General Counsel and Secretary |
| Philip E. Ende | 33 | Vice President - Leasing |
| Eric K. Helstrom | 45 | Vice President-Architecture and Construction |

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|--------------------|----|---------------------------------------|
| Daniel L. Kelly | 38 | Vice President- International Leasing |
| Catherine A. Lassi | 44 | Vice President & Treasurer |
| Gregory C. Link | 54 | Vice President-Operations |
| Michele Rothstein | 45 | Vice President-Marketing |
| Sharon M. Vuskalns | 40 | Controller |

David C. Bloom, Chairman of the Board and Chief Executive Officer since 1993. Mr. Bloom was a founder and principal of Chelsea, served as President of Chelsea from 1985 to 1993. As Chairman of the Board and Chief Executive Officer of the Company, Mr. Bloom sets policy and coordinates and directs all the Company's primary functions. Prior to founding Chelsea, he was an equity analyst with The First Boston Corporation (now Credit Suisse First Boston Corporation) in New York. Mr. Bloom graduated from Dartmouth College and received an MBA from Harvard Business School and is a member of the Board of Governors of the National Association of Real Estate Investment Trusts (NAREIT).

William D. Bloom, Vice Chairman since 2000 and Director since 1995. Mr. Bloom joined The Chelsea Group in 1986 with responsibility for leasing the Company's projects and was appointed Executive Vice President-Leasing in 1993 and Executive Vice President-Strategic Relationships in 1996. Mr. Bloom's current responsibilities include strategic leasing and relationships of key accounts and partnerships. From 2000 through 2003, Mr. Bloom's responsibilities included the day-to-day operations of Chelsea Interactive, Inc. Prior to joining Chelsea, he was an institutional bond broker with Mabon Nugent in New York. Mr. Bloom graduated from Boston University School of Management.

Brendan T. Byrne, Director since 1993. Since 1982, Mr. Byrne has been a senior partner in the law firm of Carella, Byrne, Bain, Gilfillan, Cecchi, Stewart & Olstein. Mr. Byrne previously served as Governor of New Jersey from 1974 to 1982, Prosecutor of Essex County (New Jersey), President of the Public Utility Commission and Assignment Judge of the New Jersey Superior Court. Mr. Byrne has also served as Vice President of the National District Attorneys Association; Trustee of Princeton University; Chairman of the Princeton University Council on New Jersey Affairs; Chairman of the United States Marshals Foundation; and Chairman of the National Commission on Criminal Justice Standards and Goals (1977). He serves on a Board of the National Judicial College, is a former Commissioner of the New Jersey Sports and Exposition Authority, and was a member of the board of directors of New Jersey Bell Telephone Company, Elizabethtown Water Company, Ingersoll-Rand Company and a former director of The Prudential Insurance Company of America. He is a member of the Board of Mack-Cali Realty Corporation. Mr. Byrne graduated from Princeton University and received an LL.B. from Harvard Law School.

Robert Frommer, Director since 1993. For the past twelve years, Mr. Frommer had been a real estate consultant based in San Francisco. Prior to this time, Mr. Frommer was responsible for developing major commercial, residential and mixed-use real estate projects in New York, Philadelphia, Washington, D.C., Chicago and Seattle. He has served as President of the Pebble Beach Co., the Ritz-Carlton Hotel of Chicago and PG&E Properties in California. Mr. Frommer is a graduate of the Wharton School of the University of Pennsylvania, and received an LL.B. Degree from Yale Law School.

Barry M. Ginsburg, Director since 1993. Mr. Ginsburg was a founder and principal of Ginsburg Craig Associates and its predecessor companies from 1986 to 1993, and Vice Chairman of the Company from 1993 to 1999 at which time he retired. From 1966 through 1985, he was employed by Dansk International Designs, Ltd. and was corporate Chief Operating Officer and Director from 1980 to 1985. Dansk operated a chain of 31 manufacturers' outlet stores. Mr. Ginsburg is currently a Director of Liz Lange Maternity, New Milford (Connecticut) Hospital and AGS Realty Advisors. Mr. Ginsburg graduated from Colby College and received an MBA from Cornell University.

Philip D. Kaltenbacher, Director since 1993. Since 1974, Mr. Kaltenbacher has been Chairman of the Board of Directors and Chief Executive Officer of Seton Company, a manufacturer of leather and chemicals. Mr. Kaltenbacher was a Commissioner of The Port Authority of New York and New Jersey from September 1985 through February 1993, and served as Chairman from September 1985 through April 1990. Mr. Kaltenbacher graduated from Yale

University and received an LL.B. from Yale Law School.

Reuben S. Leibowitz, Director since 1993. Mr. Leibowitz is a Managing Director of Warburg Pincus, a private equity investment firm. He has been associated with Warburg Pincus since 1984. Mr. Leibowitz currently serves as Director of a number of private companies. Mr. Leibowitz graduated from Brooklyn College, received an MBA from New York University, a JD from Brooklyn Law School, and a LL.M. from New York University School of Law.

Leslie T. Chao, President since April 1997. As President of Chelsea, Mr. Chao oversees the corporate finance, international development, legal, administrative, investor relations and human resource functions of the Company. He is also Chairman of the Board of Chelsea Japan Co., Ltd., the Company's Japanese joint venture. Mr. Chao joined Chelsea in 1987 as Chief Financial Officer. Prior to joining Chelsea, he was a Vice President in the corporate finance/treasury area of Manufacturers Hanover Corporation (now J.P. Morgan Chase & Co.), a New York bank holding company. He graduated from Dartmouth College and received an MBA from Columbia Business School.

Thomas J. Davis, Chief Operating Officer since April 1997. President U.S. Premium Outlets since 2002. As Chief Operating Officer, Mr. Davis oversees the asset management activities of the domestic outlet portfolio including leasing, operations and marketing as well as development and construction. Mr. Davis joined Chelsea in 1996 as Executive Vice President-Asset Management. From 1988 to 1995, he held various senior positions at Phillips-Van Heusen Corporation, most recently as Vice President-Real Estate. Mr. Davis has over twenty years of factory outlet industry experience and has served the industry in various trade association positions including Chairman of Manufacturers Idea Exchange as well as a board member of the Steering Committee for FOMA (Factory Outlet Marketing Association). Mr. Davis received the 1995 *Value Retail News* Award of Excellence for individual achievement in the outlet industry.

Michael J. Clarke, Executive Vice-President and Chief Financial Officer since 1999. Since joining the Company in 1994, Mr. Clarke has held various senior level financial positions. As Chief Financial Officer, he is responsible for Chelsea's financial functions including reporting, treasury, accounting, budgeting, as well as banking, investor and rating agency relationships. From 1985 to 1993, Mr. Clarke held various senior positions at a NYSE-listed owner and operator of hotels, most recently as Executive Vice President & Chief Financial Officer. Mr. Clarke graduated from Seton Hall University and is a certified public accountant.

Anthony J. Galvin, Executive Vice President- International since 2004. Mr. Galvin joined the Company in 1997 as Vice President-Leasing, and was named Senior Vice President- Leasing in January 2001 and Executive Vice President-International in February 2004. He is responsible for all aspects of the Company's international business, including development, joint venture management, leasing, marketing and operations. From 1995 to 1997, he was Director of Real Estate for Coach Leather, then a division of Sara Lee Corporation. From 1987 to 1995 he held positions in real estate and construction at Phillips-Van Heusen Corporation. Mr. Galvin has served the outlet industry in various trade association positions including Chairperson of the Northeast Merchants Association and the Board of Directors of ORMA (Outlet Retail Merchants Association). He graduated from Glassboro State College (now Rowan University), where he served on the Executive Committee of the Alumni Advisory Council for the School of Business.

John R. Klein, Senior Vice President-Real Estate, since 2001. Mr. Klein joined the Company in 1995 as Director-Acquisitions, was named Vice President-Acquisitions and Development in 1996, and named Senior Vice President-Real Estate in January 2001. He oversees the Company's domestic acquisitions, development and construction activities. From 1991 to 1995, he held various positions at Prime Retail, Inc., most recently as Vice President-Site Acquisition. At Prime, Mr. Klein was involved in the acquisition and entitlement of over two million square feet of manufacturers' outlet space in nine states. Mr. Klein graduated from Columbia University and received an MBA from George Washington University School of Business.

Richard N. Lewis, Senior Vice President- Domestic Leasing since 2004. From 1996 to 2003, Mr. Lewis held various executive positions at Charter Oak Partners, the largest privately held developer/operator of factory outlet centers,

most recently as President from 2000 until the company was sold in 2003. At Charter Oak he was responsible for the day-to-day management/operation of the 3.3 million square foot portfolio of outlet centers and the supervision of 135 employees in the corporate office and in the field. From 1990 until 1996, Mr. Lewis held leasing positions at Prime Retail, Inc, a publicly traded REIT, now a privately held company. Mr. Lewis was the Vice President of Leasing from 1994 to 1996. Mr. Lewis has been a faculty member of the University of Shopping Centers since 2002, which is part of the International Council of Shopping Center (ICSC). He is currently the Dean of the School of Open Air Centers. Mr. Lewis is a graduate of Buffalo University and has a Masters Degree from Stony Brook University.

Matthew J. Broas, Vice President, Assistant General Counsel since 2003. Mr. Broas joined Chelsea in 2000 as Assistant General Counsel. Mr. Broas oversees the Leasing Support Group, responsible for negotiating, documenting and administering retail leases and related agreements relative to the company's domestic shopping center portfolio. Prior to joining Chelsea, Mr. Broas served as Vice President, Corporate Properties for Beneficial Corporation. From 1985 to 1992, he practiced law in the Real Estate Department of the Morristown, N.J. firm of Pitney, Hardin, Kipp & Szuch. Mr. Broas graduated from Princeton University and received his J.D. from the Marshall Wythe School of Law, College of William & Mary.

Christina M. Casey, Vice President-Human Resources since 1998. Ms. Casey joined the Company in 1996 as Director of Human Resources. As Vice President-Human Resources, she oversees all aspects of the Company's human resource activities, including recruitment, benefits, compensation, policy development, training and employee relations. From 1987 to 1996 she held various positions in Human Resources with Boise Cascade Corporation, Specialty Paperboard and Rock-Tenn Company. Ms. Casey graduated from Villanova University and received a Masters in Social Service from Bryn Mawr Graduate School.

Denise M. Elmer, Vice President, General Counsel and Secretary since 1993. Ms. Elmer joined Chelsea as General Counsel in 1993. As Vice President, General Counsel and Secretary, she oversees the legal activities of the Company, including those related to property acquisition and development, leasing, finance and operations. From 1990 to 1993, she was a partner in the New York law firm of Stadtmauer Bailkin Levine & Masur, where she specialized in commercial real estate law. Ms. Elmer graduated from St. Lawrence University and received a JD from Duke University School of Law.

Philip Ende, Vice President-Leasing since 2001. Mr. Ende joined the Company in 1993 and has held various positions with increasing responsibility in leasing and construction prior to being named Vice President-Leasing in March 2001. Mr. Ende is responsible for the management of all aspects of the day-to-day leasing activities of the Company's domestic portfolio. Mr. Ende graduated from the University of Florida.

Eric K. Helstrom, Vice President-Architecture and Construction, since 1996. Mr. Helstrom joined the Company in 1995 as Director-Development and was named Vice President-Architecture and Construction in 1996. He oversees the design, engineering and construction activities of the Company. From 1987 to 1995, he held various positions including Director-Architecture/Construction with Alexander Haagen Properties, an AMEX-listed REIT. Mr. Helstrom graduated from California Polytechnic San Luis Obispo and received a Masters in Real Estate Development from the University of Southern California. Mr. Helstrom is a licensed architect and general contractor.

Daniel L. Kelly, Vice President International Leasing since 2001. Since joining the Company in 1993, Mr. Kelly has held various positions in the leasing area. From July 1999 to August 2001, Mr. Kelly served as Senior Managing Director of Chelsea Japan in Tokyo before being named Vice President-International Leasing. Mr. Kelly received his MBA in International Business from Rutgers University and a BA in mathematics from Providence College.

Catherine A. Lassi, Vice President and Treasurer since 2003. Ms. Lassi joined Chelsea in 1987, became Controller in 1990 and Treasurer in 1997. As Vice President and Treasurer, she oversees budgeting, forecasting, contract administration, cash management, banking, information systems and lease accounting activities for the Company. Ms. Lassi is a certified public accountant and graduated from the University of South Florida.

Gregory C. Link, Vice President-Operations since 1996. Mr. Link joined the Company in 1994 as Vice President-Leasing responsible for the management of the Company's leasing activities. In January 1996, Mr. Link was appointed Vice President-Operations and is responsible for supervising property management activities at the Company's operating properties. From 1987 to 1994, he served as Chairman, President and Chief Executive Officer of The Ribbon Outlet, Inc., an affiliate of the world's largest ribbon manufacturer, and in that capacity opened over 100 factory outlet stores across the United States. From 1971 to 1987 he held various senior merchandising positions with Phillips-Van Heusen Corporation, Westpoint Pepperell Corporation, May Department Stores and Associated Dry Goods Corporation. Mr. Link graduated from the College of Business and Public Administration of the University of Arizona at Tucson.

Michele Rothstein, Vice President-Marketing since 1993. Ms. Rothstein joined Chelsea in 1989 as Vice President-Marketing. As Vice President-Marketing of the Company, she oversees all aspects of the Company's marketing and promotion activities. From 1987 to 1989, she was a product manager at Regina Company and, prior to 1987, was with Waring & LaRosa Advertising in New York. Ms. Rothstein graduated from the School of Business at the State University of New York at Albany.

Sharon M. Vuskalns, Controller since 1997. Ms. Vuskalns joined the Company in 1995 as Director of Accounting Services. As Controller, she oversees the accounting, tax and financial reporting activities for the Company. Prior to joining Chelsea, Ms. Vuskalns was a Senior Audit Manager with Ernst & Young, LLP. Ms. Vuskalns graduated from Indiana University and is a certified public accountant.

David C. Bloom and William D. Bloom are brothers.

PART II

Item 5. Market for the Registrant's Common Stock and Related Security Matters

The common stock of the Company is traded on the New York Stock Exchange under the ticker symbol CPG. As of February 17, 2004, the closing market price of the Company's stock was \$55.97 per share and there were 476 shareholders of record. The Company believes it has more than 18,000 beneficial holders of common stock. The following table presents the quarterly high and low closing sales price per share (source: The Wall Street Journal) and the cash distributions declared in 2003 and 2002. All share and per share data has been adjusted to reflect a 2-for-1 stock split that was paid as a stock dividend on May 28, 2002 to shareholders of record on May 14, 2002:

| Quarter Ended ----- | Sales Price (\$) | | Distributions |
|-------------------------------|-------------------------|-------------------|----------------------|
| | High ---- | Low --- | (\$) --- |
| December 31, 2003 | \$56.13 | \$47.80 | \$ 0.535 |
| September 30, 2003 | 47.90 | 41.20 | 0.535 |
| June 30, 2003 | 43.90 | 37.63 | 0.535 |
| March 31, 2003 | 38.50 | 32.18 | 0.535 |
| December 31, 2002 | \$35.40 | \$31.13 | \$ 0.485 |
| September 30, 2002 | 34.59 | 26.40 | 0.485 |
| June 30, 2002 | 35.03 | 26.80 | 0.485 |
| March 31, 2002 | 27.40 | 23.93 | 0.405 |

While the Company intends to continue paying regular quarterly dividends, future dividend declarations will be at the discretion of the Board of Directors and will depend on the cash flow and financial condition of the Company; capital requirements; annual distribution requirements under the REIT provisions of the Internal Revenue Code; covenant limitations under the Senior Credit Facility and the Term Notes; and such other factors as the Board of Directors

deems relevant.

Item 6: Selected Financial Data

| | (In thousands except per share and number of cents) | | | |
|--|---|--------------|--------------|------------|
| | Year Ended December 31, | | | |
| Operating Data: | 2003 | 2002 | 2001 | 2000 |
| ----- | ---- | ---- | ---- | ---- |
| Rental revenue..... | \$ 277,028 | \$202,021 | \$ 142,498 | \$ 123,525 |
| Total revenues..... | 372,265 | 278,489 | 202,882 | 176,488 |
| Total expenses..... | 260,940 | 194,958 | 147,450 | 121,878 |
| Income from unconsolidated investments..... | 11,006 | 9,802 | 15,025 | 6,723 |
| Loss from and impairment of Chelsea Interactive | (2,518) | (47,756) | (5,337) | (2,364) |
| Gain (loss) on sale or write-down of assets..... | - | 10,911 | 617 | - |
| Income from continuing operations before minority interest..... | 119,813 | 56,488 | 65,737 | 58,969 |
| Minority interest..... | (22,225) | (12,523) | (14,582) | (14,359) |
| (Loss) income from discontinued operations, net of minority interest..... | (844) | 1,171 | 659 | 1,170 |
| Gain on sale of discontinued operation, net of minority interest..... | 4,784 | - | - | - |
| Net income..... | 101,528 | 45,136 | 51,814 | 45,780 |
| Preferred dividend..... | (3,336) | (3,422) | (4,188) | (4,188) |
| Net income available to common shareholders..... | \$98,192 | \$ 41,714 | \$ 47,626 | \$ 41,592 |
| Net income per common share (diluted) (1) (2)..... | \$2.20 | \$1.05 | \$1.37 | \$1.29 |
| Ownership Interest: (2) | | | | |
| REIT common shares..... | 44,597 | 39,798 | 34,710 | 32,252 |
| Operating Partnership units..... | 7,442 | 6,426 | 6,358 | 6,712 |
| Weighted average shares/units outstanding | 52,039 | 46,224 | 41,068 | 38,964 |
| Balance Sheet Data: | | | | |
| Rental properties before accumulated depreciation..... | \$2,072,783 | \$ 1,837,174 | \$ 1,127,906 | \$908,344 |
| Total assets..... | 1,970,414 | 1,703,030 | 1,099,308 | 901,314 |
| Unsecured and mortgage debt..... | 1,211,472 | 1,030,820 | 548,538 | 450,353 |
| Total liabilities | 1,304,880 | 1,107,756 | 624,246 | 528,752 |
| Minority interest..... | 144,688 | 139,443 | 115,639 | 101,203 |
| Redeemable preferred stock..... | 38,731 | 38,731 | 48,385 | 48,385 |
| Stockholders' equity..... | 520,846 | 455,831 | 359,423 | 271,359 |
| Distributions declared per common share (2) | \$2.14 | \$ 1.86 | \$1.56 | \$1.50 |
| Other Data: | | | | |
| Funds from operations (1) | \$185,095 | \$131,771 | \$108,862 | \$ 93,556 |
| Cash flows from: | | | | |
| Operating activities..... | \$181,634 | \$128,222 | \$121,723 | \$ 106,658 |
| Investing activities..... | (213,603) | (404,178) | (112,551) | (121,479) |
| Financing activities..... | 27,894 | 273,903 | (2,604) | 23,995 |
| GLA at end of period (3)..... | 16,127 | 14,386 | 12,574 | 8,159 |
| Weighted average GLA (4)..... | 15,249 | 12,758 | 9,349 | 5,703 |
| Centers in operation at end of the period..... | 60 | 58 | 57 | 27 |
| New centers developed..... | 2 | - | - | 4 |
| Centers expanded | 2 | 4 | 1 | 3 |

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| | | | | |
|--|---|---|----|---|
| Centers sold and lease terminated..... | 3 | 5 | 1 | 1 |
| Centers held for sale..... | 1 | - | - | - |
| Centers acquired | 2 | 7 | 31 | 4 |

Notes to Selected Financial Data:

- 1) Management believes that funds from operations ("FFO") should be considered in conjunction with net income, as presented in the statements of operations included elsewhere herein, to facilitate a clearer understanding of the operating results of the Company. The White Paper on Funds from Operations approved by the Board of Governors of NAREIT in October 1999 defines FFO as net income (loss) (computed in accordance with GAAP), excluding gains (or losses) from debt restructuring and sales of properties, plus real estate related depreciation and amortization and after adjustments for unconsolidated partnerships and joint ventures. The Company believes that FFO is helpful to investors as a measure of the performance of an equity REIT because, along with cash flow from operating activities, financing activities and investing activities, it provides investors with an indication of the ability of the Company to incur and service debt, to make capital expenditures and to fund other cash needs. FFO for the year ended December 31, 2002, excludes the Chelsea Interactive impairment loss of \$34.4 million. Since all companies do not calculate FFO in a similar fashion, the Company's calculation of FFO presented herein may not be comparable to similarly titled measure as reported by other companies. FFO does not represent cash generated from operating activities in accordance with GAAP and should not be considered as an alternative to net income (determined in accordance with GAAP) as an indication of the Company's financial performance or to cash flow from operating activities (determined in accordance with GAAP) as a measure of the Company's liquidity, or is it indicative of funds available to fund the Company's cash needs, including its ability to make cash distributions.

- 2) Assumes that the 2-for-1 stock split on May 28, 2002 had occurred on January 1, 1999.

- 3) At December 31, 2003, includes four joint venture centers, ownership share ranging between 40% and 50%, containing a total of 1,255,000 square feet of GLA. At year-end 2002, includes two 40% owned centers containing 470,000 square feet of GLA; at year-end 2001 and 2000 includes seven centers containing 2.4 million square feet of GLA in which the Company had joint venture interests ranging from 40% to 50%.

- 4) GLA weighted by months in operation.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in connection with the Financial Statements and notes thereto appearing elsewhere in this annual report.

Certain comparisons between periods have been made on a percentage or weighted average per square foot basis. The latter technique adjusts for square-footage changes at different times during the year.

Critical Accounting Policies and Estimates

The Company's discussion and analysis of its financial condition and results of operations are based upon the Company's consolidated financial statements which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under

different assumptions or conditions.

The Company believes that the critical accounting policies affect its more significant judgments and estimates used in the preparation of its consolidated financial statements.

Bad Debt

The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of its tenants to make required rent payments. If the financial condition of the Company's tenants were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. The Company's allowance for doubtful accounts included in tenant accounts receivable totaled \$1.6 million and \$2.6 million at December 31, 2003 and 2002, respectively.

Valuation of Investments

On a periodic basis, the Company's management team assesses whether there are any indicators that the value of real estate properties, including joint venture properties may be impaired. If the carrying amount of the property is greater than the estimated expected future cash flow (undiscounted and without interest charges) of the asset, impairment has occurred. The Company will then record an impairment loss equal to the difference between the carrying amount and the fair value of the asset. The Company does not believe that the value of any of its rental properties were impaired at December 31, 2003, 2002 and 2001. The Company recorded \$34.4 million impairment loss in 2002 on its investment in Chelsea Interactive and a \$1.2 million loss in 2001 for an impairment write-down of its investment in an outlet center in Guam.

Purchase Price Allocation

The Company allocates the purchase price of real estate to land, building, tenant improvements and if determined to be material, intangibles, such as the value of above, below and at market leases and origination cost associated with in-place leases. The Company depreciates the amount allocated to building and other intangible assets over their estimated useful lives, which generally range from five to forty years. The values of the above and below market leases are amortized and recorded as either an increase (in the case of below market leases) or a decrease (in the case of above market leases) to rental income over the remaining term of the associated lease. The values associated with in-place leases are amortized over the term of the lease. If a tenant vacates its space prior to the contractual termination of the lease and no rental payments are being made on the lease, any unamortized balance of the related intangible will be written off. The tenant improvements and origination costs are amortized as an expense over the remaining life of the lease (or charged against earnings if the lease is terminated prior to contractual expiration date). The Company assesses fair value based on estimated cash flow projections that utilize appropriate discount and capitalization rate and available market information. Estimates of future cash flows are based on a number of factors including the historical operating results, known trends and market/ economic conditions that may affect the property.

General Overview

During the three-year period ended December 31, 2003, rental revenues grew from \$123.5 million to \$277.0 million, representing an increase of \$153.5 million, or 124%. The incremental growth was driven by expanding seven centers, acquiring 41 centers, buying out partners' interests in five centers and increasing rents. Growth was further enhanced through joint venture development of two new Premium Outlet centers and the expansion of two other Premium Outlet centers. From January 1, 2001 to December 31, 2003, the number of centers more than doubled from 27 to 60 centers, while GLA increased by 8.0 million square feet or 97.8%.

Base rent on average increased 35.2%, or \$48.0 million per year, during the same three-year period, primarily from the acquisitions of domestic properties that contributed aggregate incremental revenue of \$77.8 million and the buyout

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of partners' interests that added \$42.9 million. Expansions contributed \$11.3 million during the three-year period.

Income from unconsolidated investments during the three-year period ended December 31, 2003, contributed \$46.7 million, including a \$10.9 million gain on sale of minority interests in 2002. As previously mentioned, since January 1, 2001, the Company with its joint venture partners, developed two new premium centers and expanded two premium centers. During 2002, the Company purchased the remaining interest from two joint venture partners and became the sole owner of five centers whose operating results were fully consolidated since their buyout.

At December 31, 2003, the Company's portfolio consisted of 60 wholly or partially owned properties containing 16.1 million square feet of GLA. Premium Properties include 30 centers containing 10.6 million square feet of GLA and 30 Other Properties containing 5.5 million square-feet of GLA.

Details of the 8.0 million square feet of net GLA added are as follows:

| | Since Jan 1, 2001 | 2003 | 2002 |
|--|----------------------|--------------|--------------|
| | ----- | ---- | ---- |
| Changes in GLA (sf in 000's): | | | |
| New centers developed: | | | |
| Las Vegas Premium Outlets (50% owned) | 435 | 435 | - |
| Sano Premium Outlets (40% owned) | 180 | 180 | - |
| | ----- | ----- | ----- |
| Total new centers. | 615 | 615 | - |
| Centers expanded: | | | |
| Gotemba Premium Outlets (40% owned) | 170 | 170 | - |
| Albertville Premium Outlets | 125 | 125 | - |
| Rinku Premium Outlets (40% owned) | 70 | - | 70 |
| Desert Hills Premium Outlet | 23 | - | 23 |
| Liberty Village Premium Outlets | 23 | - | 23 |
| Napa Premium Outlets | 9 | - | 9 |
| Allen Premium Outlets | 146 | - | - |
| Other (net) | (43) | (30) | (17) |
| | ----- | ----- | ----- |
| Total centers expanded. | 523 | 265 | 108 |
| Centers acquired: | | | |
| Las Vegas Outlet Center | 477 | 477 | - |
| The Crossings Factory Stores | 390 | 390 | - |
| Lakeland Factory Outlet Mall (1) | 319 | 319 | - |
| Osage Beach Premium Outlets | 391 | - | 391 |
| St. Augustine Premium Outlets | 329 | - | 329 |
| Edinburgh Outlet Center | 305 | - | 305 |
| Albertville Premium Outlets | 305 | - | 305 |
| Factory Merchants Branson | 300 | - | 300 |
| Jackson Outlet Village | 292 | - | 292 |
| Johnson Creek Outlet Center | 278 | - | 278 |
| Kittery Premium Outlets II (2) | 21 | - | - |
| 30 Other Properties (3) | 4,279 | - | - |
| | ----- | ----- | ----- |
| Total centers acquired | 7,686 | 1,186 | 2,200 |
| Centers disposed: | | | |
| American Tin Cannery Premium Outlets (4) | (135) | (135) | - |
| St. Helena Premium Outlets | (23) | (23) | - |
| Mammoth Premium Outlets | (35) | - | - |
| Other Properties (5) | (663) | (167) | (496) |
| | ----- | ----- | ----- |
| Total centers disposed: | (856) | (325) | (496) |

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| | | | | |
|---|--------------|--------------|--------------|----------|
| Net GLA added during the period..... | 7,968 | 1,741 | 1,812 | 4 |
| Other Data: | | | | |
| GLA at end of period | | 16,127 | 14,386 | 12 |
| Weighted average GLA | | 15,249 | 12,758 | 9 |
| Centers in operation at end of period..... | | 60 | 58 | |
| New centers opened. | | 2 | - | |
| Centers expanded. | | 2 | 4 | |
| Centers acquired | | 3 | 7 | |
| Centers disposed..... | | 3 | 5 | |

- 1) Acquired Lakeland Factory Outlet Mall in August 2003 in conjunction with the Las Vegas Outlet Center. The Lakeland property is being marketed for sale.
- 2) Acquired in the September 25, 2001 Konover Property Trust acquisition transaction and formerly Factory Stores of America at Kittery.
- 3) Acquired in the September 25, 2001 Konover transaction and excludes Vegas Pointe Plaza which was repurchased by Konover on December 3, 2001.
- 4) In January 2004, the Company terminated its long-term lease agreement, expiring December 2004.
- 5) Consists of properties acquired in the September 25, 2001 Konover transaction.

The Company's domestic Premium Properties produced weighted average reported tenant sales of approximately \$399 per square-foot in 2003, \$383 per square-foot in 2002 and \$379 per square-foot in 2001. Weighted average sales are a measure of tenant performance that has a direct effect on base and percentage rents that can be charged to tenants over time.

Woodbury Common Premium Outlets, the Company's largest premium center located in Central Valley, New York, generated approximately 13%, 16%, and 21% of the Company's total revenue for the years ended 2003, 2002 and 2001, respectively. In addition, approximately 23%, 25% and 28% of the Company's revenues for fiscal years 2003, 2002 and 2001, resulted from the Company's centers located in California.

The Company does not consider any single store lease to be material; no individual tenant, combining all of its store concepts, accounts for more than 5% of the Company's gross revenues. VF Corporation occupied 8% of the Company's total domestic GLA at December 31, 2003, and was the only tenant that occupied more than 5% of GLA at year end. In view of these results and the Company's past success in re-leasing available space, the Company believes that the loss of any individual tenant would not have a significant effect on future operations.

The discussion below is based upon income from continuing operations before minority interest. The minority interest in net income varies from period to period as a result of changes in Operating Partnership interests.

Comparison of year ended December 31, 2003 to year ended December 31, 2002.

Income from continuing operations before minority interest was \$119.8 million, an increase of \$63.3 million, or 112.1%, from \$56.5 million in 2002. The increase resulted primarily from the acquisitions of seven centers in 2002 and three centers in 2003, the buyout of ownership interests in five centers in 2002 previously reported as unconsolidated investments, higher rents from releasing and renewals, and a decrease in the loss from Chelsea Interactive. These increases to income were largely offset by the 2002 gain of \$10.9 million, which reflects the sale of a portion of the Company's interest in Value Retail in 2002 and higher operating and maintenance, general and administrative, interest and other expenses due to the expansion of the portfolio.

Base rentals increased \$69.6 million, or 39.0%, to \$247.9 million in 2003 from \$178.3 million in 2002 due to the acquisitions of ten centers, the buyout of partnership interests in five centers, higher average rents on releasing and

renewals, and the expansion of two wholly-owned centers in late 2002. Base rental revenue per weighted average square-foot in the Premium Properties increased to \$22.57 from \$21.30 a year earlier.

Percentage rents rose \$5.4 million, or 22.8%, to \$29.1 million in 2003 from \$23.7 million in 2002, primarily due to improved tenant sales, the acquisition of ten centers and the buyout of ownership interests in five centers in 2002.

Expense reimbursements, representing contractual recoveries from tenants of certain common area maintenance, operating, real estate tax and promotional and management expenses, increased \$21.6 million, or 33.3% to \$86.5 million in 2003 from \$64.9 million in 2002, due to the recovery of operating and maintenance costs from increased GLA. In 2003, the average recovery of reimbursable expenses for the Premium Properties was 88.4% compared with 90.6% in 2002. The average recovery of reimbursable expenses for the Other Retail centers improved to 72.0% in 2003, compared with 52.6% in the previous year. The increase from Other Retail centers was a result of better recovery of expenses at centers acquired in 2002.

Other income decreased \$2.9 million or 24.6% to \$8.7 million in 2003, from \$11.6 million in 2002. The decrease was primarily due to the expiration of the non-compete agreement which included income recognition of \$5.1 million in 2002, and decreased interest income from lower interest rates, partially offset by increased ancillary operating income and the sale of two outparcels in 2003.

Operating and maintenance expenses increased \$25.1 million, or 32.2%, to \$103.0 million in 2003 from \$77.9 million in 2002 primarily due to costs related to increased GLA and the buyouts of ownership interests in five centers during 2002. On a weighted average square-foot basis, Premium Properties operating and maintenance expenses increased to \$9.26 in 2003 from \$9.21 in 2002 primarily due to increased snow removal costs.

Depreciation and amortization expense was up \$13.9 million, or 24.5%, to \$70.8 million in 2003 from \$56.9 million in 2002 due to increased depreciation from the acquisition of the ten centers and the buyouts of ownership interests during 2002.

General and administrative expense grew \$5.3 million, or 75.2%, to \$12.4 million in 2003 from \$7.1 million in 2002. Approximately \$1.5 million of the increase is a one time charge due to timing of recognition of deferred compensation expense required under FIN 28. The balance was due to increased cost for corporate governance, compensation, including deferred compensation accrual, benefits and professional fees.

Other expenses increased \$1.0 million, or 25.8%, to \$5.0 million in 2003 from \$4.0 million in 2002 due to ground leases assumed with the acquisition of new centers, legal expenses and increased bad debt expense.

Income from unconsolidated investments was up \$1.2 million, or 12.3%, to \$11.0 million in 2003 from \$9.8 million in 2002 due to higher earnings from Chelsea Japan and Las Vegas Premium Outlets, which opened in August 2003 partially offset by the buyouts of ownership interests in five centers in 2002 that required full consolidation of the operating results from the buyout date.

The operating loss from Chelsea Interactive decreased \$45.3 million, or 94.7%, to \$2.5 million in 2003 from \$47.8 million in 2002 due to the write-off of the Company's investment at December 31, 2002. The Company recorded an impairment loss of \$34.4 million at fiscal year-end 2002.

Interest expense increased \$20.6 million, or 41.9%, to \$69.8 million in 2003, from \$49.2 million in 2002 due to higher debt that financed acquisitions and buyouts of partners' interests.

Gain on sale of unconsolidated investments of \$10.9 million in 2002 resulted from the sale of approximately 40% of the Company's partial interest in Value Retail PLC.

Gain on sale of discontinued operations of \$4.8 million, net of minority interest primarily reflects the sale of two centers in 2003.

Comparison of year ended December 31, 2002 to year ended December 31, 2001.

Income from continuing operations before minority interest was \$56.5 million in 2002, representing a decrease of \$9.2 million, or 14.1%, from \$65.7 million in 2001. This decrease was primarily the result of an operating loss and impairment loss from Chelsea Interactive of \$47.8 million in 2002 compared with an operating loss of \$5.3 million in 2001. These losses were substantially offset by the acquisition of 31 centers in September 2001, the buyout and consolidation of five centers previously held as unconsolidated investments, the acquisition of seven centers and higher rents on releasing and renewals. Income before interest expense and minority interest increased \$2.7 million to \$105.7 million in 2002 from \$103.0 million in 2001 due to additional GLA, a gain resulting from the partial sale of an unconsolidated investment, substantially offset by the impairment loss from Chelsea Interactive.

Base rents increased \$53.7 million, or 43.0%, to \$178.3 million in 2002 from \$124.6 million in 2001 due to the acquisition of 38 centers; the buyouts of ownership interests in five centers in 2002; and higher average rents as a result of higher rental rates on new leases and renewals. Base rental revenue per weighted average square-foot in the Premium Properties increased to \$21.30 in 2002 from \$20.39 in 2001.

Percentage rents increased \$5.8 million, or 32.9%, to \$23.7 million in 2002 from \$17.9 million in 2001 primarily due to higher tenant sales, the acquisition of the 38 centers and the buyouts of ownership interests in five centers during 2002.

Expense reimbursements, representing contractual recoveries from tenants of certain common area maintenance, operating, real estate tax, promotional and management expenses, increased \$15.4 million, or 31.1%, to \$64.9 million in 2002 from \$49.5 million in 2001 due to the recovery of operating and maintenance costs from increased GLA. The average recovery of reimbursable expenses for the Premium Properties was 90.6% for 2002 and 2001. The average recovery of reimbursable expenses for the Other Properties improved to 52.6% in 2002 compared with 51.1% in 2001.

Other income increased \$0.7 million, or 6.5%, to \$11.6 million in 2002 from \$10.9 million in 2001 primarily due to increased ancillary operating income from the acquisition of the 38 centers; the buyouts of ownership interests in five centers in 2002; and gains from sale of five Other Properties and an outparcel during 2002, partially offset by decreased interest income from lower interest rates.

Operating and maintenance expenses increased \$21.6 million, or 38.4%, to \$77.9 million in 2002 from \$56.3 million in 2001 primarily due to costs related to increased GLA and the buyouts of ownership interests in five centers during 2002. On a weighted average square-foot basis, Premium Properties operating and maintenance expenses increased to \$9.21 in 2002 from \$9.16 in 2001.

Depreciation and amortization expense increased \$10.1 million, or 21.6%, to \$56.9 million in 2002 from \$46.8 million in 2001 due to additional depreciation from the acquisition of the 38 retail centers, the buyouts of ownership interests in five centers in 2002 and expansions.

General and administrative expense increased \$2.5 million, or 53.1%, to \$7.1 million in 2002 from \$4.6 million in 2001 primarily due to increased professional fees, head count and deferred compensation accrual.

Other expenses increased \$1.5 million, or 56.3%, to \$4.0 million in 2002 from \$2.5 million in 2001 due to ground leases assumed with the acquisition of new centers, legal expenses and increased bad debts.

Income from unconsolidated investments decreased \$5.2 million, or 34.8%, to \$9.8 million in 2002 from \$15.0 million in 2001 due to buyouts of ownership interests in five centers that required that operations of these centers be

fully consolidated from the buyout date, partially offset by higher earnings from Chelsea Japan.

The loss from Chelsea Interactive operations increased \$8.1 million, or 150.8%, to \$13.4 million in 2002 from \$5.3 million in 2001. The increase was due to increased operating payroll, general and administrative, depreciation and amortization expense and lack of third party participation in the losses. The Company also recorded an impairment loss of \$34.4 million as of December 31, 2002.

Gain on sale of unconsolidated investments of \$10.9 million in 2002 resulted from the sale of approximately 40% of the Company's partial interest in Value Retail. The 2001 gain on sale of \$0.6 million was also from the sale of a partial interest in Value Retail offset by the write-off of the Company's investment in Guam.

Interest in excess of amounts capitalized increased \$11.9 million, or 32.0%, to \$49.2 million in 2002 from \$37.3 million in 2001, primarily due to higher debt from acquisitions and joint venture buyouts, partially offset by lower interest rates.

Liquidity and Capital Resources

The Company believes it has adequate financial resources to fund operating expenses, distributions, and planned development, construction and acquisition activities over the short term, which is less than 12 months and the long term, which is 12 months or more. Operating cash flow for the year ended December 31, 2003 of \$181.6 million is expected to increase from 1.7 million square feet of GLA added during 2003, including a full year of operations from the two joint venture openings and the acquisition of three centers as well as scheduled openings and expansions of approximately 0.9 million square feet of new GLA in 2004. As of December 31, 2003, the Company has a commitment of \$30.0 million for active domestic development projects. The Company has adequate funding sources to complete these projects from available cash, credit facilities and secured construction financing. The Company also has access to the public markets through its \$1.55 billion debt and equity shelf registrations for funding or refinancing requirements.

Operating cash flow is expected to provide sufficient funds for dividends and distributions in accordance with REIT federal income tax requirements. In addition, the Company anticipates retaining sufficient operating cash to fund re-tenanting and lease renewal tenant improvement costs, as well as capital expenditures to maintain the quality of its centers, meet funding requirements of Chelsea Interactive and partially fund development projects.

Common distributions declared and recorded in 2003 were \$107.8 million, or \$2.14 per share or unit. The Company's dividend payout ratio as a percentage of net income before minority interest, gain or loss on sale or writedown of assets and depreciation and amortization (reduced by amortization of deferred financing costs, depreciation of non-real estate assets and preferred dividends ("FFO")) was 58.2%. The Company's senior unsecured bank line of credit ("Senior Credit Facility") limits aggregate dividends and distributions to the lesser of (i) 90% of FFO on an annual basis or (ii) 100% of FFO for any two consecutive quarters.

The Company's ratio of earnings-to-fixed charges for each of the three years ended December 31, 2003, 2002, and 2001 was 2.5, 2.4 and 2.6, respectively. For purposes of computing the ratio, earnings consist of income from continuing operations after depreciation and before minority interest and fixed charges, exclusive of interest capitalized and amortization of loan costs capitalized and impairment losses. Fixed charges consist of interest expense, including interest costs capitalized, the portion of rent expense representative of interest and total amortization of debt issuance costs expensed and capitalized.

The Company's \$200.0 million Senior Credit Facility expires in March 2005 (unless extended until March 2006), bears interest on the outstanding balance at an annual rate equal to the London Interbank Offered Rate ("LIBOR") plus 0.95% (2.09% at December 31, 2003) or the prime rate, at the Company's option, and has an annual facility fee of 0.125%. The LIBOR rate spread ranges from 0.85% to 1.50% depending on the Company's Senior Debt rating. The

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Company received a debt rating upgrade in July 2003, resulting in a reduction of the LIBOR rate spread to 0.95% from 1.05%. At December 31, 2003, \$99.0 million was outstanding under the Senior Credit Facility.

During 2003, the Company completed two acquisition transactions valued at approximately \$219.0 million. On June 12, 2003, the Company purchased The Crossings Factory Stores, a 390,000 square-foot outlet center located in Tannersville, Pennsylvania, for \$111.3 million, including closing costs and the assumption of a \$60.7 million 5.85% mortgage loan due 2013. In conjunction with The Crossings Factory Stores acquisition, the Company completed an offering of 1.2 million shares of common stock at a price of \$42.10 per share. Net proceeds after expenses of \$49.4 million were used to fund substantially the entire cash portion of the acquisition.

On August 1, 2003, the Company acquired Las Vegas Outlet Center, a 477,000 square-foot outlet center in Las Vegas, Nevada, for \$104.0 million including the assumption of a \$24.4 million 8.12% mortgage loan due 2012. As part of the transaction, the Company also acquired Lakeland Factory Outlet Mall, a 319,000 square-foot outlet center near Memphis, Tennessee for an additional \$3.5 million. The Lakeland property is being marketed for sale. The approximately \$84.0 million cash portion of the overall transaction was financed with a \$100.0 million one-year term loan facility at an annual interest rate of LIBOR plus 0.80% (1.96% at December 31, 2003) that is due on July 31, 2004 and extendible for six months until January 31, 2005 at the Company's option. The LIBOR rate spread ranges from 0.70% to 1.35% depending on the Company's Senior Debt rating. Surplus proceeds from the financing of approximately \$16.0 million were used for general corporate purposes.

A summary of the Company's contractual obligations (at par) as of December 31, 2003, is as follows (in thousands):

| | Total | Less than 1 Year | 1 to 3 Years | 3 to 5 Years | M |
|-----------------------------|--------------------|---------------------|------------------|------------------|-----------|
| Unsecured bank debt | \$ 204,035 | \$100,000 | \$104,035 | \$ - | \$ |
| Unsecured notes | 625,000 | - | 50,000 | 125,000 | |
| Mortgage debt | 375,433 | 7,873 | 18,889 | 167,587 | |
| Total debt | 1,204,468 | 107,873 | 172,924 | 292,587 | |
| Ground and operating leases | 24,634 | 2,299 | 2,609 | 2,358 | |
| Real estate commitments | 49,670 | 49,670 | - | - | |
| Deferred compensation | 17,600 | - | - | 17,600 | |
| Total Obligations | \$1,296,372 | \$159,842 | \$175,533 | \$312,545 | \$ |

At December 31, 2003, construction for international and domestic development includes projects totaling 0.9 million square-feet of GLA. Internationally, projects in the pipeline include the 187,000 square-foot first phase of Tosu Premium Outlets near Fukuoka, Japan, scheduled to open in March 2004; and the 230,000 square-foot first phase of Punta Norte Premium Outlets in Mexico City scheduled to open in late 2004. Domestically, projects underway include the single-phase 438,000 square-foot Chicago Premium Outlets, scheduled to open in mid 2004. The Tosu project is a development of Chelsea Japan Co., Ltd., the Company's 40%-owned Japanese joint venture. The Punta Norte project is a development of the Company's 50% owned Mexican joint venture. The Chicago project is a 50/50 joint venture with Simon. Other projects in various stages of development are expected to open in 2004 and beyond including the 350,000 square-foot Seattle Premium Outlets, located near Seattle, Washington, scheduled to commence construction in spring 2004 and open in spring 2005. There can be no assurance that these projects will be completed or opened, or that there will not be delays in opening or completion. All current development activity is fully financed either through project specific secured construction financing, the yen denominated line of credit, the peso denominated line of credit, available cash or through the Senior Credit Facility. The Company will seek to obtain permanent financing once the projects are completed and income has been stabilized.

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In connection with the Simon joint venture, the Company has committed to provide 50% of the development costs, or approximately \$46.0 million for Chicago Premium Outlets. As of December 31, 2003, the Company had contributed \$26.7 million to the Chicago project.

The Company has an agreement with Mitsubishi Estate Co., Ltd. and Nissho Iwai Corporation to jointly develop, own and operate Premium Outlet centers in Japan under the joint venture Chelsea Japan. Borrowings related to Chelsea Japan for which the Company and the OP have provided guarantees as of December 31, 2003, are as follows:

| Total Facility | | Outstanding | | | Due |
|-----------------|------------------|-------------|------------------|-----------------|------|
| Yen | US \$ Equivalent | Yen | US \$ Equivalent | US \$ Guarantee | Date |
| --- | ----- | --- | ----- | ----- | --- |
| 4.0 billion (1) | \$37.3 million | 0.9 billion | \$ 8.4 million | \$ 8.4 million | 2004 |
| 3.8 billion (2) | 35.4 million | 3.2 billion | 30.0 million | 12.0 million | 2015 |
| 0.6 billion (2) | 5.6 million | 0.5 billion | 4.7 million | 1.9 million | 2012 |

- (1) Facility entered into by an equity investee of the Company that has a one-year extension option until April 1, 2005.
- (2) Facilities entered into by Chelsea Japan, secured by Gotemba and Rinku and 40% severally guaranteed by the Company.

The Company has a 50/50 joint venture agreement with Sordo Madaleno y Asociados and affiliates to jointly develop, own and operate Premium Outlet centers in Mexico. In July 2003, the first development project broke ground, the 230,000 square-foot first phase of Punta Norte Premium Outlets, located near Mexico City and is scheduled to open in late 2004. The Company is responsible for financing its 50% share of project costs up to approximately \$15.0 million. As of December 31, 2003, the Company had contributed \$2.5 million.

Liquidity and Capital Resources (continued)

In January 2004, a subsidiary of the Company entered into a 180.0 million peso revolving facility (USD \$16.5 million as of February 17, 2004) to provide funding for Mexican development projects. The peso facility has a three-year term and the drawn funds bear interest at The Interbank Interest Equilibrium Rate ("TIIE") plus 0.825% plus the bank's cost of funds spread limited to 20% of the TIIE and has an annual facility fee of 0.15% on the unused balance. The TIIE rate spread ranges from 0.725% to 1.37% depending on the Company's Senior Debt rating.

At December 31, 2002, the Company recognized an impairment loss equal to the net book value of its investment in Chelsea Interactive. The Company believes that it will not be able to recover the net book value of its investment in Chelsea Interactive through future cash flows. For 2003, a \$2.5 million funding loss was reported. Future funding by the Company will be reported, as a loss in the period funding is required. As of December 31, 2003, the Company had funded \$54.9 million and anticipates that Chelsea Interactive will not reach the Company's funding limit of \$60.0 million. On February 17, 2004, the Company announced a joint venture between Chelsea Interactive and a publicly traded third party, GSI Commerce, Inc. ("GSI-Chelsea Solutions"). Under the terms of the agreement, Chelsea Interactive will no longer operate its e-commerce technology, but will retain a minority interest in GSI-Chelsea Solutions. Chelsea Interactive's largest clients have entered into service agreements with GSI-Chelsea Solutions and will transition e-commerce activities to the GSI-Chelsea platform by the second quarter of 2004.

The Company has minority interests ranging from 3% to 8% in several outlet centers and outlet development projects in Europe operated by Value Retail. The Company's total investment in Europe as of December 31, 2003, was \$3.6 million. The Company has also provided \$17.1 million in limited debt service guarantees under a standby facility for

loans arranged by Value Retail to construct outlet centers in Europe. The standby facility for new guarantees, which has a maximum of \$22.0 million, expired in November 2001 and outstanding guarantees shall not survive more than five years after project completion.

To achieve planned growth and favorable returns in both the short and long-term, the Company's financing strategy is to maintain a strong, flexible financial position by: (i) maintaining a conservative level of leverage; (ii) extending and sequencing debt maturity dates; (iii) managing exposure to floating interest rates; and (iv) maintaining liquidity. Management believes that these strategies will continue to enable the Company to access a broad array of capital sources, including bank or institutional borrowings and secured and unsecured debt and equity offerings, subject to market conditions.

Net cash provided by operating activities was \$181.6 million and \$128.2 million for the years ended December 31, 2003, and 2002, respectively. The increase was primarily due to increased operating cash flow generated on the growth of the Company's GLA offset by the decreased losses from Chelsea Interactive and the payout of the deferred incentive compensation in March 2002. Net cash used in investing activities decreased to \$213.6 million in 2003 from \$404.2 million in 2002 due to reduced acquisition activity. Net cash provided by financing activities decreased to \$27.9 million from \$273.9 million for the years ended December 31, 2003, and 2002, respectively. The decrease was primarily the result of reduced borrowings, debt repayments and higher distributions in 2003.

Funds from Operations

Management believes that funds from operations ("FFO") should be considered in conjunction with net income, as presented in the statements of operations included elsewhere herein, to facilitate a clearer understanding of the operating results of the Company. The White Paper on Funds from Operations approved by the Board of Governors of NAREIT in October 1999 defines FFO as net income (loss) (computed in accordance with GAAP), excluding gains (or losses) from debt restructuring and sales of properties, plus real estate related depreciation and amortization and after adjustments for unconsolidated partnerships and joint ventures. The Company believes that FFO is helpful to investors as a measure of the performance of an equity REIT because, along with cash flow from operating activities, financing activities and investing activities, it provides investors with an indication of the ability of the Company to incur and service debt, to make capital expenditures and to fund other cash needs.

FFO for the year ended December 31, 2002, excludes the Chelsea Interactive impairment loss of \$34.4 million. Since all companies do not calculate FFO in a similar fashion, the Company's calculation of FFO presented herein may not be comparable to similarly titled measure as reported by other companies. FFO does not represent cash generated from operating activities in accordance with GAAP and should not be considered as an alternative to net income (determined in accordance with GAAP) as an indication of the Company's financial performance or to cash flow from operating activities (determined in accordance with GAAP) as a measure of the Company's liquidity, or is it indicative of funds available to fund the Company's cash needs, including its ability to make cash distributions.

Funds from Operations (continued)

| | Year Ended December 31, | | |
|--|-------------------------|----------|----------|
| | 2003 | 2002 | 2001 |
| Net income available to common shareholders | \$98,192 | \$41,714 | \$47,626 |
| Depreciation and amortization-wholly-owned..... | 73,651 | 58,275 | 48,554 |
| Depreciation and amortization-joint ventures..... | 4,069 | 4,166 | 5,964 |
| Amortization of deferred financing costs and depreciation of non-rental real estate assets..... | (2,274) | (2,401) | (1,807) |
| Net gain on sale or write-down of assets..... | (4,784) | (11,223) | (333) |
| Chelsea Interactive impairment loss..... | - | 34,370 | - |
| Minority interest..... | 22,089 | 12,718 | 14,706 |

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| | | | |
|---|-----------|-----------|-----------|
| Preferred unit distribution..... | (5,848) | (5,848) | (5,848) |
| FFO..... | \$185,095 | \$131,771 | \$108,862 |
| Average diluted shares/units outstanding (1)..... | 52,039 | 46,224 | 41,068 |
| FFO per share..... | \$3.56 | \$2.85 | \$2.65 |
| Dividends declared per share..... | \$2.14 | \$1.86 | \$1.56 |

(1) Assumes 2-for-1 stock split in May 2002 had occurred on January 1, 2001.

Recent Accounting Pronouncements

In October 2001, the FASB issued Statement of Financial Accounting Standard No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144") which was effective and adopted by the Company on January 1, 2002. SFAS 144 provides accounting guidance for financial accounting and reporting for impairment or disposal of long-lived assets. SFAS 144 supersedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of." SFAS 144 retains fundamental provisions of SFAS 121 related to the recognition and measurement of the impairment of long-lived assets to be held and used. In addition, SFAS 144 superseded APB Opinion 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." SFAS 144 extended the reporting of a discontinued operation to a "component of an entity." Thus, the operations of assets sold or held for sale are presented as discontinued operations in the Company's statement of income.

In June 2002, FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146") which was effective for exit or disposal activities initiated after December 31, 2002. SFAS 146 requires that a liability for a cost associated with an exit or disposal activity be recognized and measured initially at fair value only when the liability is incurred. See note 6 to financial statements for discussion related to the estimated future costs to be incurred in connection with the future operations of Chelsea Interactive.

In November 2002, the FASB issued No. 45, Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others ("FIN 45"). FIN 45 requires certain guarantees to be recorded at fair value, instead of recording a liability only when a loss is probable and reasonably estimable, as those terms are defined in FASB Statement No. 5, Accounting for Contingencies. FIN 45 also requires a guarantor to make significant new disclosures, even when the likelihood of making any payments under the guarantee is remote. The disclosure requirements of FIN 45 are effective for financial statements of interim or annual periods ending after December 15, 2002. The Company adopted the disclosure provisions of FIN 45 effective December 31, 2002. FIN 45's initial recognition and initial measurement provisions are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. The adoption of FIN 45 did not have a material impact on the Company's financial position or the results of operations.

Recently Issued Accounting Pronouncements (continued)

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities" ("FIN 46"). FIN 46 clarifies the application of existing accounting pronouncements to certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. The provisions of FIN 46 will be immediately effective for all variable interests in variable interest entities created after January 31, 2003. The Company has not created any variable interest entities subsequent to January 31, 2003. In December 2003, FASB issued a revision to Interpretation 46 ("FIN 46-R") to clarify the provisions of FIN 46. The application of FIN 46-R is effective for public companies, other than small business issuers, after March 15, 2004. The Company does not believe that FIN 46-R will have a significant impact on the Company's financial statements.

On April 30, 2003, FASB issued SFAS No.149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities" ("SFAS 149"). SFAS 149 amends and clarifies the accounting guidance on (1) derivative instruments (including certain derivative instruments embedded in other contracts) and (2) hedging activities that fall within the scope of SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"). SFAS 149 also amends certain other existing pronouncements, which will result in more consistent reporting of contracts that are derivatives in the entirety or that contain embedded derivatives that warrant separate accounting. SFAS 149 is effective (1) for contracts entered into or modified after June 30, 2003, with certain exceptions, and (2) for hedging relationships designed after June 30, 2003. The guidance is to be applied prospectively. The adoption of SFAS 149 did not have a material impact on the Company's financial condition, or results of operations or cash flows.

In May 2003, FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity" ("SFAS 150"). This statement establishes standards for the classification and measurement of certain financial instruments with characteristics of both liabilities and equity. SFAS 150 is effective for financial instruments entered into or modified after May 31, 2003 and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003. It is to be implemented by reporting the cumulative effect of a change in accounting principle for financial instruments created before the issuance date of the statement and still existing at the beginning of the interim period of adoption. The implementation of SFAS 150 did not have a material impact on the Company's financial condition, results of operations or cash flows.

Economic Conditions

Substantially all leases contain provisions, including escalations of base rents and percentage rentals calculated on gross sales, to mitigate the impact of inflation. Inflationary increases in common area maintenance and real estate tax expenses are substantially reimbursed by tenants.

Virtually all tenants have met their lease obligations and the Company continues to attract and retain quality tenants. The Company intends to reduce operating and leasing risks by continually improving its tenant mix, rental rates and lease terms and by pursuing contracts with creditworthy upscale and national brand-name tenants.

Item 7-A. Quantitative and Qualitative Disclosures about Market Risk

The Company is exposed to changes in interest rates primarily from its floating rate debt arrangements. In December 2000, the Company implemented a policy to protect against interest rate and foreign exchange risk. The Company's primary strategy is to protect against these risks by using derivative transactions as appropriate to minimize the variability that floating rate interest and foreign currency fluctuations could have on cash flow. In December 2000, a wholly-owned subsidiary of the Company entered into an interest rate swap agreement effective January 2, 2001 with a financial institution for a notional amount of \$69.3 million amortizing to \$64.1 million to hedge against unfavorable fluctuations in the LIBOR rates of one of its mortgage loans. The hedge effectively produces a fixed rate of 7.2625% on the notional amount until January 1, 2006.

At December 31, 2003 a hypothetical 100 basis point adverse move (increase) in US Treasury and LIBOR rates applied to unhedged debt would adversely affect the Company's annual interest cost by approximately \$2.0 million annually.

Following is a summary of the Company's debt obligations at December 31, 2003 (in thousands):

| | Expected Maturity Date | | | | | | |
|------------------------|------------------------|-----------|------|-----------|-----------|------------|-----------|
| | 2004 | 2005 | 2006 | 2007 | 2008 | Thereafter | Total |
| Fixed Rate Debt: | \$ - | \$ 49,952 | - | \$124,874 | \$164,727 | \$606,408 | \$945,961 |
| Average Interest Rate: | - | 8.38% | - | 7.25% | 6.99% | 7.18% | 7.22% |

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| | | | | | | | |
|------------------------|---------|---------|---|---|---|------------|---------|
| Variable Rate Debt: | 100,000 | 104,035 | - | - | - | 61,475 (1) | 265,510 |
| Average Interest Rate: | 1.96% | 2.09% | - | - | - | 2.62% | 2.16% |

(1) Subject to an interest rate swap which effectively produces a fixed rate of 7.2625% until January 1, 2006.

Item 8. Financial Statements and Supplementary Data

The financial statements and financial information of the Company for the years ended December 31, 2003, 2002 and 2001 and the Report of the Independent Auditors thereon are included elsewhere herein. Reference is made to the financial statements and schedules in Item 15.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

Our chief executive officer and chief financial officer evaluated the effectiveness of our disclosure controls and procedures (as defined in rule 13a-14c under the Securities Exchange Act of 1934, as amended) as of December 31, 2003 and, based on that evaluation, concluded that, as of the end of the period covered by this report, we had sufficient controls and procedures for recording, processing, summarizing and reporting information that is required to be disclosed in our reports under the Securities Exchange Act of 1934, as amended, within the time periods specified in the SEC's rules and forms.

During the year ended December 31, 2003, there have not been any significant changes to our internal controls including any corrective actions with regard to significant deficiencies and material weaknesses or other factors that could significantly affect these controls.

PART III

Items 10, 11, 12, 13 and 14.

The required information in the items will appear in the Company's Proxy Statement furnished to shareholders in connection with the 2004 Annual Meeting, and is incorporated by reference in this Form 10-K Annual Report.

Item 10. Directors and Executive Officers of the Registrant*

Item 11. Executive Compensation

Item 12. Security Ownership of Certain Beneficial Owners and Management

The information called for by Item 12 is incorporated herein by reference to our definitive proxy statement to be filed pursuant to Regulation 14A, in connection with our annual meeting of shareholders to be held on June 10, 2004, which will involve the election of directors.

The following table provides information as of December 31, 2003 with respect to compensation plans (including individual compensation arrangements) under which the Company's equity securities are authorized for issuance:

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| Plan Category | Number of securities to be issued upon exercise of outstanding options, warrants and rights | Weighted average exercise price of outstanding options, warrants and rights | Number of securities remaining available for future issuance under equity compensation plans (excluding securities in column (a)) |
|--|---|---|--|
| | (a) | (b) | (c) |
| Equity compensation plans approved by security holders | 3,292,000 | \$20.18 | 522,000 |
| Equity compensation plans not approved by security holders | - | - | - |
| Total | 3,292,000 | \$20.18 | 522,000 |

Item 13. Certain Relationships and Related Transactions

Item 14. Principal Accountant Fees and Services

* Certain information regarding Directors and Officers is included at the end of Part I.

PART IV

Item 15. Exhibits, Financial Statement Schedules and Reports on Form 8-K

(a) 1 and 2. The response to this portion of Item 15 is submitted as a separate section of this report.

3. Exhibits

3.1 Articles of Incorporation of the Company, as amended, including Articles Supplementary relating to 8 3/8% Series A Cumulative Redeemable Preferred Stock and Articles Supplementary relating to 9% Series B Cumulative Redeemable Preferred Stock. Incorporated by reference to Exhibit 3.1 to Form 10-K for the year ended December 31, 2002.

3.2 By-laws of the Company. Incorporated by reference to Exhibit 3.2 to Registration Statement filed by the Company on Form S-11 under the Securities Act of 1933 (file No. 33-67870) ("S-11").

3.3 Agreement of Limited Partnership for the Operating Partnership. Incorporated by reference to Exhibit 3.3 to S-11.

3.4 Amendments No. 1 and No. 2 to Partnership Agreement dated March 31, 1997 and October 7, 1997. Incorporated by reference to Exhibit 3.4 to Form 10-K for the year ended December 31, 1997. ("1997 10-K")

3.5 Amendment No. 3 to Partnership Agreement dated September 3, 1999. Incorporated by reference to Exhibit 3.5 to 1999 10-K.

4.1 Form of Indenture among the Company, Chelsea GCA Realty Partnership, L.P., and State Street Bank and Trust Company, as Trustee. Incorporated by reference to Exhibit 4.4 to Registration Statement filed by the Company

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on Form S-3 under the Securities Act of 1933 (File No. 33-98136).

- 10.1 Registration Rights Agreement among the Company and recipients of Units. Incorporated by reference to Exhibit 4.1 to S-11.
- 10.2 Amended and Restated Credit Agreement dated July 31, 2002 among CPG Partners, L.P. and Fleet National Bank, individually and as an agent, and other Lending Institutions listed therein. Incorporated by reference to Exhibit 10.1 to Form 10-Q for the period ending September 30, 2002.
- 10.3 Joint Venture Agreement between Chelsea GCA Realty Partnership, L.P., Mitsubishi Estate Co., Ltd. and Nissho Iwai Corporation dated June 16, 1999. Incorporated by reference to Exhibit 10.9 to 1999 10-K.
- 10.4 Agreement for Purchase and Sale of Assets dated July 12, 2001. Incorporated by reference to Exhibit 2 to current report on Form 8-K reporting on an event , which occurred on September 25, 2001.
- 10.5 Purchase Agreement dated November 11, 2002. Incorporated by reference to Exhibit 2 to current report on Form 8-K reporting on an event which occurred December 19, 2002.
- 10.8 2002-2006 Long-Term Executive Incentive Plan. Incorporated by reference to Exhibit 10.8 to Form 10-K for the year ended December 31, 2002.
- 10.9 Agreement for Purchase and Sale dated May 8, 2003, as amended. Incorporated by reference to Exhibit 2 to current report on Form 8-K reporting on an event which occurred August 1, 2003 ("2003 8-K").
- 10.10 Term Loan Agreement dated July 31, 2003 between CPG Partners, L.P. and Wachovia Bank, National Association. Incorporated by reference to Exhibit 10 to 2003 8-K.
- 21 List of Subsidiaries
- 23.1 Consent of Ernst & Young LLP.
- 31.1 Section 302 Chief Executive Officer Certificate
- 31.2 Section 302 Chief Financial Officer Certificate
- 32.1 Section 906 Chief Executive Officer Certificate
- 32.2 Section 906 Chief Financial Officer Certificate
- (b) Reports on Form 8-K.
None
- (c) Exhibits See (a) 3
- (d) Financial Statement Schedules - The response to this portion of Item 15 is submitted as a separate schedule of this report.

Item 8, Item 15(a)(1) and (2) and Item 15(d)

(a)1. Financial Statements

Consolidated Financial Statements Chelsea Property Group, Inc.

| | |
|---|-----|
| Report of Independent Auditors | F-1 |
| Consolidated Balance Sheets as of December 31, 2003 and 2002 | F-2 |
| Consolidated Statements of Income for the years ended December 31, 2003, 2002 and 2001 | F-3 |
| Consolidated Statements of Stockholders' Equity for the years ended December 31, 2003, 2002 and 2001 | F-4 |
| Consolidated Statements of Cash Flows for the years ended December 31, 2003, 2002 and 2001 | F-5 |
| Notes to Consolidated Financial Statements | F-6 |

(a)2 and (d) Financial Statement Schedule

| | |
|--|------|
| Schedule III-Consolidated Real Estate and Accumulated Depreciation | F-38 |
|--|------|

All other schedules are omitted since the required information is not present or is not present in amounts sufficient to require submission of the schedule, or because the information required is included in the consolidated financial statements and notes thereto.

Report of Independent Auditors

Board of Directors
Chelsea Property Group, Inc.

We have audited the accompanying consolidated balance sheets of Chelsea Property Group, Inc. as of December 31, 2003 and 2002, and the related consolidated statements of income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2003. Our audits also included the financial statement schedule listed in the Index as Item 15 (a)(2). These financial statements and schedule are the responsibility of Chelsea Property Group, Inc.'s management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Chelsea Property Group, Inc. as of December 31, 2003 and 2002, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2003, in conformity with accounting principles generally accepted in the United States. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

New York, New York
February 24, 2004

Chelsea Property Group, Inc.
Consolidated Balance Sheets
(In thousands, except per share data)

| | December 31, | |
|---|---------------------|---------------------|
| | 2003 | 2002 |
| Assets: | | |
| Rental properties: | | |
| Land..... | \$ 299,176 | \$ 266,461 |
| Depreciable property..... | 1,773,607 | 1,570,713 |
| | ----- | ----- |
| Total rental property..... | 2,072,783 | 1,837,174 |
| Accumulated depreciation..... | (332,406) | (284,239) |
| | ----- | ----- |
| Rental properties, net..... | 1,740,377 | 1,552,935 |
| Cash and cash equivalents..... | 18,476 | 22,551 |
| Restricted cash-escrows..... | 6,456 | 3,455 |
| Tenant accounts receivable (net of allowance for doubtful accounts of \$1,615 in 2003 and \$2,593 in 2002)..... | 11,631 | 7,762 |
| Deferred rent receivable..... | 25,018 | 18,778 |
| Property held for sale..... | 3,500 | - |
| Investments in unconsolidated affiliates..... | 107,068 | 47,997 |
| Notes receivable-related parties..... | 2,151 | 2,746 |
| Deferred costs, net..... | 22,989 | 16,706 |
| Other assets..... | 32,748 | 30,100 |
| | ----- | ----- |
| Total assets | \$ 1,970,414 | \$ 1,703,030 |
| | ----- | ----- |
| Liabilities and stockholders' equity: | | |
| Liabilities: | | |
| Unsecured bank debt..... | \$ 204,035 | \$ 103,035 |
| Unsecured notes..... | 621,803 | 621,330 |
| Mortgage debt..... | 385,634 | 306,455 |
| Construction payables..... | 7,668 | 8,046 |
| Accounts payable and accrued expenses..... | 59,738 | 45,077 |
| Accrued dividend and distribution payable..... | 5,131 | 4,927 |
| Other liabilities..... | 20,871 | 18,886 |
| | ----- | ----- |
| Total liabilities | 1,304,880 | 1,107,756 |
| Commitments and contingencies | | |
| Minority interest | 144,688 | 139,443 |
| Stockholders' equity: | | |
| 8.375% series A cumulative redeemable preferred stock, \$0.01 par value, authorized 5,000 shares, issued and outstanding 797 in 2003 and in 2002 (aggregate liquidation preference of \$39,847 in 2003 and in 2002)..... | 8 | 8 |
| Common stock, \$0.01 par value, authorized 100,000 shares, issued and outstanding 43,592 in 2003 and 41,485 in 2002..... | 435 | 415 |
| Paid-in-capital..... | 630,255 | 574,352 |
| Officer loan..... | - | (488) |
| Distributions in excess of net income | (106,403) | (112,648) |
| Accumulated other comprehensive loss..... | (3,449) | (5,808) |
| | ----- | ----- |
| Total stockholders' equity | 520,846 | 455,831 |
| | ----- | ----- |

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| | | |
|---|-------------|-------------|
| Total liabilities and stockholders' equity..... | \$1,970,414 | \$1,703,030 |
| | ===== | ===== |

The accompanying notes are an integral part of the financial statements.

Chelsea Property Group, Inc.
Consolidated Statements of Income
(In thousands, except per share data)

| | Year ended December 31, | | |
|---|-------------------------|-----------------|-----------------|
| | 2003 | 2002 | 2001 |
| | ----- | ----- | ----- |
| Revenues: | | | |
| Base rent..... | \$247,894 | \$178,298 | \$124,645 |
| Percentage rent..... | 29,134 | 23,723 | 17,853 |
| Expense reimbursements..... | 86,499 | 64,875 | 49,496 |
| Other income..... | 8,738 | 11,593 | 10,888 |
| | ----- | ----- | ----- |
| Total revenues..... | 372,265 | 278,489 | 202,882 |
| Expenses: | | | |
| Operating and maintenance..... | 102,951 | 77,863 | 56,256 |
| Depreciation and amortization..... | 70,830 | 56,870 | 46,768 |
| General and administrative..... | 12,396 | 7,074 | 4,620 |
| Other..... | 4,984 | 3,962 | 2,535 |
| | ----- | ----- | ----- |
| Total expenses..... | 191,161 | 145,769 | 110,179 |
| Income before unconsolidated investments, interest expense, minority interest and discontinued operations..... | 181,104 | 132,720 | 92,703 |
| Income from unconsolidated investments..... | 11,006 | 9,802 | 15,025 |
| Loss from and impairment of Chelsea Interactive..... | (2,518) | (47,756) | (5,337) |
| Interest expense..... | (69,779) | (49,189) | (37,271) |
| Gain on sale, net of write-down of assets..... | - | 10,911 | 617 |
| | ----- | ----- | ----- |
| Income from continuing operations before minority interest..... | 119,813 | 56,488 | 65,737 |
| Minority interest attributed to continuing operations..... | (22,225) | (12,523) | (14,582) |
| | ----- | ----- | ----- |
| Income from continuing operations..... | 97,588 | 43,965 | 51,155 |
| (Loss) income from discontinued operations, net of minority interest..... | (844) | 1,171 | 659 |
| Gain on sale of discontinued operations, net of minority interest..... | 4,784 | -- | -- |
| | ----- | ----- | ----- |
| Net income..... | 101,528 | 45,136 | 51,814 |
| Preferred dividend..... | (3,336) | (3,422) | (4,188) |
| | ----- | ----- | ----- |
| Net income available to common shareholders..... | \$98,192 | \$41,714 | \$47,626 |
| | ----- | ----- | ----- |
| Basic (per common share): | | | |
| Income from continuing operations..... | \$2.21 | \$1.06 | \$1.39 |
| (Loss) income from discontinued operations..... | (0.02) | 0.03 | 0.02 |
| Gain on sale of discontinued operations..... | 0.11 | -- | -- |
| | ----- | ----- | ----- |
| Net income per common share..... | \$2.30 | \$1.09 | \$1.41 |
| | ===== | ===== | ===== |
| Weighted average common shares outstanding..... | 42,613 | 38,245 | 33,678 |
| | ===== | ===== | ===== |
| Diluted (per common share): | | | |
| Income from continuing operations..... | \$2.11 | \$1.02 | \$1.35 |

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| | | | |
|--|---------------|---------------|---------------|
| (Loss) income from discontinued operations..... | (0.02) | 0.03 | 0.02 |
| Gain on sale of discontinued operations..... | 0.11 | - | -- |
| | ----- | ----- | ----- |
| Net income per common share..... | \$2.20 | \$1.05 | \$1.37 |
| | ===== | ===== | ===== |
| Weighted average common shares outstanding..... | 44,597 | 39,798 | 34,710 |
| | ===== | ===== | ===== |

The accompanying notes are an integral part of the financial statements.

Chelsea Property Group, Inc.
Consolidated Statements of Stockholders' Equity
(In thousands, except per share data)

| | Preferred Stock At Par Value | Common Stock At Par Value | Paid-in- Capital | Officer Loan | Distrib. in Excess of Net Income | Accum. Other Comp Loss | To |
|---|--|---------------------------------------|---------------------|-----------------|--|---------------------------------|-------|
| | ----- | ----- | ----- | ----- | ----- | ----- | ----- |
| Balance December 31, 2000..... | \$10 | \$160 | \$348,141 | \$- | \$(76,829) | \$(123) | \$2 |
| Net income..... | - | - | - | - | 51,814 | - | 5 |
| Other comprehensive income | | | | | | | |
| Foreign currency translation..... | - | - | - | - | - | (198) | - |
| Interest rate swap..... | - | - | - | - | - | (2,658) | - |
| Total comprehensive income..... | - | - | - | - | - | - | 4 |
| Preferred dividend requirement..... | - | - | - | - | (4,188) | - | (|
| Cash distributions declared (\$1.56 per common share)..... | - | - | - | - | (52,939) | - | 5 |
| Exercise of stock options..... | - | 2 | 2,020 | - | - | - | - |
| Shares issued through offerings..... | - | 26 | 109,975 | - | - | - | 11 |
| Shares issued in exchange for units of the Operating Partnership..... | - | 2 | 2,289 | - | - | - | - |
| Shares issued through Employee Stock Purchase Plan (net of costs)..... | - | - | 128 | - | - | - | - |
| Revaluation of minority interest..... | - | - | (18,209) | - | - | - | (1 |
| | ----- | ----- | ----- | ----- | ----- | ----- | ----- |
| Balance December 31, 2001..... | 10 | 190 | 444,344 | - | (82,142) | (2,979) | 35 |
| Net income..... | - | - | - | - | 45,136 | - | 4 |
| Other comprehensive income | | | | | | | |
| Foreign currency translation..... | - | - | - | - | - | 274 | - |
| Interest rate swap..... | - | - | - | - | - | (3,103) | (|
| Total comprehensive income..... | - | - | - | - | - | - | 4 |
| Preferred dividend requirement..... | - | - | - | - | (3,422) | - | (|
| Cash distributions declared (\$1.86 per common share)..... | - | - | - | - | (72,220) | - | (7 |
| Two-for-one stock split..... | - | 189 | (189) | - | - | - | - |
| Redemption of Preferred stock (net of costs)..... | (2) | - | (9,652) | - | - | - | (|
| Exercise of stock options..... | - | 1 | 6,011 | - | - | - | - |
| Officer loan..... | - | - | - | (488) | - | - | - |
| Shares issued through offerings..... | - | 35 | 118,732 | - | - | - | 11 |
| Shares issued in exchange for units.... | - | - | 239 | - | - | - | - |
| Shares issued through Employee Stock Purchase Plan (net of costs)..... | - | - | 216 | - | - | - | - |
| Revaluation of minority interest..... | - | - | 14,651 | - | - | - | 1 |
| | ----- | ----- | ----- | ----- | ----- | ----- | ----- |

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| | | | | | | | |
|---|------------|--------------|------------------|-------------|--------------------|------------------|------------|
| Balance December 31, 2002 | 8 | 415 | 574,352 | (488) | (112,648) | (5,808) | 45 |
| Net income..... | - | - | - | - | 101,528 | - | 10 |
| Other comprehensive income | | | | | | | |
| Foreign currency translation..... | - | - | - | - | - | 430 | |
| Interest rate swap..... | - | - | - | - | - | 1,929 | |
| Total comprehensive income..... | - | - | - | - | - | - | 10 |
| Preferred dividend requirement..... | - | - | - | - | (3,336) | - | (3) |
| Cash distributions declared (\$2.14 per common share)..... | - | - | - | - | (91,947) | - | (91) |
| Exercise of stock options..... | - | 7 | 9,987 | - | - | - | |
| Repayment of Officer loan..... | - | - | - | 488 | - | - | |
| Shares issued through offerings..... | - | 12 | 49,251 | - | - | - | 4 |
| Shares issued in exchange for units of the Operating Partnership..... | - | 1 | 2,080 | - | - | - | |
| Shares issued through Employee Stock Purchase Plan (net of costs)..... | - | - | 321 | - | - | - | |
| Revaluation of minority interest..... | - | - | (5,736) | - | - | - | (|
| | ----- | ----- | ----- | ----- | ----- | ----- | ----- |
| Balance December 31, 2003 | \$8 | \$435 | \$630,255 | \$ - | \$(106,403) | \$(3,449) | \$5 |
| | ===== | ===== | ===== | ===== | ===== | ===== | ===== |

The accompanying notes are an integral part of the financial statements.

Chelsea Property Group, Inc.
Consolidated Statements of Cash Flows
(In thousands)

| | Year ended December 31, | | |
|--|-------------------------|----------------|--------------|
| | 2003 | 2002 | 2001 |
| | ----- | ----- | ----- |
| Cash flows from operating activities | | | |
| Net income..... | \$101,528 | \$ 45,136 | \$51,8 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Depreciation and amortization..... | 73,651 | 58,275 | 48,5 |
| Equity in earnings of unconsolidated investments in excess of distributions received..... | (5,491) | (2,407) | (2,2 |
| Impairment of and loss from Chelsea Interactive..... | - | 47,756 | 5,3 |
| Loss from interest rate swap..... | 514 | - | |
| Gain on sale of assets..... | - | (11,514) | (3 |
| Gain on sale of discontinued operations..... | (4,784) | - | |
| Minority interest in net income..... | 22,089 | 12,718 | 14,7 |
| Proceeds from non-compete receivable..... | - | 4,300 | 4,6 |
| Amortization of non-compete receivable..... | - | (5,136) | (5,1 |
| Additions to deferred lease costs..... | (2,642) | (1,153) | (1,8 |
| Other operating activities..... | (1,487) | (845) | (5 |
| Changes in assets and liabilities: | | | |
| Straight-line rent..... | (7,285) | (3,872) | (1,7 |
| Due from affiliates..... | (5,742) | (284) | (1,9 |
| Other assets..... | (467) | (3,211) | 9 |
| Deferred incentive compensation..... | - | (14,401) | |
| Accounts payable and other liabilities..... | 11,750 | 2,860 | 9,5 |
| | ----- | ----- | ----- |
| Net cash provided by operating activities | 181,634 | 128,222 | 121,7 |
| Cash flows from investing activities | | | |
| Additions to rental properties..... | (171,685) | (385,519) | (103,5 |
| Net proceeds from sale of centers..... | 13,853 | 7,929 | 7,1 |
| Additions to investments in unconsolidated affiliates..... | (46,688) | (37,855) | (14,7 |
| Proceeds from sale of investments in unconsolidated affiliates..... | - | 11,293 | 2,8 |

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| | | | |
|---|------------------|------------------|---------------|
| Additions to deferred lease costs from acquisitions..... | (8,536) | - | |
| Additions to deferred development costs..... | (1,630) | (898) | (8,2 |
| Payments from related parties..... | 1,083 | 1,085 | 1,6 |
| Loans to related parties..... | - | (550) | (2,7 |
| Distributions from investments in unconsolidated affiliates in excess of earnings..... | - | 337 | 5,0 |
| | ----- | ----- | ----- |
| Net cash used in investing activities..... | (213,603) | (404,178) | (112,5 |
| Cash flows from financing activities | | | |
| Debt proceeds..... | 124,000 | 503,958 | 177,5 |
| Debt repayments..... | (38,078) | (249,540) | (217,3 |
| Net proceeds from sale of common stock | 59,577 | 124,990 | 112,1 |
| Distributions..... | (116,828) | (92,717) | (72,8 |
| Preferred stock redemption | - | (9,654) | |
| Additions to deferred financing costs..... | (777) | (3,134) | (2,1 |
| | ---- | ----- | ----- |
| Net cash provided by (used in) financing activities..... | 27,894 | 273,903 | (2,6 |
| Net (decrease) increase in cash and cash equivalents..... | (4,075) | (2,053) | 6,5 |
| Cash and cash equivalents, beginning of period..... | 22,551 | 24,604 | 18,0 |
| | ----- | ----- | ----- |
| Cash and cash equivalents, end of period..... | \$18,476 | \$22,551 | \$24,6 |
| | ===== | ===== | ===== |

The accompanying notes are an integral part of the financial statements.

Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements

1. Organization and Basis of Presentation

Organization

Chelsea Property Group, Inc. (the "Company") is a self-administered and self-managed real estate investment trust ("REIT"). The Company is the managing general partner of CPG Partners, L.P. (the "Operating Partnership" or "OP"), an operating partnership that specializes in owning, developing, leasing, marketing and managing upscale and fashion-oriented manufacturers' outlet centers. As of December 31, 2003, the Company wholly or partially owned 60 centers in 31 states and Japan containing approximately 16.1 million square feet of gross leasable area ("GLA"). As of December 31, 2003, the Company's portfolio was comprised of 30 Premium Outlet centers containing 10.6 million square feet of GLA (the "Premium Properties") and 30 other centers containing approximately 5.5 million square feet of GLA ("Other Properties") (collectively the "Properties"). The Company's Premium Properties generated approximately 75% and 86% of the Company's real estate net operating income for the years ended December 31, 2003, and 2002, respectively. The Premium Properties generally are located near metropolitan areas including New York City, Los Angeles, Chicago, Boston, Washington, D.C., San Francisco, Sacramento, Atlanta, Dallas, and Tokyo and Osaka, Japan. Some Premium Properties are also located within 20 miles of major tourist destinations including Palm Springs, Napa Valley, Orlando, Las Vegas and Honolulu.

Basis of Presentation

Virtually, all of the Company's assets are held by, and all of its operations conducted through, the Operating Partnership. Due to the Company's ability, as the sole general partner, to exercise financial and operational control over the Operating Partnership, the Operating Partnership is consolidated in the accompanying financial statements. All significant intercompany transactions and accounts have been eliminated in consolidation.

On May 1, 2002, the Company declared a 2-for-1 stock split of the Company's common shares. The stock dividend was paid May 28, 2002, to shareholders of record on May 14, 2002. The Operating Partnership simultaneously declared a 2-for-1 split of its limited units. All applicable share and per share information in the accompanying financial statements have been adjusted to reflect the stock split.

2. Summary of Significant Accounting Principles

Rental Properties

Rental properties are presented at cost net of accumulated depreciation. Depreciation is computed on the straight-line basis over the estimated useful lives of the assets. The Company uses 25-40 year estimated lives for buildings, and 15 and 5-7 year estimated lives for improvements and equipment, respectively. Expenditures for ordinary maintenance and repairs are charged to operations as incurred, while significant renovations and enhancements that improve and or extend the useful life of an asset are capitalized and depreciated over the estimated useful life. The Company reviews real estate assets for impairment wherever events or changes in circumstances indicate that the carrying value of assets to be held and used may not be recoverable. Impaired assets are reported at the lower of cost or fair value. Assets to be disposed of are reported at the lower of cost or fair value less cost to sell. No impairment write-downs of rental properties were required for the three years ended December 31, 2003. At December 31, 2003, the Lakeland Factory Outlet Mall was held for sale. The Lakeland property was purchased in August 2003 in conjunction with the Las Vegas Outlet Center. The Company anticipates selling the Lakeland property during 2004. At December 31, 2002, no assets were held for sale.

Gains and losses from sales of real estate are recorded when title is conveyed to the buyer, subject to the buyer's financial commitment being sufficient to provide economic substance to the sale.

Chelsea Property Group, Inc. Notes to Consolidated Financial Statements

2. Summary of Significant Accounting Principles (continued)

Rental Properties (continued)

In accordance with Statement of Financial Accounting Standards No.141, or SFAS 141, "Business Combinations," the Company allocates the purchase price of real estate to land, building, tenant improvements and if determined to be material, intangibles, such as the value of above, below and at market leases and origination cost associated with in-place leases. The Company depreciates the amount allocated to building and other intangible assets over their estimated useful lives, which generally range from five to forty years. The values of the above and below market leases are amortized and recorded as either an increase (in the case of below market leases) or a decrease (in the case of above market leases) to rental income over the remaining term of the associated lease. The value associated with in-place leases are amortized over the term of the lease. If a tenant vacates its space prior to the contractual termination of the lease and no rental payments are being made on the lease, any unamortized balance of the related intangible will be written off. The tenant improvements and origination costs are amortized as an expense over the remaining life of the lease (or charged against earnings if the lease is terminated prior to contractual expiration date). The Company assesses fair value based on estimated cash flow projections that utilize appropriate discount and capitalization rate and available market information. Estimates of future cash flows are based on a number of factors including the historical operating results, known trends and market/ economic conditions that may affect the property.

Cash and Equivalents

All demand and money market accounts and certificates of deposit with original terms of three months or less from the date of purchase are considered cash equivalents. The Company places its cash investments in excess of insured

amounts with high quality financial institutions. At December 31, 2003 and 2002, cash equivalents consisted of repurchase agreements, commercial paper, U.S. Government agency securities, domestic bank obligations and other corporate and municipal obligations that mature between January and March of the following year. The carrying amount of such investments approximated fair value.

Investment in Unconsolidated Joint Ventures

The Company accounts for its investments in unconsolidated joint ventures under the equity method of accounting as the Company exercises significant influence, but does not control these entities. In all the joint ventures, the rights of the minority investor are both protective as well as participating. These rights preclude the Company from consolidating these investments. These investments are recorded initially at cost, as investments in unconsolidated joint ventures, and subsequently adjusted for equity in earnings (loss) and cash contributions and distributions. Any difference between the carrying amount of these investments on the balance sheet of the Company and the underlying equity in net assets is amortized as an adjustment to equity in earnings (loss) of unconsolidated joint ventures over the associated rental property's useful life.

Development Costs

Development costs, including interest, taxes, insurance and other costs incurred in developing new properties, are capitalized. Upon completion of construction, development costs are amortized on a straight-line basis over the useful lives of the respective assets. Development costs related to inactive projects are expensed at such time as the project is deemed abandoned.

Capitalized Interest

Interest, including the amortization of deferred financing costs for borrowings used to fund development and construction, is capitalized as construction in progress and allocated to individual property costs.

Chelsea Property Group, Inc. Notes to Consolidated Financial Statements

2. Summary of Significant Accounting Principles (continued)

Foreign Currency Translation

The Company conforms to the requirements of the Statement of Financial Accounting Standards No. 52 entitled "Foreign Currency Translation." Accordingly, assets and liabilities of foreign equity investees are translated at prevailing year-end rates of exchange. Translation gain or loss is recognized as a component of other comprehensive income.

Rental Expense

Rental expense is recognized on a straight-line basis over the initial term of the lease.

Deferred Lease Costs

Deferred lease costs consist of fees and direct internal costs incurred to initiate and renew operating leases, and are amortized on a straight-line basis over the initial lease term or renewal period as appropriate.

Deferred Financing Costs

Deferred financing costs represent commitment fees, legal and other third party costs associated with obtaining commitments for financing which result in a closing of such financing. Deferred financing costs are amortized as interest costs over the terms of the respective agreements. Unamortized deferred financing costs are expensed when the associated debt is retired before maturity. Costs incurred in seeking financial transactions which do not close are expensed in the period it is determined the financing will not be closing.

Revenue Recognition

Leases with tenants are accounted for as operating leases. Base rent revenue is recognized on a straight-line basis over the lease term according to the provisions of the lease. The excess of rents recognized over amounts contractually due and unpaid rents are included in deferred rent receivable in the accompanying financial statements. Certain lease agreements contain provisions for rents that are calculated on a percentage of sales and recorded on the accrual basis. These rents are accrued monthly once the required thresholds per the lease agreement are exceeded. Virtually all lease agreements contain provisions for additional rents representing reimbursement of real estate taxes, insurance, advertising and common area maintenance costs.

Bad Debt Expense

Bad debt expense included in other expense totaled \$2.2 million, \$2.0 million and \$1.2 million for the years ended December 31, 2003, 2002 and 2001, respectively. The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of its tenants to make required rent payments.

Chelsea Property Group, Inc. Notes to Consolidated Financial Statements

2. Summary of Significant Accounting Principles (continued)

Income Taxes

The Company is taxed as a REIT under Section 856(c) of the Internal Revenue Code of 1986, as amended, commencing with the tax year ended December 31, 1993. As a REIT, the Company generally is not subject to federal income tax. To maintain qualification as a REIT, the Company must distribute at least 90% of its REIT taxable income to its stockholders and meet certain other requirements. If the Company fails to qualify as a REIT in any taxable year, the Company will be subject to federal income tax on its taxable income at regular corporate rates. The Company may also be subject to certain state and local taxes on its income and property. Under certain circumstances, federal income and excise taxes may be due on its undistributed taxable income. At December 31, 2003 and 2002, the Company was in compliance with all REIT requirements.

The following summarizes the tax components of the Company's common dividends declared for the years ended December 31, 2003, 2002 and 2001:

| | 2003 | 2002 | 2001 |
|--------------------------------------|---------------|--------|--------|
| | ----- | ----- | ----- |
| Dividends per share..... | \$2.14 | \$1.86 | \$1.56 |
| Capital gain (a)..... | (0.13) | (0.21) | - |
| Unrecaptured Section 1250 gain | - | (0.01) | - |
| | ----- | ----- | ----- |
| Ordinary income..... | \$2.01 | \$1.64 | \$1.56 |
| | ===== | ===== | ===== |

(a) Capital rates were 15% and 20% in 2003 and 2002, respectively.

Pursuant to amendments to the Code that became effective January 2001, the Company has elected or may elect to treat certain of its existing or newly created corporate subsidiaries as taxable REIT subsidiaries (each "TRS"). In general, a TRS of the Company may perform non-customary services for tenants of the Company, hold assets that the Company can not hold directly and generally may engage in any real estate or non-real estate related business. A TRS is subject to corporate federal income tax.

Net Income Per Common Share

Basic earnings per common share is computed using the weighted average number of shares outstanding. Diluted earnings per common share is computed using the weighted average number of shares outstanding adjusted for the incremental shares attributed to outstanding options to purchase common stock of 2.0 million in 2003, 1.5 million in 2002 and 1.0 million in 2001.

Chelsea Property Group, Inc. Notes to Consolidated Financial Statements

2. Summary of Significant Accounting Principles (continued)

Net Income Per Common Share (continued)

The following table sets forth the computation of basic and diluted earnings per share for the periods indicated and assumes that the Company's 2-for-1 stock split in May 2002 had occurred on January 1, 2001 (in thousands, except per share amounts):

| | 2003 | 2002 | 2001 |
|--|-----------------|----------|----------|
| Numerator | | | |
| Numerator for basic and diluted earnings per share- | | | |
| Net income available to common shareholders | \$98,192 | \$41,714 | \$47,626 |
| Denominator | | | |
| Denominator for basic earnings per share- | | | |
| Weighted average shares | 42,613 | 38,245 | 16,839 |
| Increase in shares due to effect of 2-for-1 stock split | - | - | 16,839 |
| Denominator for basic earnings per share | 42,613 | 38,245 | 33,678 |
| Effect of dilutive securities- | | | |
| Stock options | 1,984 | 1,553 | 516 |
| Increase in shares due to effect of 2-for-1 stock split | - | - | 516 |
| Effect of dilutive securities | 1,984 | 1,553 | 1,032 |
| Denominator for diluted earnings per share- | | | |
| Adjusted weighted average shares assumed conversions ... | 44,597 | 39,798 | 17,355 |
| Increase in shares due to effect of 2-for-1 stock split | - | - | 17,355 |
| Denominator for diluted earnings per share | 44,597 | 39,798 | 34,710 |
| Per share amounts: | | | |
| Net income - basic | \$ 2.30 | \$ 1.09 | \$ 1.41 |
| Net income - diluted | \$ 2.20 | \$ 1.05 | \$ 1.37 |

Concentration of Company's Revenue and Credit Risk

For the years ended December 31, 2003, 2002 and 2001, respectively, 13%, 16% and 21% of the Company's revenues were derived from Woodbury Common Premium Outlets. The loss of this center or a material decrease in revenues

from the center for any reason may have a material adverse effect on the Company. In addition, for the years ended December 31, 2003, 2002 and 2001, respectively, 23%, 25% and 28% of the Company's revenues were derived from the Company's centers in California.

Management of the Company performs ongoing credit evaluations of its tenants and requires certain tenants to provide security deposits. Although the Company's tenants operate principally in the retail industry, there is no dependence upon any single tenant.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Chelsea Property Group, Inc. Notes to Consolidated Financial Statements

2. Summary of Significant Accounting Principles (continued)

Minority Interest

Minority interest is comprised of the following:

The common unitholders' interest in the OP that was issued in exchange for the assets contributed to the OP on November 2, 1993, and additional units exchanged for property acquisitions during 1997 and 2002. The unitholders' interest at December 31, 2003, and 2002 was 14.4% and 15.4% respectively (7,356,000 units and 7,563,000 units). Common shares are reserved for the potential conversion of the units. Units may be exchanged for shares of the Company's common stock on a one-for-one basis. Upon exchange, shares are valued at the book value of the units on the date of the exchange. During the years ended December 31, 2003, 2002 and 2001, the Company made the following distributions per unit (assumes that the 2-for-1 stock/unit split in May 2002 had occurred on January 1, 2001):

| | 2003 | 2002 | 2001 |
|-------------------------------------|---------|---------|---------|
| | ----- | ----- | ----- |
| Distributions per unit..... | \$ 2.14 | \$ 1.86 | \$ 1.56 |
| Capital gain (a)..... | (0.13) | (0.21) | - |
| Unrecaptured Section 1250 gain..... | - | (0.01) | - |
| | ----- | ----- | ----- |
| Ordinary income..... | \$ 2.01 | \$1.64 | \$1.56 |
| | ===== | ===== | ===== |

(a) In 2003 and 2002, capital rates were 15% and 20%, respectively.

The preferred unit holder's interest in the OP which was issued in a private sale of \$65.0 million of Series B Cumulative Redeemable Preferred Units to an institutional investor in September 1999.

Accumulated Other Comprehensive Loss

At December 31, 2003 and 2002, other comprehensive loss was comprised of the following (in thousands):

| | |
|------|------|
| 2003 | 2002 |
|------|------|

| | | |
|------------------------------|---------|---------|
| Interest rate swap | \$3,832 | \$5,761 |
| Foreign currency translation | (383) | 47 |
| Total | \$3,449 | \$5,808 |

Derivative and Financial Instruments

In the normal course of business, the Company uses a variety of derivative and financial instruments to manage, or hedge, interest rate and foreign currency risk. The Company requires that hedging derivative instruments are effective in reducing the interest rate or foreign currency risk exposure as they are designated. This effectiveness is an essential for hedge accounting under accounting principles generally accepted in the United States. Derivative instruments may be associated with the hedge of an anticipated transaction. In those cases, hedge effectiveness criteria also require that it be probable that the underlying transaction occurs. Instruments that meet these hedging criteria are formally designated as hedges at the inception of the derivative contract and recorded on the balance sheet at their fair values with the changes in fair value reflected in accumulated other comprehensive income (loss). When the terms of an underlying transaction are modified, or when the underlying hedged item ceases to exist, all changes in the fair value of the instrument are marked-to-market with changes in value included in net income each period until the instrument matures or is terminated or assigned. Any derivative instrument used for risk management that does not meet the hedging criteria is marked-to-market each period in net income.

Chelsea Property Group, Inc. Notes to Consolidated Financial Statements

2. Summary of Significant Accounting Principles (continued)

Derivative and Financial Instruments (continued)

To determine the fair values of derivative and financial instruments, the Company uses a variety of methods and assumptions that are based on market conditions and risks existing at each balance sheet date. For the majority of financial instruments including most derivatives, long-term investments and long-term debt, standard market conventions and techniques such as discounted cash flow analysis, option pricing models, replacement cost, and termination cost are used to determine fair value. All methods of assessing fair value result in a general approximation of value, and such value may never actually be realized.

Stock Option Plans

The Company elected Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB No. 25") and related Interpretations in accounting for its employee stock options. Under APB No. 25's intrinsic value method, compensation expense, if any, is measured based on the award's intrinsic value, the excess of the market price of the underlying stock over the exercise price on the measurement date (which usually is the date of grant). Appropriately, through December 31, 2003, the intrinsic value of all employee stock options issued on the date of the grant was zero, resulting in no compensation expense.

Pro forma information regarding net income and earnings per share is required by SFAS No. 123, and has been determined as if the Company had accounted for its employee stock options under the fair value method. The fair value for these options was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted average assumptions for each year:

| | | |
|-------|-------|-------|
| 2003 | 2002 | 2001 |
| ----- | ----- | ----- |

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| | | | |
|--------------------------------------|----------------|---------|---------|
| Price of stock on date of grant..... | \$36.20 | \$26.30 | \$20.62 |
| Exercise price of option..... | \$36.20 | \$26.30 | \$20.62 |
| Risk-free interest rate..... | 4.0% | 5.0% | 5.0% |
| Expected volatility factor | 0.166 | 0.236 | 0.236 |
| Expected dividend yield..... | 6.0% | 6.0% | 6.0% |
| Expected option life..... | 4 years | 4 years | 4 years |

The results in a fair value estimate will be higher when one or more of the following variables increase; the price of the stock, the expected volatility, the expected life of the option and/or the risk-free interest rate. Conversely, an increase in the exercise price of the option and/or the expected dividend yield of stock lowers the fair value of the underlying stock.

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options, and changes in the subjective input assumptions can materially affect the fair value estimate, management believes the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

The Company granted the following options for the years ended December 31:

| | | | |
|-------------------------------|----------------|-----------|---------|
| | 2003 | 2002 | 2001 |
| | ---- | ---- | ---- |
| Plan year..... | 2000 | 2000 | 2000 |
| Options granted..... | 45,000 | 1,510,000 | 140,000 |
| Expiration date..... | 2013 | 2012 | 2011 |
| Exercise price per share..... | \$36.20 | \$26.30 | \$20.62 |

Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements

2. Summary of Significant Accounting Principles (continued)

Stock Option Plans (continued)

For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the options' vesting period. The Company's pro forma information for the years ended December 31 is as follows (in thousands except for earnings per share data):

| | | | |
|--|------------------|-----------|-----------|
| | 2003 | 2002 | 2001 |
| | ----- | ----- | ----- |
| Net income to common shareholders; as reported..... | \$ 98,192 | \$ 41,714 | \$ 47,626 |
| Add: Stock based employee expense included in reported net income..... | - | - | - |
| Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of minority interest..... | (1,471) | (2,080) | (969) |
| | ----- | ----- | ----- |
| Pro forma net income..... | \$ 96,721 | \$ 39,634 | \$ 46,657 |
| | ===== | ===== | ===== |

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| | | | |
|----------------------------|---------------|--------|--------|
| Earnings per share: | | | |
| Basic - as reported..... | \$2.30 | \$1.09 | \$1.41 |
| Basic - pro forma..... | \$2.27 | \$1.04 | \$1.39 |
| Diluted - as reported..... | \$2.20 | \$1.05 | \$1.37 |
| Diluted - pro forma..... | \$2.17 | \$1.00 | \$1.34 |

A summary of the Company's stock option activity, and related information for the years ended December 31 follows:

| | 2003 | | 2002 | | 2001 | |
|--|--------------------|----------------------|--------------------|----------------------|--------------------|------------|
| | Options (000's) | Wtd-avg Ex. price | Options (000's) | Wtd-avg Ex. price | Options (000's) | Wtd Ex. |
| Outstanding beginning of year..... | 3,967.9 | \$19.12 | 2,988.0 | \$14.68 | 2,972.2 | \$14 |
| Granted..... | 45.0 | 36.20 | 1,510.0 | 26.30 | 140.0 | 20 |
| Exercised..... | (720.7) | 14.47 | (410.1) | 14.65 | (124.2) | 15 |
| Forfeited..... | - | - | (120.0) | 13.91 | - | - |
| Outstanding end of year..... | 3,292.2 | \$20.18 | 3,967.9 | 19.12 | 2,988.0 | \$14 |
| Exercisable at end of year..... | 1,973.1 | \$16.32 | 1,895.8 | \$14.68 | 1,910.0 | \$14 |
| Weighted average fair value of each option granted during the year..... | \$2.70 | | \$3.44 | | \$2.54 | |

Exercise prices for options outstanding as of December 31, 2003 ranged from \$11.69 to \$36.20 per share. The weighted average remaining contractual life of the options was 6.3 years. The Company has reserved approximately 3.8 million shares for its stock option plans.

Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements

2. Summary of Significant Accounting Principles (continued)

Recently Issued Accounting Pronouncements

In October 2001, the FASB issued Statement of Financial Accounting Standard No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144") which was effective and adopted by the Company on January 1, 2002. SFAS 144 provides accounting guidance for financial accounting and reporting for impairment or disposal of long-lived assets. SFAS 144 supersedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of." SFAS 144 retains fundamental provisions of SFAS 121 related to the recognition and measurement of the impairment of long-lived assets to be held and used. In addition, SFAS 144 superseded APB Opinion 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." SFAS 144 extended the reporting of a discontinued operation to a "component of an entity." Thus, the operations of assets sold or held for sale are presented as discontinued operations in the Company's statement of income.

In June 2002, FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146") which was effective for exit or disposal activities initiated after December 31, 2002. SFAS 146 requires that a liability for a cost associated with an exit or disposal activity be recognized and measured initially at fair value only when the liability is incurred. See note 6 to financial statements for discussion related to the estimated future costs to be incurred in connection with the future operations of Chelsea Interactive.

In November 2002, the FASB issued No. 45, Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others ("FIN 45"). FIN 45 requires certain guarantees to be recorded at fair value, instead of recording a liability only when a loss is probable and reasonably estimable, as those terms are defined in FASB Statement No. 5, Accounting for Contingencies. FIN 45 also requires a guarantor to make significant new disclosures, even when the likelihood of making any payments under the guarantee is remote. The disclosure requirements of FIN 45 are effective for financial statements of interim or annual periods ending after December 15, 2002. The Company adopted the disclosure provisions of FIN 45 effective December 31, 2002. FIN 45's initial recognition and initial measurement provisions are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. The adoption of FIN 45 did not have a material impact on the Company's financial position or the results of operations.

In January 2003, the FASB issued Interpretation No. 46, Consolidation of Variable Interest Entities ("FIN 46"). FIN 46 clarifies the application of existing accounting pronouncements to certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. The provisions of FIN 46 will be immediately effective for all variable interests in variable interest entities created after January 31, 2003. The Company has not created any variable interest entities subsequent to January 31, 2003. In December 2003, FASB issued a revision to Interpretation 46 ("FIN 46-R") to clarify the provisions of FIN 46. The application of FIN 46-R is effective for public companies, other than small business issuers, after March 15, 2004. The Company does not believe that FIN 46-R will have a significant impact on the Company's financial statements.

Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements

2. Summary of Significant Accounting Principles (continued)

Recently Issued Accounting Pronouncements

On April 30, 2003, FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities" ("SFAS 149"). SFAS 149 amends and clarifies the accounting guidance on (1) derivative instruments (including certain derivative instruments embedded in other contracts) and (2) hedging activities that fall within the scope of SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"). SFAS 149 also amends certain other existing pronouncements, which will result in more consistent reporting of contracts that are derivatives in the entirety or that contain embedded derivatives that warrant separate accounting. SFAS 149 is effective (1) for contracts entered into or modified after June 30, 2003, with certain exceptions, and (2) for hedging relationships designed after June 30, 2003. The guidance is to be applied prospectively. The adoption of SFAS 149 did not have a material impact on the Company's financial condition, or results of operations or cash flows.

In May 2003, FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity" ("SFAS 150"). This statement establishes standards for the classification and measurement of certain financial instruments with characteristics of both liabilities and equity. SFAS 150 is effective for financial instruments entered into or modified after May 31, 2003 and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003. It is to be implemented by reporting the cumulative effect of a change in accounting principle for financial instruments created before the issuance date of the statement and still existing at the beginning of the interim period of adoption. The implementation of SFAS 150 did not have a material impact on the Company's financial condition, results of operations or cash flows.

Reclassifications

Certain amounts in the 2002 and 2001 financial statements have been reclassified to conform to the 2003 presentation.

3. Acquisitions and Dispositions

Acquisitions

In June 2003, the Company purchased The Crossings Factory Stores ("The Crossings"), a 390,000 square-foot outlet center located in Tannersville, Pennsylvania, for \$111.3 million, including closing costs, and assumed a \$60.7 million 5.85% mortgage loan due 2013. The stated interest rate was greater than that available to the Company for comparable debt. Consequently, the Company recognized a \$3.4 million debt premium that will be amortized over the period of the loan, which reduces the effective rate to 5.1%. An additional \$5.0 million will be due to the sellers upon the completion of a 21,000 square-foot expansion scheduled to open in late 2004, subject to permits. In accordance with the provisions of SFAS 141, the Company allocated the purchase price between land, building and in-place leases. Tenant origination costs of \$4.0 million are included in deferred costs on the balance sheet and a net intangible lease liability of \$3.1 million is included in other liabilities. The tenant origination costs and intangible lease liability are being amortized over the respective lease terms. For the period ended December 31, 2003, the Company recognized rental income of \$0.5 million related to the amortization of in-place leases.

In August 2003, the Company acquired Las Vegas Outlet Center ("Las Vegas"), a 477,000 square-foot outlet center in Las Vegas, Nevada, for \$104.0 million including the assumption of a \$24.4 million 8.12% mortgage loan due 2012. The stated interest rate was greater than that available to the Company for comparable debt. Consequently, the Company recognized a \$1.9 million debt premium that will be amortized over the period of the loan, which reduces the effective rate to 6.29%. As part of the transaction, the Company also acquired Lakeland Factory Outlet Mall ("Lakeland"), a 319,000 square-foot outlet center near Memphis, Tennessee, for an additional \$3.5 million. The Lakeland property is being marketed for sale. In accordance with the provisions of SFAS 141, the Company allocated the purchase price between land, building and in-place leases. Tenant origination costs of \$4.5 million are included in deferred costs on the balance sheet and a net intangible lease liability of \$0.4 million is included in other liabilities. The tenant origination costs and intangible lease liability are being amortized over the respective lease terms. For the period ending December 31, 2003, the Company recognized a charge against rental income of \$0.3 million related to the amortization of in-place leases.

Chelsea Property Group, Inc. Notes to Consolidated Financial Statements

3. Acquisitions and Dispositions

Acquisitions

On April 1, 2002, the Company became the sole owner of the Orlando Premium Outlets ("Simon-Orlando") by acquiring Simon Property Group, Inc.'s ("Simon") 50% undivided ownership interest for \$46.6 million in cash and the assumption of \$29.7 million of existing mortgage debt and the guarantee related thereto. On June 16, 2002, the Company repaid the outstanding balance of \$59.4 million and extinguished the mortgage. After closing the transaction the operating results and balance sheet of Simon-Orlando were consolidated in the accompanying financial statements.

On April 1, 2002, the Company purchased a 305,000 square foot outlet center located in Edinburgh, Indiana for \$27.0 million in cash.

On August 20, 2002, the Company became the sole owner of four Premium Outlet centers by acquiring Fortress Registered Investment Trust's ("Fortress") 51% undivided ownership interest in the F/C Acquisition Holdings, LLC joint venture ("F/C Acquisition"). The Company paid \$58.9 million in cash and assumed \$86.5 million of existing mortgage debt on the properties. After closing the transaction the operating results and balance sheet of the four Premium Outlet centers including \$169.6 million of existing nonrecourse mortgage debt, were consolidated in the accompanying financial statements.

On November 22, 2002, the Company purchased two outlet centers from JMJ Properties, Inc. ("JMJ"); a 305,000 square-foot center located in Albertville, Minnesota and a 278,000 square foot center located in Johnson Creek, Wisconsin for a total purchase price of \$89.5 million. The Company paid \$44.9 million in cash and the OP issued 1.3 million limited partnership units in the OP with an assigned value of \$44.6 million.

On December 19, 2002 the Company acquired four outlet centers for an all cash price of \$193.0 million from New Plan Excel Realty Trust, Inc. ("NPXL"). The four properties consist of a 292,000 square foot outlet center located in Jackson, New Jersey; a 391,000 square foot outlet center located in Osage Beach, Missouri; a 329,000 square foot outlet center located in St. Augustine, Florida; and a 300,000 square foot outlet center located in Branson, Missouri.

Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements

3. Acquisitions and Dispositions

Acquisitions

The aggregate condensed balance sheet (unaudited) on the date of acquisition of the acquired properties is as follows (in thousands):

| | 2003 ----- | 2002 ----- |
|--------------------------|------------------|---------------|
| Land | \$ 33,660 | \$100,540 |
| Depreciable property | 190,716 | 591,018 |
| Accumulated depreciation | - | (15,977) |
| Other assets | 945 | 19,487 |
| | ----- | ----- |
| Total assets | \$225,321 | \$695,068 |
| | ===== | ===== |
| Mortgage debt | \$ 90,491 | \$228,025 |
| Other liabilities | 383 | 9,884 |
| | ----- | ----- |
| Total liabilities | 90,874 | 237,909 |
| | ----- | ----- |
| Net equity | \$134,447 | \$457,159 |
| | ===== | ===== |

The following condensed pro forma (unaudited) information assumes that the acquisitions of The Crossings Factory Stores, Las Vegas Outlet Center and Lakeland Factory Outlet Mall had occurred on January 1, 2002. Additionally, it assumes that the effect of the sale of 1.2 million shares of the Company's common stock in conjunction with The Crossings acquisition and the \$100.0 million term loan in conjunction with the Las Vegas acquisition occurred on January 1, 2002 (in thousands):

| | Year Ended December 31, 2003 ---- | 2002 ---- |
|-----------------------------------|---|--------------|
| Total revenue | \$386,407 | \$307,284 |
| Net income to common shareholders | 101,476 | 47,105 |
| Earnings per share: | | |
| Basic: | | |
| Net income to common shareholders | \$2.32 | \$1.19 |

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| | | |
|--|--------|--------|
| Weighted average common shares outstanding | 43,727 | 39,445 |
| Diluted: | | |
| Net income to common shareholders | \$2.22 | \$1.15 |
| Weighted average common shares outstanding | 45,711 | 40,998 |

Chelsea Property Group, Inc. Notes to Consolidated Financial Statements

Acquisitions and Dispositions (continued)

Dispositions

In June 2003, the Company sold a 23,000 square-foot Premium Outlet center located in St. Helena, California for \$7.4 million, resulting in a gain of approximately \$4.7 million. The center partially secured a mortgage note due April 2010 and \$5.0 million of the sales proceeds were used to pay down the mortgage loan. Revenues and expenses, net of minority interest related to the St. Helena property, have been reclassified to discontinued operations in the period of sale and comparable periods in the accompanying financial statements.

In September 2003, the Company realized a gain of approximately \$0.9 million from the sale of one of its non-core properties, the former Factory Stores of America at Mesa, Arizona ("Mesa property"). Revenues and expenses, net of minority interest connected with the Mesa property have been reclassified to discontinued operations in the period of sale and comparable periods in the accompanying financial statements.

The Company terminated its long-term lease on American Tin Cannery Premium Outlets. Revenues and expenses, net of minority interest, connected with the ATC property have been reclassified to discontinued operations in the period of termination and comparable periods in the accompanying financial statements.

During June and July 2002, the Company sold four Other Properties centers and two outparcels generating net proceeds of approximately \$6.8 million, which approximated the net book value of these properties. Accordingly, no gain or loss on the sales was recognized. The aggregate revenues and net income of the sold properties were \$1.2 million and \$0.3 million for the year ended December 31, 2002, respectively, and \$0.6 million and \$0.2 million for the year ended December 31, 2001, respectively.

In November 2002, the Company sold an additional Other Properties center and an outparcel that generated net proceeds of approximately \$1.1 million, which resulted in a gain of approximately \$0.6 million which is included in other income in the accompanying financial statements. The aggregate revenues and net income of the sold property were \$0.6 million and \$0.4 million for the year ended December 31, 2002, respectively and \$0.1 million and \$40,000 for the year ended December 31, 2001, respectively.

In October 2001, the Company sold a Premium Properties center and recognized a loss of approximately \$0.3 million that is included as a charge in other income in the accompanying financial statements. The aggregate revenues and net income of the sold property were immaterial to the operations of the Company for the years ended December 31, 2001 and 2000.

4. Rental Properties

The following summarizes the carrying values of rental properties as of December 31 (in thousands):

| | 2003 | 2002 |
|--|------|------|
| | | |

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| | | |
|---|-------------|-------------|
| Land and improvements..... | \$ 495,819 | \$ 460,227 |
| Buildings and improvements..... | 1,536,998 | 1,351,183 |
| Construction-in-progress..... | 16,838 | 6,708 |
| Equipment and furniture..... | 23,128 | 19,056 |
| | ----- | ----- |
| Total rental property..... | 2,072,783 | 1,837,174 |
| Accumulated depreciation and amortization.. | (332,406) | (284,239) |
| | ----- | ----- |
| Total rental property, net..... | \$1,740,377 | \$1,552,935 |
| | ===== | ===== |

Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements

4. Rental Properties (continued)

Interest costs capitalized as part of buildings and improvements were \$4.3 million, \$2.9 million and \$2.0 million for the years ended December 31, 2003, 2002 and 2001, respectively.

Commitments for land, new construction, development, and acquisitions including the Company's 50% share of joint venture activity, totaled approximately \$49.7 million and \$19.1 million at December 31, 2003 and 2002, respectively.

Depreciation expense (including amortization of the capital lease) amounted to \$67.3 million, \$53.1 million and \$42.9 million for the years ended December 31, 2003, 2002 and 2001, respectively.

5. Restricted Cash-Escrows

Restricted cash escrows include \$6.5 million and \$3.5 million at December 31, 2003 and 2002, respectively, of escrows and reserve funds for real estate taxes, property insurance, capital and tenant improvements and leasing costs established pursuant to certain mortgage loan agreements.

6. Investments in Affiliates

The Company holds interests in several domestic and international joint ventures. Non-controlling investments are accounted for under the equity method. Equity in earnings or losses of these affiliates and related management advisory, license, leasing and guarantee fees earned are included in income from unconsolidated investments and loss from impairment of Chelsea Interactive in the accompanying financial statements.

As of December 31, 2003 and 2002, the Company's interests in joint ventures included: a 50% interest in Las Vegas Premium Outlets ("Simon-Las Vegas") and a 50% interest in Chicago Premium Outlets ("Simon-Chicago") with Simon (collectively "Simon-Ventures"); a 40% interest in Chelsea Japan Co., Ltd. ("Chelsea Japan"); a 50% interest in a strategic alliance with Sordo Madaleno y Asociados and affiliates; minority interests in various outlet centers and development projects in Europe operated by Value Retail PLC ("Value Retail"); and 100% of the non-voting preferred stock of Chelsea Interactive and 50% of the non-voting common stock representing 40% of the total common stock. As of December 31, 2001, the Company's investment in joint ventures also included a 50% interest in Simon-Orlando and a 49% interest in F/C Acquisition.

Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements

6. Investments in Affiliates (continued)

In June 2002, the Company and Simon entered into a 50/50 joint venture to develop and operate Las Vegas Premium Outlets, a 435,000 square-foot single-phase outlet center located in Las Vegas, Nevada, which opened on August 1, 2003. The Company is responsible for financing its 50% share of development costs, or approximately \$48.0 million. As of December 31, 2003, the Company had contributed \$44.7 million and capitalized interest and other costs of \$2.3 million.

In August 2002, the Company and Simon entered into a new 50/50 joint venture to develop and operate Simon-Chicago, a 438,000 square-foot single-phase premium outlet center located in Aurora, Illinois, near Chicago. The center is scheduled to open in mid-2004. On September 23, 2002, Simon-Chicago purchased a 140-acre site, including 80 acres of conservation area, and commenced construction. The Company is responsible for financing its 50% share of the development costs, which are expected to be approximately \$46.0 million. As of December 31, 2003, the Company had contributed \$26.7 million and capitalized interest and other costs of \$1.5 million.

In June 1999, the Company entered into an agreement with Mitsubishi Estate Co., Ltd. and Nissho Iwai Corporation to jointly develop, own and operate Premium Outlet centers in Japan. The Company has a 40% interest in Chelsea Japan. In conjunction with the agreement, the Company contributed \$1.7 million in equity and provides its share of construction financing and/or loan guarantees. Chelsea Japan opened its initial project, the 220,000 square-foot first phase of Gotemba Premium Outlets, on July 13, 2000. Gotemba has grown to 390,000 square feet with the completion of its 170,000 square-foot second phase that opened in July 2003. Gotemba is located on the Tomei Expressway, approximately 60 miles west of Tokyo and midway between Mt. Fuji and the Hakone resort area. Chelsea Japan opened its second project, located outside Osaka, the second-largest city in Japan, the 180,000 square-foot first phase of Rinku Premium Outlets on November 23, 2000. Rinku increased to 250,000 square feet in March 2002, upon opening its 70,000 square-foot second phase. Rinku's 70,000 square-foot third phase is scheduled to open in late 2004. Chelsea Japan's third project, the 180,000 square foot first phase of Sano Premium Outlets opened in March 2003 and in Fall 2004, Sano is scheduled to open its 55,000 square foot second phase. Sano is located 40 miles north of Tokyo off Tohoku Expressway.

In May 2002, the Company entered into a 50/50 joint venture agreement with Sordo Madaleno y Asociados and affiliates to jointly develop Premium Outlet centers in Mexico. Construction on the 230,000 square-foot first phase of Punta Norte Premium Outlets commenced in July 2003 and the center is scheduled to open in late 2004. The Company is responsible for financing its 50% share of project costs of approximately \$15.0 million. As of December 31, 2003, the Company contributed \$2.5 million. In January 2004, an affiliate of the Company entered into a 180.0 million Peso denominated credit facility which is guaranteed by the Company to fund its share of construction costs.

At December 31, 2003 and 2002, the Company had minority interests ranging from 3% to 8% and 5% to 15% at December 31, 2001, in several outlet centers and outlet development projects in Europe. Five outlet centers, containing approximately 900,000 square feet of GLA, including Bicester Village, outside London, England, La Roca Company Stores outside of Barcelona, Spain, Las Rozas Village outside Madrid, Spain, La Vallee near Disneyland Paris and Maasmechelen Village in Belgium are currently open and operated by Value Retail PLC and its affiliates. In July 2002, the Company sold approximately 40% of its holdings in Value Retail to a third party for \$11.4 million, resulting in a gain of approximately \$10.9 million which was recorded as a gain on sale of unconsolidated investments in the accompanying financial statements. In 2001, the Company sold a portion of its Bicester Village holding resulting in a gain of \$1.8 million, which was included in gain on sale of unconsolidated investments, net of write-down in the accompanying financial statements.

Chelsea Property Group, Inc.
Notes to Condensed Consolidated Financial Statements

6. Investments in Affiliates (continued)

The Company and Simon entered into a 50/50 joint venture agreement to develop and operate Simon-Orlando a 428,000 square foot center that was completed in May 2000 and is located on Interstate 4, midway between Walt Disney World/EPCOT and Sea World in Orlando. In April 2002, the Company purchased Simon's 50% undivided ownership interest in the center for \$46.6 million in cash and assumed Simon's \$29.7 million pro-rata share of existing mortgage debt. The operations and balance sheet of the center are consolidated in the accompanying financial statements from the buyout date.

In December 2000, the Company and Fortress acquired four outlet centers from a competitor, through F/C Acquisition in which the Company had a 49% interest. The total purchase price was \$240.0 million, including the assumption of approximately \$174.0 million of 6.99% fixed-rate non-recourse mortgage debt due in 2008. In July 2002, Fortress exercised its option under the F/C Limited Liability Company Agreement to invoke the "Buy/Sell Right" which gave the Company the option to sell its 49% ownership interest in F/C Acquisition or buy the partner's 51% ownership interest. On August 20, 2002, the Company exercised its right to buy the 51% interest for cash of \$58.9 million and assumed \$86.5 million of existing mortgage debt on the properties. The operations and balance sheet of the four F/C Acquisition Premium Outlet centers have been consolidated in the accompanying financial statements from the buyout date.

In December 2001, the Company had a 15% minority interest in a partnership that owns an outlet center located in Guam. The center had been generating operating losses and the Company did not anticipate recovering its investment. Therefore, in December 2001, the Company wrote off its investment in Guam and recognized a loss of \$1.2 million which is included in gain on sale of unconsolidated investments, net of write-down in 2001 in the accompanying financial statements. During the year ended December 31, 2002, the Company withdrew as a partner in the Guam outlet center.

Chelsea Interactive

At December 31, 2002, the Company recognized an impairment loss equal to the net book value of its investment in Chelsea Interactive. The Company believes that it will not be able to recover the net book value of its investment in Chelsea Interactive through future cash flows. A \$2.5 million funding loss was reported for the year ended December 31, 2003. Future funding by the Company will be reported as a loss in the period funding is required. Through December 31, 2003, the Company had funded \$54.9 million and anticipates that funding to Chelsea Interactive will not reach the Company's funding limit of \$60.0 million. On February 17, 2004, the Company announced a joint venture between Chelsea Interactive and a publicly traded third party, GSI Commerce, Inc. Under the terms of the agreement, Chelsea Interactive will no longer operate its e-commerce technology, but will retain a minority interest in GSI-Chelsea Solutions. Chelsea Interactive's largest clients have entered into service agreements with GSI-Chelsea Solutions and will transition e-commerce activities to the GSI-Chelsea platform by the second quarter of 2004.

Chelsea Property Group, Inc. Notes to Consolidated Financial Statements

The following is a summary of investments in and amounts due from affiliates at December 31, 2003 and 2002 (in thousands):

| | F/C | Chelsea Japan | Simon- Orlando | Simon- Ventures | Chelsea Interactive | Other | Tot |
|---|-----------|------------------|-------------------|--------------------|------------------------|----------|-------|
| Balance December 31, 2001... | \$ 36,118 | \$ 9,296 | \$ 9,723 | \$ - | \$ 34,856 | \$ 3,696 | \$ 93 |
| Additional investment..... | - | 655 | - | 31,281 | 13,508 | 303 | 45 |
| Income (loss) from unconsolidated investments..... | 4,331 | 4,136 | 1,310 | - | (13,386) | 25 | (3) |
| Distributions and fees..... | (2,841) | (2,528) | (250) | - | - | - | (5) |
| Buyout reclassifications.... | (36,531) | - | (9,199) | - | - | - | (45) |

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| | | | | | | | |
|--|---------|---------------|---------------|----------------|---------------------|----------------|-----------|
| Impairment loss..... | - | - | - | - | (34,370) | - | (34,370) |
| Disposition..... | - | - | - | - | - | (382) | (382) |
| Advances (net)..... | (1,077) | 912 | (1,584) | 638 | (608) | (35) | (1,077) |
| Balance December 31, 2002... | \$ - | \$ 12,471 | \$ - | \$ 31,919 | \$ - | \$ 3,607 | \$ 47,817 |
| | F/C | Chelsea Japan | Simon-Orlando | Simon-Ventures | Chelsea Interactive | Chelsea Mexico | |
| Balance December 31, 2002..... | \$ - | \$ 12,471 | \$ - | \$ 31,919 | \$ - | \$ - | \$ 44,390 |
| Additional Investment..... | - | 1,591 | - | 43,965 | - | 6,212 | 51,768 |
| Income (loss) from unconsolidated investments..... | - | 8,574 | - | 2,432 | - | - | 11,006 |
| Distributions and fees..... | - | (5,102) | - | (2,754) | - | - | (7,856) |
| Foreign exchange..... | - | 503 | - | - | - | - | 503 |
| Advances (net)..... | - | 1,424 | - | 2,177 | - | - | 3,601 |
| Balance December 31, 2003... | \$ - | \$ 19,461 | \$ - | \$ 77,739 | \$ - | \$ 6,212 | \$ 93,412 |

Chelsea Property Group, Inc.
Notes to Condensed Consolidated Financial Statements

The Company's share of income before depreciation, depreciation expense and income from unconsolidated investments for the years ended December 31, 2003, 2002 and 2001 is as follows (in thousands):

| For the Year Ended: | F/C | Chelsea Japan | Simon-Orlando | Simon-Ventures | Other | Total |
|---|----------|---------------|---------------|----------------|----------|-----------|
| December 31, 2003 | | | | | | |
| Income (loss) before depreciation..... | \$ - | \$ 11,923 | \$ - | \$ 3,152 | \$ - | \$ 15,075 |
| Depreciation..... | - | 3,349 | - | 720 | - | 4,069 |
| Income (loss) from unconsol. investment | \$ - | \$ 8,574 | \$ - | \$ 2,432 | \$ - | \$ 11,006 |
| December 31, 2002 | | | | | | |
| Income (loss) before depreciation..... | \$ 6,178 | \$ 5,932 | \$ 1,833 | \$ - | \$ 25 | \$ 13,968 |
| Depreciation..... | 1,847 | 1,796 | 523 | - | - | 4,166 |
| Impairment loss..... | - | - | - | - | - | - |
| Income (loss) from unconsol. investment | \$ 4,331 | \$ 4,136 | \$ 1,310 | \$ - | \$ 25 | \$ 9,802 |
| December 31, 2001 | | | | | | |
| Income (loss) before depreciation..... | \$ 9,214 | \$ 4,676 | \$ 7,374 | \$ - | \$ (275) | \$ 20,989 |
| Depreciation..... | 2,692 | 1,390 | 1,882 | - | - | 5,964 |
| Income (loss) from unconsol. investment | \$ 6,522 | \$ 3,286 | \$ 5,492 | \$ - | \$ (275) | \$ 15,025 |

(1) A \$2.5 million funding loss was reported for the year ended December 31, 2003.

Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements

Condensed financial information as of December 31, 2003 and 2002, and for the years then ended for Chelsea Japan and Simon-Ventures (which are included in "Real Estate") and Chelsea Interactive is as follows (in thousands):

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| | Real Estate ----- | Chelsea Interactive ----- |
|--------------------------------------|----------------------|---------------------------------|
| Property, plant and equipment (net) | | |
| December 31, 2003..... | \$288,780 | \$ - |
| December 31, 2002..... | 140,057 | - |
| Total assets | | |
| December 31, 2003..... | 380,426 | - |
| December 31, 2002..... | 190,157 | 1,887 |
| Long term debt (1) | | |
| December 31, 2003..... | 129,731 | - |
| December 31, 2002..... | 75,139 | - |
| Total liabilities | | |
| December 31, 2003..... | 220,238 | 1,352 |
| December 31, 2002..... | 119,886 | 1,548 |
| Net income (loss) | | |
| December 31, 2003..... | 12,717 | (2,518) |
| December 31, 2002..... | 12,594 | (14,247) |
| Company's share of net income (loss) | | |
| December 31, 2003..... | 5,488 | (2,518) |
| December 31, 2002..... | 5,795 | (13,386) |
| Fee income | | |
| December 31, 2003..... | 5,518 | - |
| December 31, 2002..... | 3,982 | - |

(1) Long-term debt in 2003 and 2002 consists of borrowings related to Chelsea Japan.

7. Deferred Costs

The following summarizes the carrying amounts for deferred costs at December 31, 2003 and 2002 (in thousands):

| | 2003 ----- | 2002 ----- |
|--------------------------------|-----------------|---------------|
| Lease costs..... | \$29,609 | \$28,074 |
| FAS 141 lease adjustment..... | 8,536 | - |
| Financing costs..... | 10,506 | 9,200 |
| Development costs..... | 2,311 | 1,572 |
| Other..... | 371 | 871 |
| | ----- | ----- |
| Total deferred costs..... | 51,333 | 39,717 |
| Accumulated amortization..... | (28,344) | (23,011) |
| | ----- | ----- |
| Total deferred costs, net..... | \$22,989 | \$16,706 |
| | ===== | ===== |

Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements

8. Non-Compete Agreement

In October 1998 the Company sold its interest in and terminated the development of Houston Premium Outlets, a joint venture project with Simon. Under the terms of the agreement, the Company received non-compete payments totaling \$21.4 million from The Mills Corporation; \$3.0 million at closing and four annual installments of \$4.6 million, terminating in January 2002. The January 2002 payment had a \$0.3 million legal escrow reserve withheld. The revenue is being recognized on a straight-line basis over the term of the non-compete agreement and the Company recognized income of \$5.1 million during the years ended December 31, 2002 and 2001. Such amounts are included in other income in the accompanying financial statements.

9. Other Assets

The following summarizes the components of other assets at December 31 (in thousands):

| | 2003 | 2002 |
|--------------------------------|----------|----------|
| | ----- | ----- |
| Sales tax receivable..... | \$10,728 | \$11,708 |
| Prepaid expenses..... | 10,680 | 9,902 |
| Deferred compensation..... | 8,800 | 6,400 |
| Non-compete receivable..... | 300 | 300 |
| Due from equity investees..... | - | 136 |
| Other..... | 2,240 | 1,654 |
| | ----- | ----- |
| Total other assets..... | \$32,748 | \$30,100 |
| | ===== | ===== |

Chelsea Property Group, Inc. Notes to Consolidated Financial Statements

10. Debt

Unsecured Bank Debt

The Company has a \$200.0 million senior unsecured bank line of credit (the "Senior Credit Facility") with an expiration date of March 31, 2005, which the Company has the right to extend until March 31, 2006. The Senior Credit Facility bears interest on the outstanding balance, payable monthly, at a rate equal to the London Interbank Offered Rate ("LIBOR") plus 0.95% (2.09% at December 31, 2003) or the prime rate, at the Company's option. The LIBOR rate spread ranges from 0.85% to 1.50% depending on the Company's Senior Debt rating. The Company received a debt rating upgrade in July 2003, resulting in a reduction of the LIBOR rate spread to 0.95% from 1.05%. At December 31, 2003, \$99.0 million was outstanding under the Senior Credit Facility.

The Company also has a \$5.0 million term loan that carries the same interest rate and maturity as the Senior Credit Facility.

The Company has a one-year \$100.0 million unsecured bridge loan (the "Bridge Loan Facility") due July 31, 2004 and has the right to extend the loan until January 31, 2005. The Bridge Loan Facility bears interest on the outstanding balance, payable monthly, at a rate equal to LIBOR plus 0.80% (1.96% at December 31, 2003). The LIBOR rate spread ranges from 0.70% to 1.35% depending on the Company's Senior Debt rating.

Unsecured Notes

A summary of the terms of the unsecured notes outstanding at December 31, 2003 and December 31, 2002, is as follows (in thousands):

| December 31, | December 31, | Effective |
|--------------|--------------|-----------|
|--------------|--------------|-----------|

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| | 2003 | 2002 | Yield (1) |
|--|-----------|-----------|-----------|
| 8.375% Unsecured Notes due August 2005.... | \$ 49,952 | \$ 49,922 | 8.44% |
| 7.250% Unsecured Notes due October 2007... | 124,874 | 124,841 | 7.39% |
| 8.625% Unsecured Notes due August 2009.... | 49,943 | 49,933 | 8.76% |
| 8.250% Unsecured Notes due February 2011.. | 148,963 | 148,817 | 8.40% |
| 6.875% Unsecured Notes due June 2012..... | 99,878 | 99,825 | 6.90% |
| 6.000% Unsecured Notes due January 2013... | 148,193 | 147,992 | 6.18% |
| | ----- | ----- | |
| Total unsecured notes | \$621,803 | \$621,330 | |
| | ===== | ===== | |

(1) Including discount on the notes

Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements

10. Debt (continued)

Mortgage Debt

A summary of the terms of the mortgage debt outstanding at December 31 2003 and 2002, and the related interest rate and Net Book Value ("NBV") of the associated collateral as of December 31, 2003, is as follows (in thousands):

| | December 31, 2003 | December 31, 2002 | Effective Interest Rate | NBV |
|----------------------------|----------------------|----------------------|-------------------------------|-----------|
| Due July 2008 (1)..... | \$164,727 | \$167,723 | 7.26% | \$252,972 |
| Due April 2010 (2)..... | 61,475 | 67,250 | 7.26% | 67,978 |
| Due December 2012 (3)..... | 25,477 | - | 6.29% | 101,341 |
| Due December 2012 (4)..... | 70,460 | 71,482 | 7.67% | 74,416 |
| Due March 2013 (5)..... | 63,495 | - | 5.10% | 112,650 |
| | ----- | ----- | | ----- |
| | \$385,634 | \$306,455 | | \$609,357 |
| | ===== | ===== | | ===== |

- 1) The F/C mortgage loan was consolidated as part of the August 20, 2002 buyout of Fortress' 51% interest in the F/C Acquisition joint venture. The mortgage bears interest at 6.99% per annum through July 11, 2008, (the "Optional Prepayment Date") and thereafter at a rate equal to the greater of 8.4% plus 5% or the Treasury Rate, as defined, plus 6.5% until the earlier of the date the mortgage is paid in full or its maturity date of July 11, 2028. The mortgage may be prepaid in whole or in part at any time after the Optional Prepayment Date without a prepayment penalty. The mortgage calls for a \$1.2 million fixed monthly interest plus principal payment based on a 26-year amortization schedule. The F/C Mortgage Loan had a face value of \$169.6 million and a carrying amount fair value of \$168.7 million on the buyout date. During the year ended December 31, 2003, the Company recognized \$135,000 in debt discount amortization that is included in interest expense in the accompanying financial statements.
- 2) In April 2000, Chelsea Financing entered into a \$70.0 million mortgage loan due April 2010 originally secured by its four properties. On June 2, 2003 the Company sold one of the encumbered properties for \$7.4 million with an NBV of \$2.5 million. Proceeds of \$5.0 million were used to pay down the mortgage loan. In February 2004, the Company amended the mortgage loan to unsecure the properties and reduced the interest rate to LIBOR plus 1.25% from LIBOR plus 1.50% (2.62% at December 31, 2003). The loan calls for quarterly principal amortization of \$0.25 million through April 2005 and thereafter \$0.45 million per quarter until maturity. In December 2000, the Company entered into an interest rate swap agreement to hedge against unfavorable

fluctuations in LIBOR rates by fixing the interest rate at 7.26% until January 2006. During the years ended December 31, 2003 and 2002, the Company recognized interest expense of \$3.1 million and \$2.7 million, respectively on the hedge that is included in interest expense in the accompanying financial statements.

- 3) The mortgage loan due December 2012 was assumed as part of an August 2003 acquisition. The stated interest rate of 8.12% was greater than that available to the Company for comparable debt. Consequently, the Company recognized a \$1.9 million debt premium that will be amortized over the period of the loan, which reduces the effective interest rate to 6.29%. The mortgage loan calls for a \$0.3 million fixed monthly debt service payment on a 17-year amortization schedule. During the year ended December 31, 2003, the Company recognized approximately \$120,000 in debt premium amortization that is included in interest expense in the accompanying financial statements.
- 4) The mortgage loan was assumed as part of a September 2001 acquisition. The stated interest rate of 9.1% was greater than that available to the Company in the public debt markets. Accordingly, the Company recorded a \$6.9 million debt premium that will be amortized over the period of the loan which reduces the effective interest rate to 7.67%. The loan calls for fixed monthly debt service payments of \$0.5 million for interest plus principal based on a 26-year amortization schedule. The mortgage loan matures in March 2028 but can be prepaid beginning December 2012. During the years ended December 31, 2003 and 2002, the Company recognized \$0.5 million and \$0.4 million, respectively, in debt premium amortization that is included in interest expense in the accompanying financial statements.
- 5) The mortgage loan due March 2013 was assumed as part of a June 2003 acquisition. The stated interest rate of 5.85% was greater than that available to the Company for comparable debt. Accordingly, the Company recorded a \$3.4 million debt premium that will be amortized over the period of the loan, which reduces the effective interest rate to 5.10%. The loan calls for a \$0.4 million fixed monthly debt service payment on a 25-year amortization schedule. During the year ended December 31, 2003, the Company recognized approximately \$144,000 in debt premium amortization that is included in interest expense in the accompanying financial statements.

Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements

10. Debt (continued)

Mortgage Debt (continued)

Following is a schedule of the estimated fair value of the Company's debt using current broker quotations at December 31, 2003, (in thousands):

| Description | Carrying Value | Principal Balance | Estimated Fair Value |
|-------------------------|----------------|-------------------|----------------------|
| Fixed Rate Debt..... | \$945,962 | \$938,959 | \$1,043,232 |
| Variable Rate Debt..... | 265,510 | 265,510 | 265,510 |

Interest paid, excluding amounts capitalized, was \$70.2 million, \$47.5 million and \$34.5 million for the years ended December 31, 2003 2002 and 2001, respectively.

Following is a schedule of the Company's debt maturities, including debt premium amortization, at December 31, 2003, (in thousands):

| | |
|-----------------|--------------------|
| 2004..... | \$107,873 |
| 2005..... | 163,095 |
| 2006..... | 9,829 |
| 2007..... | 135,442 |
| 2008..... | 157,145 |
| Thereafter..... | 638,088 |
| | ----- |
| | \$1,211,472 |
| | ===== |

Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements

11. Financial Instruments: Derivatives and Hedging

In the normal course of business, the Company is exposed to the effect of interest rate changes. The Company limits these risks by following established risk management policies and procedures including the use of derivatives. For interest rate exposures, derivatives are used primarily to align rate movements between interest rates associated with the Company's financial assets with interest rates on related debt, and manage the cost of borrowing obligations. For foreign currency exposures, derivatives are used primarily to align movements between currency rates to protect forecasted returns of fees to the U.S.

The Company has a policy of only entering into contracts with major financial institutions based upon their credit ratings and other factors. When viewed in conjunction with the underlying and offsetting exposure that the derivatives are designed to hedge, the Company has not sustained a material loss from those instruments nor does it anticipate any material adverse effect on its net income or financial position in the future from the use of derivatives.

To manage interest rate and foreign currency risk, the Company may employ options, forwards, interest rate swaps, caps and floors or a combination thereof depending on the underlying exposure. The Company undertakes a variety of borrowings: from lines of credit, to medium- and long-term financings. To reduce overall interest cost, the Company uses interest rate instruments, typically interest rate swaps, to convert a portion of variable rate debt to fixed rate debt, or a portion of its fixed-rate debt to variable rate. Interest rate differentials that arise under these swap contracts are recognized in interest expense over the life of the contracts.

Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements

11. Financial Instruments: Derivatives and Hedging (continued)

Interest rate swaps that are designated as cash flow hedges hedge the future cash outflows on debt. Interest rate swaps that convert variable payments to fixed payments, interest rate caps, floors, collars, and forwards are cash flow hedges. Unrealized gains and losses in the fair value of cash flow hedges are reported on the balance sheet with a corresponding adjustment to Accumulated Other Comprehensive Income to the extent they are offsetting and otherwise qualify in the period for cash flow hedge accounting. Over time, the unrealized gains and losses held in Accumulated Other Comprehensive Income will be reclassified to earnings through interest expense. This reclassification occurs over the same time period in which the hedged items affect earnings. The Company hedges its exposure to variability in future cash flows for forecasted transactions other than those associated with existing floating-rate debt over a maximum period of 12 months. During the forecast period, unrealized gains and losses in the hedging instrument will be reported in Accumulated Other Comprehensive Income. Once the hedged transaction takes

place, the hedge gains and losses will be reported in earnings during the same period in which the hedged item is recognized in earnings. During 2003, the Company paid down approximately \$5.0 million of hedged debt and reclassified approximately \$0.5 million out of accumulated other comprehensive loss to other expense. The ineffective portion of the hedge will be marked to market through earnings.

The notional value and fair value of the swap provide an indication of the extent of the Company's involvement in financial derivative instruments at December 31, 2003. It does not represent exposure to credit, interest rate or market risks. At December 31, 2003, and 2002, the swap was reported at its fair value and classified as other liabilities in the accompanying financial statements of \$4.8 million and \$6.7 million, respectively. Within the next twelve months, the Company expects to reclassify to earnings approximately \$2.7 million of the current balance held in accumulated other comprehensive loss related to the interest rate swap.

| As of December 31, 2003 | | | | |
|-------------------------|----------------|---------|----------|-------------|
| Hedge Type | Notional Value | Rate | Maturity | Fair Value |
| Swap, Cash Flow | \$66.5 mil | 5.7625% | 1/1/06 | (\$4.8 mil) |

During 2002, the Company had Japanese yen forward contracts with a notional value of 255 million yen and a fair value of \$10,000 as a hedge against its yen-denominated receivable due from Chelsea Japan. During the year ended December 31, 2002, the receivable and yen forward contracts were settled and the Company received \$1.9 million and recognized a \$0.1 million foreign exchange loss, which is included in income from unconsolidated investments in the accompanying financial statements.

During 2001, the Company entered into a yen forward contract with a notional value of \$1.4 million and a fair value of \$40,000 as a hedge against its yen-denominated receivable. During the year ended December 31, 2001 the receivable and yen forward contract were settled and the Company received \$1.4 million.

12. Preferred Stock

In October 1997, the Company issued 1.0 million shares of non-voting 8.375% Series A Cumulative Redeemable Preferred Stock (the "Preferred Stock"), par value \$0.01 per share, having a liquidation preference of \$50 per share. The Preferred Stock has no stated maturity and is not convertible into any other securities of the Company. The Preferred Stock is redeemable on or after October 15, 2027, at the Company's option.

During the year ended December 31, 2002, the Company redeemed and retired 136,500 shares of Preferred Stock at a net price of \$47 per share and 66,552 shares at a net share of \$47.25 per share.

Chelsea Property Group, Inc. Notes to Consolidated Financial Statements

13. Common Stock

At a special meeting of shareholders held on January 16, 2003, the Company obtained shareholder approval to amend its articles of incorporation to increase the authorized shares of the Company's common stock to 100 million shares.

In June 2003, the Company sold 1.2 million shares of common stock at a price of \$42.10 per share, yielding net proceeds after expenses of \$49.4 million, which were used to fund the Crossings acquisition.

In November 2002, the Company sold 3.5 million shares of common stock at a price of \$34.65 per share, yielding net proceeds after expenses of \$118.8 million, which were used to fund the NPXL acquisition.

On May 1, 2002, the Company declared a 2-for-1 stock split on the Company's common shares. The stock dividend was paid May 28, 2002, to shareholders of record on May 14, 2002.

14. Lease Agreements

The Company is the lessor and sub-lessor of retail stores under operating leases with term expiration dates ranging from 2004 to 2020. Most leases are renewable for five years after expiration of the initial term at the lessee's option. Future minimum lease receipts under non-cancelable operating leases at December 31, 2003, exclusive of renewal option periods, were as follows (in thousands):

| | |
|-----------------|--------------------|
| 2004..... | \$ 252,259 |
| 2005..... | 230,216 |
| 2006..... | 196,693 |
| 2007..... | 162,283 |
| 2008..... | 129,848 |
| Thereafter..... | 309,278 |
| | ----- |
| | \$1,280,577 |
| | ===== |

In 1987, a predecessor partnership entered into a lease agreement for property in California. Land was estimated to be approximately 37% of the fair market value of the property, and accordingly the portion of the lease attributed to land was classified as an operating lease. The portion attributed to building was classified as a capital lease as the present value of payments related to the building exceeded 90% of its fair value at inception of the lease. The initial lease term was 25 years with two options of 5 and 4.5 years, respectively. The lease provided for additional rent based on specific levels of income generated by the property. No additional rental payments were incurred during 2003, 2002 or 2001. The Company terminated the lease agreement and recognized a \$0.1 million gain on the termination.

Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements

14. Lease Agreements (continued)

Operating Leases

Future minimum rental payments under operating leases for administrative offices at December 31, 2003, are as follows (in thousands):

| | |
|-----------|----------------|
| 2004..... | \$1,480 |
| 2005..... | 916 |
| 2006..... | 52 |
| | ----- |
| | \$2,448 |
| | ===== |

Rental expense amounted to \$1.4 million for the years ended December 31, 2003 and 2002, and \$0.8 million for the year ended December 31, 2001.

Capital Lease

A leased property included in rental properties at December 31, 2002 consisted of the following (in thousands):

| | |
|------------------------------------|---------|
| Building..... | \$6,796 |
| Less accumulated amortization..... | (5,865) |

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| | |
|---------------------------|--------|
| Leased property, net..... | \$ 931 |
|---------------------------|--------|

Amortization expense on capital lease of \$0.9 million for the year ended December 31, 2003 and \$0.3 million for the years ended December 31, 2002 and 2001, is included in depreciation and amortization expense in the financial statements.

Ground Lease

In connection with the 2003 and 2002 property acquisitions, the Company acquired six properties subject to ground leases that were assumed by the Company. These ground leases have termination dates ranging from 2007 to 2087 and allow for renewal terms of 4 to 30 years.

Future minimum lease payments under ground leases at December 31, 2003, exclusive of renewal option periods were as follows (in thousands):

| | |
|-----------------|----------|
| 2004..... | \$ 819 |
| 2005..... | 819 |
| 2006..... | 822 |
| 2007..... | 811 |
| 2008..... | 1,547 |
| Thereafter..... | 17,368 |
| | ----- |
| | \$22,186 |
| | ===== |

**Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements**

15. Commitments and Contingencies

In connection with the Simon-Ventures, the Company has committed to provide 50% of the development costs or approximately \$48.0 million to Simon-Las Vegas and \$46.0 million to Simon-Chicago. As of December 31, 2003, the Company had contributed \$44.7 million to Simon-Las Vegas and \$26.7 million to Simon-Chicago.

Borrowings related to Chelsea Japan for which the Company and the OP have provided guarantees for repayment of debt as of December 31, 2003, are as follows (in thousands):

| Total Facility | | | Outstanding | | | Due Date | Interest Rate |
|-----------------|------------------|--|-------------|------------------|-----------------|----------|---------------|
| Yen | US \$ Equivalent | | Yen | US \$ Equivalent | US \$ Guarantee | | |
| 4.0 billion (1) | \$37.3 million | | 0.9 billion | \$8.4 million | \$ 8.4 million | 2004 | 1.31% |
| 3.8 billion (2) | 35.4 million | | 3.2 billion | 30.0 million | 12.0 million | 2015 | 2.20% |
| 0.6 billion (2) | 5.6 million | | 0.5 billion | 4.7 million | 1.9 million | 2012 | 1.50% |

(1) Facility entered into by an equity investee of the Company and has a one-year extension option; until April 1, 2005.

(2) Facilities entered into by Chelsea Japan, secured by Gotemba and Rinku and 40% severally guaranteed by the Company.

In May 2002, the Company entered into a 50/50 joint venture agreement with Sordo Madaleno y Asociados and affiliates to jointly develop Premium Outlet centers in Mexico. Construction on the 230,000 square-foot first phase of Punta Norte Premium Outlets commenced in July 2003 and the center is scheduled to open in late 2004. The

Company is responsible for financing its share of project costs of approximately \$15.0 million. As of December 31, 2003, the Company had contributed \$2.5 million. In January 2004, an affiliate of the Company entered into a Peso denominated credit facility which is guaranteed by the Company to fund its share of construction costs.

As of December 31, 2003, the Company had provided limited debt service guarantees of approximately \$17.1 million to Value Retail and affiliates, under a standby facility for loans provided to Value Retail and affiliates to construct outlet centers in Europe. The standby facility, which has a maximum limit of \$22.0 million, expired in November 2001, and outstanding guarantees, shall not survive more than five years after project completion.

At December 31, 2003, other assets include \$8.8 million and accrued expenses and other liabilities include \$17.6 million related to the 2002 deferred unit incentive program which may be paid to certain key officers in 2007.

The Company is not presently involved in any material litigation nor, to its knowledge, is any material litigation threatened against the Company or its properties, other than routine litigation arising in the ordinary course of business. Management believes the costs incurred by the Company related to any of its litigation will not be material and have been adequately provided for in the consolidated financial statements.

Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements

16. Related Party Information

In 1999, the Company established a \$6.0 million secured loan facility that expires in June 2004 for the benefit of certain unitholders. Each borrower issued a note that is secured by OP units, bears interest at a rate of LIBOR plus 200 basis points per annum payable quarterly and is due by the facility expiration date. At December 31, 2003, the \$2.2 million note receivable from related parties represents a loan made to a unitholder, who is also an officer and director of the Company. During the year ended December 31, 2003, the Company received \$1.1 million from a unitholder in full repayment of his loan. Effective June 2002, the Company changed its policy to eliminate new loans to directors and officers.

The Company leased space to related parties of approximately 56,000 square feet during the year ended December 31, 2001. Rental income from those tenants, including reimbursement for taxes, common area maintenance and advertising, totaled \$2.1 million during the year ended December 31, 2001.

In August 1997, the Company and one of its directors entered into a Consulting Agreement pursuant to which the director agreed to perform services for the Company in connection with the development and operation of manufacturer's outlet centers in Japan and Hawaii. The agreement provided for payments to the director of \$10,000 per month and was terminated by the Company in December 1999. During the term of the agreement and for four years after the termination, the director will be entitled to deferred compensation of 1% of the development costs, up to a maximum amount of \$0.5 million per project, on all projects in which he was involved in Japan or Hawaii either directly or as a result of Mitsubishi and/or Nissho Iwai committing to develop such project with the Company in Japan during the previously mentioned four year period. Fees paid under this agreement totaled \$0.3 million for the year ended December 31, 2003. These fees are included in investment in affiliates in the accompanying financial statements. The final payment under this agreement, related to the opening of Tosu Premium Outlets which was Board approved during 2003, is expected to be paid in 2004.

17. Dividend Reinvestment Plan

Shareholders who own at least 100 shares of the Company's common stock are eligible to reinvest dividends quarterly. The Company pays administration costs associated with the plan.

Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements

18. Employee Stock Purchase Plan

The Company's Board of Directors and shareholders approved an Employee Stock Purchase Plan (the "Purchase Plan"), effective July 1, 1998. The Purchase Plan covers an aggregate of 1.0 million shares of common stock. Eligible employees have been in the employ of the Company or a participating subsidiary for five months or more and customarily work more than 20 hours per week. The Purchase Plan excludes employees who are "highly compensated employees", as defined, or own 5% or more of the voting interest of the Company's stock. Eligible employees will purchase shares through automatic payroll deductions up to a maximum of 10% of weekly base pay. The Purchase Plan will be implemented by consecutive three-month offerings (each an "Option Period"). The price at which shares may be purchased shall be the lower of (a) 85% of the fair market value of the stock on the first day of the Option Period or (b) 85% of the fair market value of the stock on the last day of the Option Period. As of December 31, 2003, 118 employees were enrolled in the Purchase Plan and \$10,000 in expenses has been incurred and is included in the Company's general and administrative expense. The Purchase Plan will terminate in July 2008 unless terminated earlier by the Board of Directors.

19. 401(k) Plan

The Company maintains a defined contribution 401(k) savings plan (the "Plan"), which was established to allow eligible employees to make tax-deferred contributions through voluntary payroll withholdings. All employees of the Company are eligible to participate in the Plan after completing six months of service and attaining age 21. Employees who elect to enroll in the Plan may elect to have from 1% to 15% of their pre-tax gross pay contributed to their account each pay period. As of January 1, 1998 the Plan was amended to include an employer discretionary matching contribution which currently excludes certain officers, in an amount not to exceed 100% of each participant's first 6% of yearly compensation to the Plan. Matching contributions of approximately \$156,000 in 2003, \$96,000 in 2002 and \$128,000 in 2001 are included in the Company's general and administrative expense in the accompanying financial statements.

20. Quarterly Financial Information (Unaudited)

The following summary represents the results of operations, expressed in thousands except per share amounts, for each quarter during 2003 and 2002:

| | March 31 | June 30 | September 30 | December 31 |
|--|----------|----------|--------------|-------------|
| | ----- | ----- | ----- | ----- |
| 2003 | | | | |
| ---- | | | | |
| Base rental revenue..... | \$59,159 | \$59,461 | \$63,645 | \$ 65,629 |
| Total revenues..... | 83,282 | 86,609 | 92,203 | 110,171 |
| Net income available to common shareholders..... | 18,413 | 24,705 | 25,006 | 30,068 |
| Net income per weighted average common share..... | \$0.43 | \$0.56 | \$0.55 | \$0.66 |
| 2002 | | | | |
| ---- | | | | |
| Base rental revenue..... | \$37,629 | \$42,458 | \$46,100 | \$ 52,111 |
| Total revenues..... | 55,395 | 63,844 | 70,387 | 88,863 |
| Net income (loss) available to common shareholders..... | 11,887 | 13,408 | 24,223 | (7,804) |
| Net income(loss) per weighted average | | | | |

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common share (diluted, except for the
quarter ended December 31)..... \$0.31 \$0.34 \$0.61 \$ (0.20)

Chelsea Property Group, Inc.
Notes to Consolidated Financial Statements

21. Segment Information

The Company is principally engaged in the development, ownership, acquisition and operation of manufacturers' outlet centers and has determined that under SFAS No.131 "Disclosures About Segments of an Enterprise and Related Information" it has three reportable real estate segments: premium domestic, other domestic and international in 2003 and 2002. The Company evaluates real estate performance and allocates resources based on Net Operating Income ("NOI") defined as total revenue less operating expenses. The primary sources of revenue are generated from tenant base rents, percentage rents and reimbursement revenue. Operating expenses primarily consist of common area maintenance, real estate taxes and promotional expenses. The real estate business segments meet the quantitative threshold for determining reportable segments:

| For the years ended: (in thousands) | Premium Domestic | Other Domestic | International | Other | Total |
|--|---------------------|-------------------|---------------|----------|-----------|
| | | (2) | (3) | (4) | |
| Total revenues (1) | | | | | |
| December 31, 2003..... | \$ 266,944 | \$104,797 | \$ - | \$ 524 | \$372,265 |
| December 31, 2002..... | 224,701 | 48,306 | - | 5,482 | 278,489 |
| Interest income (1) | | | | | |
| December 31, 2003..... | 1,015 | 35 | - | 156 | 1,206 |
| December 31, 2002..... | 1,169 | 124 | - | 358 | 1,651 |
| Income (loss) from unconsolidated investments | | | | | |
| December 31, 2003..... | 2,432 | - | 8,574 | (2,518) | 8,488 |
| December 31, 2002..... | 5,641 | - | 15,072 | (47,756) | (27,043) |
| NOI | | | | | |
| December 31, 2003..... | 196,444 | 70,386 | 15,449 | (12,985) | 269,294 |
| December 31, 2002..... | 176,001 | 30,664 | 7,891 | (12,216) | 202,340 |
| Fixed asset additions | | | | | |
| December 31, 2003..... | 17,404 | 239,519 | - | 1,006 | 257,929 |
| December 31, 2002..... | 398,933 | 309,540 | - | 795 | 709,268 |
| Total assets | | | | | |
| December 31, 2003..... | 1,341,535 | 501,093 | 29,306 | 98,480 | 1,970,414 |
| December 31, 2002..... | 1,262,190 | 394,984 | 16,077 | 29,779 | 1,703,030 |

- (1) Excludes revenue for St. Helena, Mesa and American Tin Cannery properties which are classified as discontinued operations.
- (2) Approximately 16% and 23% of the GLA is occupied by and approximately 9% and 12% of annual base rent is derived from one tenant during the 2003 and 2002 periods, respectively.
- (3) Principally comprised of the Company's interest in Chelsea Japan.
- (4) Includes corporate overhead assets and results from Chelsea Interactive.

Chelsea Property Group, Inc.

Notes to Consolidated Financial Statements

21. Segment Information (continued)

Following is a reconciliation of net operating income to net income for the years ended December 31, 2003 and 2002, (in thousands):

| | 2003 | 2002 |
|--|------------|------------|
| Segment NOI..... | \$ 269,294 | \$ 202,340 |
| Interest expense - consolidated..... | (69,215) | (48,693) |
| Interest expense - unconsolidated investments..... | (886) | (556) |
| Depreciation expense - consolidated..... | (73,651) | (58,275) |
| Depreciation expense - unconsolidated investments..... | (4,069) | (4,166) |
| Depreciation expense - Chelsea Interactive..... | - | (8,271) |
| Impairment loss- Chelsea Interactive..... | - | (34,370) |
| Income tax - unconsolidated investments..... | (2,640) | (1,378) |
| Gain/(loss) on sale of centers..... | 4,784 | 312 |
| Gain on sale, net of writedown - International..... | - | 10,911 |
| Minority interest..... | (22,089) | (12,718) |
| Net income..... | \$ 101,528 | \$ 45,136 |

22. Non-Cash Investing and Financing Activities

In December 2003, 2002 and 2001, the Company declared quarterly distributions per share of \$0.535, \$0.485, and \$0.390, respectively (assumes May 2002, 2-for-1 stock split occurred on January 1, 2001). The limited partners' distributions were paid in January of each subsequent year.

In connection with the Crossings and Las Vegas acquisitions, the Company assumed approximately \$64.1 million and \$26.3 million, respectively, in mortgage loans payable.

In connection with the buyout of Simon's 50% interest in Simon-Orlando in April 2002, the Company assumed additions of approximately \$68.9 million in rental properties, \$6.5 million in accumulated depreciation, \$8.8 million in other assets, \$3.2 million in other liabilities and \$59.4 million in mortgage debt.

In connection with the buyout of Fortress' 51% interest in F/C Acquisition in August 2002, the Company assumed additions of approximately \$207.0 million in rental properties, \$9.4 million in accumulated depreciation, \$11.7 million in other assets, and \$5.3 million in other liabilities and \$168.7 million in mortgage debt.

In connection with the purchase of the JMJ properties in November 2002, the OP issued 1.3 million units with an assigned value of \$44.6 million.

In connection with the Konover acquisition in 2001, the Company assumed approximately \$131.0 million in REMIC and mortgage loans payable.

Chelsea Property Group, Inc.
Schedule III-Consolidated Real Estate and Accumulated Depreciation
for the year ended December 31, 2003 (in thousands)

| Initial Cost to Company | Cost Capitalized (Disposed of) Subsequent to Acquisition (Improvements) | Step-Up Related to Acquisition of Partnership Interest (1) |
|-------------------------|--|---|
|-------------------------|--|---|

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| Description Outlet Center Name | Encum- brances | Buildings, Fixtures and Equipment | | | Buildings, Fixtures and Equipment | | | Land | Buildin Fixtures Equipmen |
|-----------------------------------|-------------------|---|-----------|-------------|---|-----------|-----------|---------|---------------------------------|
| | | Land | Equipment | Land | Equipment | Land | Equipment | | |
| Woodbury Common, NY | - | \$4,448 | \$16,073 | \$4,967 | \$127,871 | \$ - | \$ - | \$ - | |
| Orlando, FL (6) | - | 9,946 | 65,711 | 300 | 1,151 | 7,957 | 31,82 | | |
| Gilroy, CA (6) | (4) | 17,053 | 84,641 | 2 | 840 | 1,812 | 8,84 | | |
| Wrentham, MA | - | 157 | 2,817 | 3,842 | 84,595 | - | - | | |
| Waialeale, HI | - | 22,800 | 54,357 | - | 3,374 | - | - | | |
| Leesburg, VA | - | 6,296 | - | (811) | 71,995 | - | - | | |
| Desert Hills, CA | - | 975 | - | 2,376 | 67,366 | 830 | 4,93 | | |
| Michigan City, IN (6) | (4) | 7,264 | 60,107 | - | 885 | 772 | 6,24 | | |
| Camarillo, CA | - | 4,000 | - | 10,696 | 58,254 | - | - | | |
| Osage Beach, MO (6) | - | 10,395 | 58,701 | - | 1,869 | - | - | | |
| Jackson, NJ (6) | - | 10,302 | 58,178 | - | 339 | - | - | | |
| Albertville, MN (6) | - | 15,794 | 45,977 | 2,851 | 12,029 | - | - | | |
| North Georgia, GA | - | 2,960 | 34,726 | (223) | 22,252 | - | - | | |
| Waterloo, NY (6) | (4) | 5,258 | 42,942 | - | 670 | 559 | 4,51 | | |
| Clinton, CT | - | 4,124 | 43,656 | 202 | 1,674 | - | - | | |
| Allen, TX | - | 8,938 | 2,068 | (834) | 37,203 | - | - | | |
| Vacaville, CA | - | 9,683 | 38,850 | 18 | 1,921 | - | - | | |
| Folsom, CA | (2) | 4,169 | 10,465 | 2,692 | 27,140 | - | - | | |
| Carolina Outlet (I), NC | - | 6,220 | 24,860 | (181) | 794 | - | - | | |
| Carolina Outlet (II), NC | (5) | - | 7,862 | - | 305 | - | - | | |
| Petaluma Village, CA | - | 3,735 | - | 2,959 | 32,370 | - | - | | |
| St. Augustine, FL (6) | - | 5,783 | 32,658 | - | 585 | - | - | | |
| Liberty Village, NJ | - | 345 | 405 | 1,499 | 23,159 | 11,015 | 2,19 | | |
| Napa, CA | (2) | 3,456 | 2,113 | 7,908 | 19,756 | - | - | | |
| Kittery (I), ME (6) | (4) (5) | 2,143 | 23,985 | 6 | 289 | 228 | 2,35 | | |
| Kittery (II), ME | - | 567 | 2,265 | - | 92 | - | - | | |
| Johnson Creek, WI (6) | - | 4,648 | 26,341 | 3 | 113 | - | - | | |
| Aurora, OH | - | 637 | 6,884 | 1,055 | 23,023 | - | - | | |
| Edinburgh, IN (6) | - | 5,415 | 21,659 | - | 2,118 | - | - | | |
| North Bend, WA | - | 4,735 | 18,925 | (83) | (283) | - | - | | |
| The Crossings, PA | (7) | 17,187 | 97,443 | 35 | (597) | - | - | | |
| Las Vegas Outlet, NV | (8) | 15,930 | 90,270 | 19 | (3,915) | - | - | | |
| Branson II (6) | - | 2,892 | 16,332 | - | 270 | - | - | | |
| Columbia Gorge, OR | (2) | 934 | - | 428 | 13,845 | 497 | 2,64 | | |
| Santa Fe, NM | - | 74 | - | 1,300 | 12,188 | 491 | 1,77 | | |
| American Tin Cannery, CA | - | - | 8,621 | - | (8,621) | - | - | | |
| Patriot Plaza, VA | - | 789 | 1,854 | 976 | 4,081 | - | - | | |
| Corporate Offices, NJ, CA | - | - | 60 | - | 7,542 | - | - | | |
| St. Helena, CA | - | 1,029 | 1,522 | (1,067) | (1,600) | 38 | 7 | | |
| Poconos, PA | - | 330 | - | - | - | - | - | | |
| Tinton Falls, NJ | - | 110 | - | - | - | - | - | | |
| Chicago, IL | - | 465 | - | (465) | - | - | - | | |
| Las Vegas, NV | - | 405 | - | (405) | - | - | - | | |
| Other retail | (3) (5) | 15,406 | 64,911 | (2,885) | (6,986) | - | - | | |
| (2) (3) (4) | | 385,634 | \$237,797 | \$1,068,239 | \$37,180 | \$639,955 | \$24,199 | \$65,41 | |

Gross Amount Carried
at Close of Period
December 31, 2003

| Description Outlet Center Name | Land | Buildings, Fixtures and Equipment | | Total | Accumulated Depreciation | Date of Construction | Life Used Comput Depreciai in Late Income Stateme |
|-----------------------------------|---------|---|-----------|----------|-----------------------------|-------------------------|--|
| | | Equipment | Total | | | | |
| Woodbury Common, NY | \$9,415 | \$143,944 | \$153,359 | \$57,875 | '85, '93, '95, '98 | 40 | |
| Orlando, FL (6) | 18,203 | 98,691 | 116,894 | 14,161 | '00 | 40 | |
| Gilroy, CA (6) | 18,867 | 94,321 | 113,188 | 7,270 | '90, '91, '92, '94, '95 | 40 | |
| Wrentham, MA | 3,999 | 87,412 | 91,411 | 23,735 | '95, '00 | 40 | |
| Waialeale, HI | 22,800 | 57,731 | 80,531 | 13,190 | '98 | 40 | |
| Leesburg, VA | 5,485 | 71,995 | 77,480 | 19,090 | '96-'00 | 40 | |
| Desert Hills, CA | 4,181 | 72,302 | 76,483 | 31,164 | '90, '94-'95, '97, -'98 | 40 | |

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| | | | | | | |
|---------------------------|-----------|-------------|-------------|-----------|-----------------------------------|----|
| Michigan City, IN (6) | 8,036 | 67,235 | 75,271 | 5,220 | '87, '88, '89, '91, '94, '95, '97 | 40 |
| Camarillo, CA | 14,696 | 58,254 | 72,950 | 18,584 | '94-'99 | 40 |
| Osage Beach, MO (6) | 10,395 | 60,570 | 70,965 | 1,543 | '87-90 | 40 |
| Jackson, NJ (6) | 10,302 | 58,517 | 68,819 | 1,463 | '97, '98 | 40 |
| Albertville, MN (6) | 18,645 | 58,006 | 76,651 | 1,529 | '00, '01 | 40 |
| North Georgia, GA | 2,737 | 56,978 | 59,715 | 19,816 | '95-'99 | 40 |
| Waterloo, NY (6) | 5,817 | 48,131 | 53,948 | 3,716 | '95, '96, '97 | 40 |
| Clinton, CT | 4,326 | 45,330 | 49,656 | 18,533 | '95-'96 | 40 |
| Allen, TX | 8,104 | 39,271 | 47,375 | 6,520 | 99-'01 | 40 |
| Vacaville, CA | 9,701 | 40,771 | 50,472 | 2,333 | '88, '91, '92 | 40 |
| Folsom, CA | 6,861 | 37,605 | 44,466 | 13,425 | '90, '92, '93, '96-'97, '00 | 40 |
| Carolina Outlet (I), NC | 6,039 | 25,654 | 31,693 | 1,528 | '87, '95, '96, '99 | 40 |
| Carolina Outlet (II), NC | - | 8,167 | 8,167 | 502 | '87, '95, '96, '99 | 40 |
| Petaluma Village, CA | 6,694 | 32,370 | 39,064 | 11,742 | '93, '95-'96 | 40 |
| St. Augustine, FL (6) | 5,783 | 33,243 | 39,026 | 846 | '90-'92 | 40 |
| Liberty Village, NJ | 12,859 | 25,759 | 38,618 | 9,492 | '81, '97-'98 | 30 |
| Napa, CA | 11,364 | 21,869 | 33,233 | 8,275 | '62, '93, '95 | 40 |
| Kittery (I), ME (6) | 2,377 | 26,628 | 29,005 | 2,234 | '86 | 40 |
| Kittery (II), ME | 567 | 2,357 | 2,924 | 139 | '10, '84, '89, '95 | 40 |
| Johnson Creek, WI (6) | 4,651 | 26,454 | 31,105 | 873 | '98, '99, '01 | 40 |
| Aurora, OH | 1,692 | 29,907 | 31,599 | 10,777 | '90, '93, '94, '95 | 40 |
| Edinburgh, IN (6) | 5,415 | 23,777 | 29,192 | 1,020 | '89, '95 | 40 |
| North Bend, WA | 4,652 | 18,642 | 23,294 | 1,088 | '90, '95 | 40 |
| The Crossings, PA | 17,222 | 96,846 | 114,068 | 1,418 | '03 | 40 |
| Las Vegas Outlet, NV | 15,949 | 86,355 | 102,304 | 964 | '03 | 40 |
| Branson II (6) | 2,892 | 16,602 | 19,494 | 421 | '88, '94 | 40 |
| Columbia Gorge, OR | 1,859 | 16,492 | 18,351 | 6,371 | '91, '94 | 40 |
| Santa Fe, NM | 1,865 | 13,960 | 15,825 | 4,874 | '93, '98 | 40 |
| American Tin Cannery, CA | - | - | - | - | '87, '98 | 0 |
| Patriot Plaza, VA | 1,765 | 5,935 | 7,700 | 2,638 | '86, '93, '95 | 40 |
| Corporate Offices, NJ, CA | - | 7,602 | 7,602 | 4,824 | - | 5 |
| St. Helena, CA | - | - | - | - | '83 | 40 |
| Poconos, PA | 330 | - | 330 | - | - | 0 |
| Tinton Falls, NJ | 110 | - | 110 | - | - | 0 |
| Chicago, IL | - | - | - | - | - | 40 |
| Las Vegas, NV | - | - | - | - | - | 40 |
| Other retail | 12,521 | 57,925 | 70,446 | 3,213 | various | 40 |
| (2) (3) (4) | \$299,176 | \$1,773,607 | \$2,072,783 | \$332,406 | | |

The aggregate cost of the land, buildings, fixtures and equipment for federal tax purposes was approximately \$1,754 million at December 31, 2003.

- (1) As part of the formation transaction assets acquired for cash have been accounted for as a purchase. The step-up represents the amount of the purchase price that exceeds the net book value of the assets acquired.
- (2) Projects encumbered by mortgage totaling \$61.5 million at December 31, 2003.
- (3) Projects encumbered by mortgage totaling \$70.5 million at December 31, 2003.
- (4) Projects encumbered by mortgage totaling \$164.7 million at December 31, 2003.
- (5) Project held under long term land lease.
- (6) Purchase price has been tentatively allocated.
- (7) Projects encumbered by mortgage totaling \$63.5 million at December 31, 2003.
- (8) Projects encumbered by mortgage totaling \$25.5 million at December 31, 2003.

Chelsea Property Group, Inc.
Schedule III-Consolidated Real Estate
and Accumulated Depreciation (continued)
(in thousands)

The changes in total real estate:

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| | Year ended December 31, 2003 | 2002 |
|-----------------------------------|---------------------------------|-------------|
| | ----- | ----- |
| Balance, beginning of period..... | \$1,837,174 | \$1,127,906 |
| Additions..... | 268,318 | 719,857 |
| Dispositions and other..... | (32,709) | (10,589) |
| | ----- | ----- |
| Balance, end of period..... | \$2,072,783 | \$1,837,174 |
| | ===== | ===== |

The changes in accumulated depreciation:

| | Year ended December 31, 2003 | 2002 |
|--|---------------------------------|-----------|
| | ----- | ----- |
| Balance, beginning of period..... | \$284,239 | \$217,462 |
| Additions..... | 67,023 | 53,065 |
| Consolidation of properties previously held as investments in unconsolidated affiliates.. | - | 15,977 |
| Dispositions and other..... | (18,856) | (2,265) |
| | ----- | ----- |
| Balance, end of period..... | \$332,406 | \$284,239 |
| | ===== | ===== |

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized on the 26th of February 2004.

CHELSEA PROPERTY GROUP, INC.

By: /s/ David C. Bloom

David C. Bloom, Chief Executive Officer

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

| Signature ----- | Title ----- | Date ---- |
|---|--|-------------------|
| /s/ David C. Bloom ----- David C. Bloom | Chairman of the Board and Chief Executive Officer | February 26, 2004 |
| /s/ William D. Bloom ----- William D. Bloom | Vice Chairman | February 26, 2004 |
| /s/ Leslie T. Chao ----- Leslie T. Chao | President | February 26, 2004 |
| /s/ Michael J. Clarke | Chief Financial Officer and | February 26, 2004 |

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| | | |
|---|--------------------------|-------------------|
| ----- Michael J. Clarke | Chief Accounting Officer | |
| /s/ Brendan T. Byrne ----- Brendan T. Byrne | Director | February 26, 2004 |
| /s/ Robert Frommer ----- Robert Frommer | Director | February 26, 2004 |
| /s/ Barry M. Ginsburg ----- Barry M. Ginsburg | Director | February 26, 2004 |
| /s/ Philip D. Kaltenbacher ----- Philip D. Kaltenbacher | Director | February 26, 2004 |
| /s/ Reuben S. Leibowitz ----- Reuben S. Leibowitz | Director | February 26, 2004 |