

Extra Space Storage Inc.  
Form S-3ASR  
August 12, 2011

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As filed with the Securities and Exchange Commission on August 12, 2011

Registration No. 333-

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

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**Form S-3**

**REGISTRATION STATEMENT UNDER  
THE SECURITIES ACT OF 1933**

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**Extra Space Storage Inc.**

(Exact Name of Registrant as Specified in Its Charter)

**Maryland**

(State or Other Jurisdiction of  
Incorporation or Organization)

**20-1076777**

(I.R.S. Employer  
Identification Number)

**2795 East Cottonwood Parkway, Suite 400  
Salt Lake City, Utah 84121  
(801) 562-5556**

(Address, Including Zip Code, and Telephone Number, Including Area Code, of Registrant's Principal Executive Offices)

**Spencer F. Kirk**

**Chairman and Chief Executive Officer  
Extra Space Storage Inc.**

**2795 East Cottonwood Parkway, Suite 400  
Salt Lake City, Utah 84121  
(801) 562-5556**

(Name, Address, Including Zip Code, and Telephone Number, Including Area Code, of Agent for Service)

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Copy to:

**Craig M. Garner, Esq.  
Latham & Watkins LLP  
12636 High Bluff Drive, Suite 400  
San Diego, California 92130  
(858) 523-5400**

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## Approximate date of commencement of proposed sale to the public:

From time to time after the effective date of this Registration Statement, as determined by market conditions.

If the only securities being registered on this Form are being offered pursuant to dividend or interest reinvestment plans, please check the following box.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, other than securities offered only in connection with dividend or interest reinvestment plans, check the following box.

If this form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a registration statement pursuant to General Instruction I.D. or a post-effective amendment thereto that shall become effective upon filing with the Commission pursuant to Rule 462(e) under the Securities Act, check the following box.

If this Form is a post-effective amendment to a registration statement filed pursuant to General Instruction I.D. filed to register additional securities or additional classes of securities pursuant to Rule 413(b) under the Securities Act, check the following box.

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

Large accelerated filer 
                     Accelerated filer 
                     Non-accelerated filer 
                     Smaller reporting company

(Do not check if a smaller reporting company)

### CALCULATION OF REGISTRATION FEE

Title of Securities Being Registered(1)	Amount to be Registered	Proposed Maximum Offering Price Per Unit	Proposed Maximum Aggregate Offering Price	Amount of Registration Fee
Common Stock, Preferred Stock, Depositary Shares, Warrants, Rights and Units	(2)(3)	(2)(3)	(2)(3)	(4)

- (1) This registration statement also covers delayed delivery contracts that may be issued by the registrant under which the counterparty may be required to purchase common stock, preferred stock, depositary shares or warrants to purchase common stock, preferred stock or depositary shares. Such contracts may be issued together with the specific securities to which they relate. In addition, securities registered hereunder may be sold separately, together or as units with other securities registered hereunder.
- (2) Omitted pursuant to Form S-3 General Instruction II.E.
- (3) An unspecified number of the securities of each identified class of securities is being registered for possible issuance from time to time at indeterminate prices. Separate consideration may or may not be received for securities that are issuable on exercise, conversion or exchange of other securities or that are issued in units or represented by depositary shares. In accordance with Rules 456(b) and 457(r) under the Securities Act, we are deferring payment of all applicable registration fees.
- (4) Deferred in reliance upon Rules 456(b) and 457(r) under the Securities Act, except for \$1,018.48 that has already been paid with respect to securities that were previously registered by Extra Space Storage Inc. on Registration Statement No. 333-153081, filed on August 19, 2008, and were not sold thereunder. Pursuant to Rule 457(p), such unutilized filing fee may be applied to the filing fee payable pursuant to this registration statement.

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**PROSPECTUS**

## **Extra Space Storage Inc.**

**Common Stock  
Preferred Stock  
Depository Shares  
Warrants  
Rights  
Units**

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We may from time to time offer, in one or more classes or series, separately or together, and in amounts, at prices and on terms to be set forth in one or more supplements to this prospectus, the following securities:

shares of common stock;

shares of preferred stock;

depository shares representing entitlement to all rights and preferences of fractions of shares of preferred stock of a specified series and represented by depository receipts;

warrants to purchase preferred stock, common stock or depository shares;

rights to purchase shares of common stock; and

units consisting of two or more of the foregoing.

We refer to the common stock, preferred stock, depository shares, warrants, rights and units registered hereunder collectively as the "securities" in this prospectus.

The specific terms of each series or class of the securities will be set forth in the applicable prospectus supplement and will include, where applicable:

in the case of common stock, any public offering price;

in the case of preferred stock, the specific designation, preferences, conversion and other rights, voting powers, restrictions, limitations as to transferability, dividends and other distributions, qualifications and terms and conditions of redemption and any public offering price;

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in the case of depositary shares, the fractional share of preferred stock represented by each such depositary share;

in the case of warrants or rights, the duration, offering price, exercise price and detachability; and

in the case of units, the constituent securities comprising the units, the offering price and detachability.

In addition, the specific terms may include limitations on actual or constructive ownership and restrictions on transfer of the securities, in each case as may be appropriate to preserve the status of our company as a real estate investment trust, or REIT, for federal income tax purposes.

The applicable prospectus supplement will also contain information, where applicable, about certain United States federal income tax consequences relating to, and any listing on a securities exchange of, the securities covered by such prospectus supplement.

The securities may be offered directly by us or by any selling security holder, through agents designated from time to time by us or to or through underwriters or dealers. If any agents, dealers or underwriters are involved in the sale of any of the securities, their names, and any applicable purchase price, fee, commission or discount arrangement between or among them will be set forth, or will be calculable from the information set forth, in the applicable prospectus supplement. See the sections entitled "About This Prospectus" and "Plan of Distribution" for more information. No securities may be sold without delivery of this prospectus and the applicable prospectus supplement describing the method and terms of the offering of such series of securities.

Our common stock currently trades on the New York Stock Exchange under the symbol "EXR." On August 11, 2011, the last reported sale price of our common stock was \$20.02 per share.

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**You should consider the risks that we have described in "Risk Factors" on page 2 before investing in our securities.**

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**Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.**

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**The date of this prospectus is August 12, 2011**

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References in this prospectus to "Extra Space Storage Inc.," "Extra Space," "we," "our," "us" and "our company" refer to Extra Space Storage Inc., a Maryland corporation, Extra Space Storage LP, and any of our other subsidiaries. Extra Space Storage LP is a Delaware limited partnership of which we are the indirect general partner and to which we refer in this prospectus as our operating partnership. References to "OP units" include common operating partnership units and preferred operating partnership units.

You should rely only on the information contained in this prospectus, in an accompanying prospectus supplement or incorporated by reference herein or therein. We have not authorized anyone to provide you with information or make any representation that is different. If anyone provides you with different or inconsistent information, you should not rely on it. This prospectus and any accompanying prospectus supplement do not constitute an offer to sell or a solicitation of an offer to buy any securities other than the registered securities to which they relate, and this prospectus and any accompanying prospectus supplement do not constitute an offer to sell or the solicitation of an offer to buy securities in any jurisdiction where, or to any person to whom, it is unlawful to make such an offer or solicitation. You should not assume that the information contained in this prospectus and any accompanying prospectus supplement is correct on any date after the respective dates of the prospectus and such prospectus supplement or supplements, as applicable, even though this prospectus and such prospectus supplement or supplements are delivered or shares are sold pursuant to the prospectus and such prospectus supplement or supplements at a later date. Since the respective dates of the prospectus contained in this registration statement and any accompanying prospectus supplement, our business, financial condition, results of operations and prospects may have changed. We may only use this prospectus to sell the securities if it is accompanied by a prospectus supplement.

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**EXTRA SPACE STORAGE**

We are a fully integrated, self-administered and self-managed REIT focused on owning, operating, managing, acquiring, developing and redeveloping professionally managed self-storage facilities. We were formed as a Maryland corporation in April 2004 to continue the business of Extra Space Storage LLC and its subsidiaries, which had engaged in the self-storage business since 1977.

As of June 30, 2011, we held ownership interests in 680 operating properties. Of these operating properties, 325 are wholly owned and 355 are owned in joint venture partnerships. An additional 180 operating properties are owned by franchisees or third parties and operated by us in exchange for a management fee, bringing the total number of operating properties which we own and/or manage to 860. These operating properties are located in 34 states and Washington, D.C. and contain approximately 62 million square feet of net rentable space in approximately 570,000 units.

We operate in three distinct segments: (1) property management, acquisition and development; (2) rental operations; and (3) tenant reinsurance. Our property management, acquisition and development activities include managing, acquiring, developing and selling self-storage facilities. Our rental operations activities include rental operations of self-storage facilities. Tenant reinsurance activities include the reinsurance of risks relating to the loss of goods stored by tenants in our self storage facilities.

Our primary business objectives are to maximize cash flow available for distribution to our stockholders and to achieve sustainable long-term growth in cash flow per share in order to maximize long-term stockholder value. We seek to maximize revenue by responding to changing market conditions through our advanced technology system's ability to provide real-time, interactive rental rate and discount management. Our size allows us greater ability than many of our competitors to implement national, regional and local marketing programs, which we believe attracts more customers to our stores at a lower net cost. In addition, our management business enables us to generate increased revenues through management fees and to expand our geographic footprint. We believe this expanded footprint enables us to reduce our operating costs through economies of scale. We also continue to pursue the acquisition of single properties and multi-property portfolios that we believe can provide stockholder value.

Extra Space Storage LP and its subsidiaries conduct substantially all of our operations and hold all of our real estate assets. We believe our status as an umbrella partnership real estate investment trust, or UPREIT, enables flexibility when structuring transactions.

Our principal corporate offices are located at 2795 East Cottonwood Parkway, Suite 400, Salt Lake City, Utah 84121, and our telephone number is (801) 562-5556. We maintain a website that contains information about us at [www.extraspace.com](http://www.extraspace.com). The information included on our website is not, and should not be considered, a part of this prospectus or any accompanying prospectus supplement.

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**RISK FACTORS**

*Investment in any securities offered pursuant to this prospectus involves risks. You should carefully consider the risk factors incorporated by reference to our most recent Annual Report on Form 10-K and our subsequent Quarterly Reports on Form 10-Q and the other information contained in this prospectus, as updated by our subsequent filings under the Securities Exchange Act of 1934, as amended, or the Exchange Act, and the risk factors and other information contained in the applicable prospectus supplement before acquiring any of such securities. The occurrence of any of these risks might cause you to lose all or part of your investment in the offered securities. Please also refer to the section below entitled "Forward-Looking Statements."*

**ABOUT THIS PROSPECTUS**

This prospectus is part of an automatic shelf registration statement that we filed with the Securities and Exchange Commission as a "well-known seasoned issuer" as defined in Rule 405 under the Securities Act of 1933, as amended, or the Securities Act, using a "shelf" registration process. Under this process, we may sell common stock, preferred stock, depositary shares, warrants, rights and units in one or more offerings. In addition, selling security holders to be named in a prospectus supplement may sell certain of our securities from time to time. This prospectus provides you with a general description of the securities we or any selling security holder may offer. Each time we or any selling security holder sells securities, we or the selling security holder will provide a prospectus supplement containing specific information about the terms of the applicable offering. Such prospectus supplement may add, update or change information contained in this prospectus. You should read this prospectus and the applicable prospectus supplement together with additional information described below under the heading "Where You Can Find More Information."

We or any selling security holder may offer the securities directly, through agents, or to or through underwriters. The applicable prospectus supplement will describe the terms of the plan of distribution and set forth the names of any underwriters involved in the sale of the securities. See "Plan of Distribution" for more information on this topic. No securities may be sold without delivery of a prospectus supplement describing the method and terms of the offering of those securities.

**WHERE YOU CAN FIND MORE INFORMATION**

We file annual, quarterly and special reports, proxy statements and other information with the Securities and Exchange Commission. You may read and copy any document we file with the Securities and Exchange Commission at the public reference room of the Securities and Exchange Commission, 100 F Street, N.E., Washington, D.C. 20549. Information about the operation of the public reference room may be obtained by calling the Securities and Exchange Commission at 1-800-SEC-0330. Our Securities and Exchange Commission filings are also available to you on the Securities and Exchange Commission's website at [www.sec.gov](http://www.sec.gov). You can inspect reports and other information we file at the offices of the New York Stock Exchange, or NYSE, 20 Broad Street, New York, New York 10005. In addition, we maintain a website that contains information about us at [www.extraspace.com](http://www.extraspace.com). The information included on our website is not, and should not be considered, a part of this prospectus or any accompanying prospectus supplement.

We have filed with the Securities and Exchange Commission a registration statement on Form S-3, of which this prospectus is a part, including exhibits, schedules and amendments filed with, or incorporated by reference in, this registration statement, under the Securities Act with respect to the securities registered hereby. This prospectus and any accompanying prospectus supplement do not contain all of the information set forth in the registration statement and exhibits and schedules to the registration statement. For further information with respect to our company and the securities registered hereby, reference is made to the registration statement, including the exhibits to the

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registration statement. Statements contained in this prospectus and any accompanying prospectus supplement as to the contents of any contract or other document referred to in, or incorporated by reference in, this prospectus and any accompanying prospectus supplement are not necessarily complete and, where that contract is an exhibit to the registration statement, each statement is qualified in all respects by the exhibit to which the reference relates. Copies of the registration statement, including the exhibits and schedules to the registration statement, may be examined without charge at the public reference room of the Securities and Exchange Commission, 100 F Street, N.E., Washington, D.C. 20549. Information about the operation of the public reference room may be obtained by calling the Securities and Exchange Commission at 1-800-SEC-0330. The registration statement, of which this prospectus forms a part, is also available to you on the Securities and Exchange Commission's website at [www.sec.gov](http://www.sec.gov).

**INCORPORATION OF CERTAIN DOCUMENTS BY REFERENCE**

The Securities and Exchange Commission allows us to "incorporate by reference" the information we file with the Securities and Exchange Commission, which means that we can disclose important information to you by referring to those documents. The information incorporated by reference herein is an important part of this prospectus. The incorporated documents contain significant information about us, our business and our finances. Any information contained in this prospectus or in any document incorporated or deemed to be incorporated by reference in this prospectus will be deemed to have been modified or superseded to the extent that a statement contained in this prospectus, in any other document we subsequently file with the Securities and Exchange Commission that also is incorporated or deemed to be incorporated by reference in this prospectus or in any applicable prospectus supplement modifies or supersedes the original statement. Any statement so modified or superseded will not be deemed, except as so modified or superseded, to be a part of this prospectus. We incorporate by reference the following documents we filed with the Securities and Exchange Commission:

our Annual Report on Form 10-K for the year ended December 31, 2010;

our Quarterly Report on Form 10-Q for the quarter ended March 31, 2011;

our Quarterly Report on Form 10-Q for the quarter ended June 30, 2011;

our Current Report on Form 8-K filed on February 10, 2011;

our Current Report on Form 8-K filed on May 17, 2011;

our Current Report on Form 8-K filed on May 23, 2011;

our Current Report on Form 8-K filed on July 12, 2011; and

the description of our common stock contained in our registration statement on Form 8-A filed on August 4, 2004 (File No. 001-32269), including any amendments or reports filed for the purpose of updating this description.

All documents that we file with the Securities and Exchange Commission pursuant to Section 13(a), 13(c), 14 or 15(d) of the Exchange Act after the date of this prospectus and prior to the termination of the offering of any securities made under this prospectus (excluding any portions of such documents that are deemed "furnished" to the Securities and Exchange Commission pursuant to applicable rules and regulations) will also be considered to be incorporated by reference in this prospectus.

If you request, either orally or in writing, we will provide you with a copy of any or all documents that are incorporated by reference. Such documents will be provided to you free of charge, but will not contain any exhibits, unless those exhibits are incorporated by reference into the document. Requests should be addressed to Extra Space Storage Inc., 2795 East Cottonwood Parkway, Suite 400, Salt Lake City, Utah 84121,



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Attn: Investor Relations, telephone: (801) 562-5556.

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**FORWARD-LOOKING STATEMENTS**

This prospectus, any accompanying prospectus supplement and the documents that we incorporate by reference in each contain "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 (set forth in Section 27A of the Securities Act and Section 21E of the Exchange Act). Also, documents we subsequently file with the Securities and Exchange Commission and incorporate by reference will contain forward-looking statements. In particular, statements pertaining to our capital resources, portfolio performance and results of operations contain forward-looking statements. Likewise, our statements regarding anticipated growth in our funds from operations and anticipated market conditions, demographics and results of operations are forward-looking statements. Forward-looking statements involve numerous risks and uncertainties and you should not rely on them as predictions of future events. Forward-looking statements depend on assumptions, data or methods that may be incorrect or imprecise, and we may not be able to realize them. We do not guarantee that the transactions and events described will happen as described (or that they will happen at all). You can identify forward-looking statements by the use of forward-looking terminology such as "believes," "expects," "may," "will," "should," "seeks," "approximately," "intends," "plans," "estimates" or "anticipates" or the negative of these words and phrases or similar words or phrases. You can also identify forward-looking statements by discussions of strategy, plans or intentions. The following factors, among others, could cause actual results and future events to differ materially from those set forth or contemplated in the forward-looking statements:

changes in general economic conditions, the real estate industry and the markets in which we operate;

the effect of competition from new and existing self-storage facilities or other storage alternatives, which could cause rents and occupancy rates to decline;

difficulties in our ability to evaluate, finance, complete and integrate acquisitions and developments successfully and to lease up those properties, which could adversely affect our profitability;

potential liability for uninsured losses and environmental contamination;

the impact of the regulatory environment as well as national, state, and local laws and regulations including, without limitation, those governing REITs, which could increase our expenses and reduce our cash available for distribution;

disruptions in credit and financial markets and resulting difficulties in raising capital or obtaining credit at reasonable rates or at all, which could impede our ability to grow;

increased interest rates and operating costs;

reductions in asset valuations and related impairment charges;

the failure to maintain our REIT status for federal income tax purposes;

economic uncertainty due to the impact of war or terrorism, which could adversely affect our business plan; and

our ability to attract and retain qualified personnel and management members.

While forward-looking statements reflect our good faith beliefs, they are not guarantees of future performance. We disclaim any obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. For a further discussion of these and other factors that could impact our future results, performance or transactions, see the section above entitled "Risk Factors,"

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including the risks incorporated therein from our most recent Annual Report on Form 10-K and subsequent Quarterly Reports on Form 10-Q, as updated by our subsequent filings under the Exchange Act.

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**USE OF PROCEEDS**

Unless we indicate otherwise in the applicable prospectus supplement, we intend to contribute the net proceeds from any sale of the securities pursuant to this prospectus to our operating partnership in exchange for operating partnership units, which we refer to as OP units. Our operating partnership will subsequently use the net proceeds received from us to potentially acquire or develop additional properties and for general corporate purposes, which may include the repayment of existing indebtedness and improvements to the properties in our portfolio. Pending application of cash proceeds, we will invest the net proceeds in interest-bearing accounts and short-term, interest-bearing securities which are consistent with our intention to continue to qualify as a REIT for federal income tax purposes. Further details regarding the use of the net proceeds from the sale of a specific series or class of the securities will be set forth in the applicable prospectus supplement.

If a prospectus supplement includes an offering by selling security holders, we will not receive any proceeds from such sales.

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**RATIO OF EARNINGS TO FIXED CHARGES**

The following table sets forth ratios of earnings to fixed charges for the periods shown:

	<b>Six months ended</b>		<b>Year ended December 31,</b>			
	<b>June 30,</b>					
	<b>2011</b>	<b>2010</b>	<b>2009</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>
<b>Ratio of Earnings to Fixed Charges</b>	1.94	1.67	1.65	1.68	1.56	1.35

The ratios of earnings to fixed charges were computed by dividing earnings by fixed charges. For this purpose, earnings consist of income before extraordinary items and fixed charges included in expense. Fixed charges consist of interest costs, whether expensed or capitalized, and the amortization of debt issuance costs.

For the periods shown, we had neither issued any shares of, nor paid any dividends on, preferred stock. Accordingly, the ratios of earnings to fixed charges and preferred stock dividends are not presented because they are identical to the ratios of earnings to fixed charges for each of the periods.

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**DESCRIPTION OF COMMON STOCK**

**General**

This prospectus describes the general terms of our common stock. For a more detailed description of these securities, you should read the applicable provisions of the Maryland General Corporation Law, or MGCL, and our charter and bylaws. When we offer to sell a particular class or series of stock, we will describe the specific terms of the series in a prospectus supplement. Accordingly, for a description of the terms of any class or series of stock, you must refer to both the prospectus supplement relating to that class or series and the description of stock in this prospectus. To the extent the information contained in the prospectus supplement differs from this summary description, you should rely on the information in the prospectus supplement.

Our charter provides that we may issue up to 300,000,000 shares of our common stock, par value \$0.01 per share. Our charter authorizes our board of directors, with the approval of a majority of our board of directors and without stockholder approval, to amend our charter from time to time to increase or decrease the aggregate number of authorized shares of stock or the number of shares of any class or series. As of June 30, 2011, 94,243,303 shares of our common stock were issued and outstanding. Under Maryland law, stockholders generally are not liable for our debts or obligations.

All shares of our common stock offered hereby will be duly authorized, fully paid and nonassessable. Subject to the preferential rights of any other class or series of stock and to the provisions of our charter regarding the restrictions on ownership and transfer of stock, holders of shares of our common stock are entitled to receive dividends on such stock if, as and when authorized by our board of directors out of assets legally available therefor and declared by us and to share ratably in the assets of our company legally available for distribution to our stockholders in the event of our liquidation, dissolution or winding up after payment of or adequate provision for all known debts and liabilities of our company.

**Provisions of Our Charter**

Subject to the provisions of our charter regarding the restrictions on ownership and transfer of stock, and except as may otherwise be specified in the terms of any class or series of our common stock, each outstanding share of our common stock entitles the holder to one vote on all matters submitted to a vote of stockholders, including the election of directors and, except as provided with respect to any other class or series of stock, the holders of such shares will possess the exclusive voting power. There is no cumulative voting in the election of our board of directors, which means that the holders of a majority of the outstanding shares of our common stock can elect all of the directors then standing for election and the holders of the remaining shares will not be able to elect any directors.

Holders of shares of our common stock have no preference, conversion, exchange, sinking fund, redemption or appraisal rights and have no preemptive rights to subscribe for any of our securities. Subject to the provisions of our charter regarding the restrictions on ownership and transfer of stock, shares of our common stock will have equal dividend, liquidation and other rights.

Under the MGCL, a Maryland corporation generally cannot dissolve, amend its charter, merge, sell all or substantially all of its assets, engage in a statutory share exchange or engage in similar transactions outside the ordinary course of business unless declared advisable by our board of directors and approved by the affirmative vote of stockholders holding at least two-thirds of the shares entitled to vote on the matter, unless a lesser percentage (but not less than a majority of all of the votes entitled to be cast on the matter) is set forth in the corporation's charter. Except for certain charter amendments, our charter provides for a majority percentage in these situations. However, our operating assets may be held by our subsidiaries and these subsidiaries may be able to transfer all of their assets without any vote of our stockholders.

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Our charter authorizes our board of directors to reclassify any unissued shares of our common stock into other classes or series of stock, and to establish the number of shares in each class or series, and to set the preferences, conversion and other rights, voting powers, restrictions, limitations as to dividends or other distributions, qualifications and terms and conditions of redemption for each such class or series.

**Power to Increase Authorized Stock and Issue Additional Shares of Our Common Stock**

We believe that the power of our board of directors to amend our charter to increase the number of authorized shares of stock, to cause us to issue additional authorized but unissued shares of our common stock and to classify or reclassify unissued shares of our common stock and thereafter to cause us to issue such classified or reclassified shares of stock will provide us with increased flexibility in structuring possible future financings and acquisitions and in meeting other needs which might arise. The additional classes or series, as well as the common stock, will be available for issuance without further action by our stockholders, unless stockholder consent is required by applicable law or the rules of any stock exchange or automated quotation system on which our securities may be listed or traded. Although our board of directors does not currently intend to do so, it could authorize us to issue a class or series that could, depending upon the terms of the particular class or series, delay, defer or prevent a transaction or a change of control of our company that might involve a premium price for our stockholders or otherwise be in their best interest.

**Restrictions on Ownership and Transfer**

To assist us in complying with certain federal income tax requirements applicable to REITs, we have adopted certain restrictions relating to the ownership and transfer of our common stock. See "Restrictions on Ownership and Transfer."

**Transfer Agent and Registrar**

The transfer agent and registrar for our common stock is American Stock Transfer & Trust Company.

**DESCRIPTION OF PREFERRED STOCK**

**General**

This prospectus describes the general terms of our preferred stock. For a more detailed description of these securities, you should read the applicable provisions of the MGCL and our charter and bylaws. When we offer to sell a particular class or series of stock, we will describe the specific terms of the class or series in a prospectus supplement. Accordingly, for a description of the terms of any class or series of stock, you must refer to both the prospectus supplement relating to that class or series and the description of stock in this prospectus. To the extent the information contained in the prospectus supplement differs from this summary description, you should rely on the information in the prospectus supplement.

Our charter provides that we may issue up to 50,000,000 shares of preferred stock, par value \$0.01 per share. Our charter authorizes our board of directors to amend our charter from time to time to increase or decrease the number of authorized shares of any class or series without stockholder approval. As of June 30, 2011, no shares of preferred stock were issued and outstanding. Under Maryland law, stockholders generally are not liable for our debts or obligations.

Our charter authorizes our board of directors to classify any unissued shares of preferred stock and to reclassify any previously classified but unissued shares of any class or series. Prior to issuance of shares of each class or series, our board of directors is required by the MGCL and our charter to set

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the preferences, conversion or other rights, voting powers, restrictions, including without limitation, restrictions on transferability, limitations as to dividends or other distributions, qualifications and terms and conditions of redemption for each such class or series. The issuance of preferred stock could adversely affect the voting power, dividend rights and other rights of holders of our common stock. Our board of directors could authorize the issuance of shares of preferred stock with terms and conditions which could have the effect of delaying, deferring or preventing a transaction or a change of control of our company that might involve a premium price for holders of our stock or otherwise be in their best interest. Management believes that the availability of preferred stock provides the company with increased flexibility in structuring possible future financings and acquisitions and in meeting other needs that might arise.

The specific terms of a particular class or series of preferred stock will be described in the prospectus supplement relating to that class or series, including a prospectus supplement providing that preferred stock may be issuable upon the exercise of warrants we issue. The description of preferred stock set forth below and the description of the terms of a particular class or series of preferred stock set forth in the applicable prospectus supplement do not purport to be complete and are qualified in their entirety by reference to the articles supplementary relating to that class or series.

The preferences and other terms of the preferred stock of each class or series will be fixed by the articles supplementary relating to such class or series. A prospectus supplement, relating to each class or series, will specify the terms of the preferred stock as follows:

the title and stated value, if any, of the preferred stock;

the number of shares of the preferred stock, the liquidation preference per share of the preferred stock and the offering price of the preferred stock;

the dividend rate(s), period(s) and/or payment date(s) or method(s) of calculation thereof applicable to the preferred stock;

whether dividends on the preferred stock will be cumulative or not and, if cumulative, the date from which dividends on the preferred stock will accumulate;

the procedures for any auction and remarketing, if any, for the preferred stock;

the provision for a sinking fund, if any, for the preferred stock;

the provision for redemption, if applicable, of the preferred stock;

any listing of the preferred stock on any securities exchange;

preemptive rights, if any;

the terms and conditions, if applicable, upon which the preferred stock may or will be convertible into our common stock, including the conversion price or manner of calculation thereof;

the relative ranking and preferences of the preferred stock as to dividend rights and rights upon liquidation, dissolution or winding up of our affairs;



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any limitations on actual, beneficial or constructive ownership and restrictions on transfer, in each case as may be appropriate to preserve our status as a REIT;

a discussion of any material United States federal income tax considerations applicable to the ownership and disposition of the preferred stock;

any limitations on issuance of any class or series of preferred stock ranking senior to or on a parity with such class or series of preferred stock as to dividend rights and rights upon liquidation, dissolution or winding up of our affairs;

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any voting rights of the preferred stock; and

any other specific terms, preferences, rights, limitations or restrictions of the preferred stock.

### **Rank**

Unless otherwise specified in the applicable prospectus supplement, the preferred stock will, with respect to dividend rights and rights upon liquidation, dissolution or winding up of our company, rank:

- (1) senior to all classes or series of common stock and to all equity securities issued by us that are expressly designated as ranking junior to the preferred stock;
- (2) on a parity with all equity securities issued by us other than those referred to in clauses (1) and (3); and
- (3) junior to all equity securities issued by us that are expressly designated as ranking senior to the preferred stock.

### **Dividends**

Unless otherwise specified in the applicable prospectus supplement, the preferred stock will have the rights with respect to payment of dividends set forth below.

Holders of the preferred stock of each series will be entitled to receive, when, as and if authorized by our board of directors and declared by us, out of our assets legally available for payment, cash dividends in the amounts and on the dates as will be set forth in the applicable prospectus supplement. Each dividend shall be payable to holders of record as they appear on our stock transfer books on the record dates as shall be fixed by our board of directors.

Dividends on any series of preferred stock may be cumulative or non-cumulative, as provided in the applicable prospectus supplement. Dividends, if cumulative, will accumulate from and after the date set forth in the applicable prospectus supplement setting forth the terms of any series of preferred stock. If the board of directors fails to authorize, and we fail to declare, a dividend payable on a dividend payment date on any series of preferred stock for which dividends are non-cumulative, then the holders of this series of preferred stock will have no right to receive a dividend in respect of the related dividend period and we will have no obligation to pay the dividend accrued for the period, whether or not dividends on this series of preferred stock are declared payable on any future dividend payment date.

If shares of preferred stock of any series are outstanding, no full dividends will be declared and paid or declared and set apart for payment on any of our stock of any other series ranking, as to dividends, on a parity with or junior to the preferred stock of this series for any period unless:

if this series of preferred stock has a cumulative dividend, full cumulative dividends have been, or contemporaneously are, declared and paid or declared and a sum sufficient for the payment thereof set apart for the payment for all past dividend periods; or

if this series of preferred stock does not have a cumulative dividend, full dividends for the then current dividend period have been, or contemporaneously are, declared and paid or declared and a sum sufficient for the payment thereof set apart for the payment on the preferred stock of this series.

When dividends are not paid in full or a sum sufficient for the full payment is not so set apart upon preferred stock of any series and the shares of any other series of preferred stock ranking on a parity as to dividends with the preferred stock of this series, all dividends declared upon the preferred stock of this series and any other series of preferred stock ranking on a parity as to dividends with the preferred stock shall be declared pro rata so that the amount of dividends declared per share of



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preferred stock of this series and the other series of preferred stock shall in all cases bear to each other the same ratio that accrued dividends per share on the preferred stock of this series and the other series of preferred stock, which shall not include any accumulation in respect of unpaid dividends for prior dividend periods if the preferred stock does not have a cumulative dividend, bear to each other. No interest, or sum of money in lieu of interest, shall be payable in respect of any dividend payment or payments on preferred stock of this series which may be in arrears.

Except as provided in the immediately preceding paragraph, unless (1) if this series of preferred stock has a cumulative dividend, full cumulative dividends on the preferred stock of this series have been, or contemporaneously are, declared and paid or declared and a sum sufficient for the payment thereof set apart for payment for all past dividend periods, and (2) if this series of preferred stock does not have a cumulative dividend, full dividends on the preferred stock of this series have been, or contemporaneously are, declared and paid or declared and a sum sufficient for the payment thereof set apart for payment for the then current dividend period, no dividends, other than in shares of common stock or other stock ranking junior to the preferred stock of this series as to dividends and upon liquidation, shall be declared and paid or declared and set aside for payment or other distribution shall be declared and made upon the common stock, or any of our other stock ranking junior to or on a parity with the preferred stock of this series as to dividends or upon liquidation, dissolution or winding up, nor shall any shares of common stock, or any other of our capital stock ranking junior to or on a parity with the preferred stock of this series as to dividends or upon liquidation, be redeemed, purchased or otherwise acquired for any consideration or any moneys be paid to or made available for a sinking fund for the redemption of any of the shares by us except:

by conversion into or exchange for other shares of our stock ranking junior to the preferred stock of this series as to dividends and upon liquidation, dissolution or winding up; or

redemptions for the purpose of preserving our qualification as a REIT.

Any dividend payment made on shares of a series of preferred stock shall first be credited against the earliest accrued but unpaid dividend due with respect to shares of that series which remains payable.

**Redemption**

If so provided in the applicable prospectus supplement, the preferred stock will be subject to mandatory redemption or redemption at our option, as a whole or in part, in each case upon the terms, at the times and at the redemption prices set forth in the prospectus supplement.

The prospectus supplement relating to a series of preferred stock that is subject to mandatory redemption will specify the number of shares of the preferred stock that shall be redeemed by us in each year commencing after a date to be specified, at a redemption price per share to be specified, together with an amount equal to all accrued and unpaid dividends thereon which shall not, if the preferred stock does not have a cumulative dividend, include any accumulation in respect of unpaid dividends for prior dividend periods, to the date of redemption. The redemption price may be payable in cash or other property, as specified in the applicable prospectus supplement. If the redemption price for preferred stock of any series is payable only from the net proceeds of the issuance of our stock, the terms of that preferred stock may provide that, if no such stock shall have been issued or to the extent the net proceeds from any issuance are insufficient to pay in full the aggregate redemption price then due, that preferred stock shall automatically and mandatorily be converted into shares of our applicable stock pursuant to conversion provisions specified in the applicable prospectus supplement.

Notwithstanding the foregoing, unless (1) if this series of preferred stock has a cumulative dividend, full cumulative dividends on all shares of any series of preferred stock shall have been, or contemporaneously are, declared and paid or declared and a sum sufficient for the payment thereof set

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apart for payment for all past dividend periods, and (2) if this series of preferred stock does not have a cumulative dividend, full dividends on the preferred stock of any series have been, or contemporaneously are, declared and paid or declared and a sum sufficient for the payment thereof set apart for payment for the then current dividend period, no shares of any series of preferred stock shall be redeemed unless all outstanding preferred stock of this series is simultaneously redeemed; provided, however, that the foregoing shall not prevent the purchase or acquisition of preferred stock of this series to preserve our REIT qualification or pursuant to a purchase or exchange offer made on the same terms to holders of all outstanding preferred stock of this series. In addition, unless (a) if this series of preferred stock has a cumulative dividend, full cumulative dividends on all outstanding shares of any series of preferred stock have been, or contemporaneously are, declared and paid or declared and a sum sufficient for the payment thereof set apart for payment for all past dividend periods, and (b) if this series of preferred stock does not have a cumulative dividend, full dividends on the preferred stock of any series have been, or contemporaneously are, declared and paid or declared and a sum sufficient for the payment thereof set apart for payment for the then current dividend period, we shall not purchase or otherwise acquire, directly or indirectly, any shares of preferred stock of this series except by conversion into, or exchange for, our capital stock ranking junior to the preferred stock of this series as to dividends and upon liquidation; provided, however, that the foregoing shall not prevent the purchase or acquisition of preferred stock of this series to preserve our REIT qualification or pursuant to a purchase or exchange offer made on the same terms to holders of all outstanding preferred stock of this series.

If fewer than all of the outstanding shares of preferred stock of any series are to be redeemed, the number of shares to be redeemed will be determined by us and the shares may be redeemed pro rata from the holders of record of the shares in proportion to the number of the shares held, or for which redemption is requested, by the holder, with adjustments to avoid redemption of fractional shares, or by lot in a manner determined by us.

Notice of redemption will be mailed at least 30 days but not more than 60 days before the redemption date to each holder of record of preferred stock of any series to be redeemed at the address shown on our stock transfer books. Each notice shall state:

the redemption date;

the number of shares and series of the preferred stock to be redeemed;

the redemption price;

the place or places where certificates, if any, for the preferred stock are to be surrendered for payment of the redemption price;

that dividends on the shares to be redeemed will cease to accumulate on the redemption date; and

the date upon which the holder's conversion rights, if any, as to the shares shall terminate.

If fewer than all the shares of preferred stock of any series are to be redeemed, the notice mailed to each holder thereof shall also specify the number of shares of preferred stock to be redeemed from each holder. If notice of redemption of any preferred stock has been given and if the funds necessary for the redemption have been set aside by us in trust for the benefit of the holders of any preferred stock so called for redemption, then from and after the redemption date dividends will cease to accumulate on the preferred stock, and all rights of the holders of the preferred stock will terminate, except the right to receive the redemption price.

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**Liquidation Preference**

Upon any voluntary or involuntary liquidation, dissolution or winding up of our affairs, then, before any distribution or payment shall be made to the holders of any common stock or any other class or series of our stock ranking junior to the preferred stock of this series in the distribution of assets upon any liquidation, dissolution or winding up of our company, the holders of the preferred stock shall be entitled to receive out of our company's assets legally available for distribution to stockholders liquidating distributions in the amount of the liquidation preference per share that is set forth in the applicable prospectus supplement, plus an amount equal to all dividends accumulated and unpaid thereon, which shall not include any accumulation in respect of unpaid dividends for prior dividend periods if the preferred stock does not have a cumulative dividend. After payment of the full amount of the liquidating distributions to which they are entitled, the holders of preferred stock will have no rights or claim to any of our remaining assets. In the event that, upon any voluntary or involuntary liquidation, dissolution or winding up, our available assets are insufficient to pay the amount of the liquidating distributions on all outstanding preferred stock of this series and the corresponding amounts payable on all shares of other classes or series of capital stock of our company ranking on a parity with the preferred stock in the distribution of assets, then the holders of the preferred stock and all other classes or series of capital stock shall share ratably in any distribution of assets in proportion to the full liquidating distributions to which they would otherwise be respectively entitled.

Our consolidation or merger with or into any other entity, or the merger of another entity with or into our company, or a statutory share exchange by us, or the sale, lease or conveyance of all or substantially all of our property or business, shall not be deemed to constitute a liquidation, dissolution or winding up of our company.

In determining whether a distribution (other than upon voluntary or involuntary liquidation), by dividend, redemption or other acquisition of shares of our stock or otherwise, is permitted under Maryland law, amounts that would be needed, if we were to be dissolved at the time of distribution, to satisfy the preferential rights upon dissolution of holders of shares of the preferred stock will not be added to our total liabilities.

**Voting**

Holders of the preferred stock will not have any voting rights, except as set forth below or as indicated in the applicable prospectus supplement.

Whenever dividends on any series of preferred stock shall be in arrears for six or more quarterly periods, the holders of the preferred stock, voting separately as a class with all other series of preferred stock upon which like voting rights have been conferred and are exercisable, will be entitled to vote for the election of two additional directors of our company at a special meeting called by the holders of record of at least ten percent of any series of preferred stock so in arrears, unless the request is received less than 90 days before the date fixed for the next annual or special meeting of the stockholders, or at the next annual meeting of stockholders, and at each subsequent annual meeting until (1) if this series of preferred stock has a cumulative dividend, all dividends accumulated on these shares of preferred stock for the past dividend periods shall have been fully paid or declared and a sum sufficient for the payment thereof set aside for payment or (2) if this series of preferred stock does not have a cumulative dividend, four quarterly dividends shall have been fully paid or declared and a sum sufficient for the payment thereof set aside for payment. In these cases, the entire board of directors will be increased by two directors.

Unless provided otherwise for any series of preferred stock, so long as any shares of the preferred stock remain outstanding, we will not, without the affirmative vote or consent of the holders of at least

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two-thirds of the shares of this series of preferred stock outstanding at the time, given in person or by proxy, either in writing or at a meeting with this series voting separately as a class:

- (1) authorize or create, or increase the number of authorized or issued shares of, any class or series of stock ranking senior to the preferred stock with respect to payment of dividends or the distribution of assets upon liquidation, dissolution or winding up of our company, or reclassify any of our authorized stock into this series of preferred stock, or create, authorize or issue any obligation or security convertible into or evidencing the right to purchase any of this series of preferred stock; or
- (2) amend, alter or repeal the provisions of the charter or the articles supplementary for this series of preferred stock, whether by merger, consolidation or otherwise, so as to materially and adversely affect any right, preference, privilege or voting power of this series of preferred stock;

provided, however, with respect to the occurrence of any of the events set forth in (2) above, so long as this series of preferred stock remains outstanding with the terms thereof materially unchanged, taking into account that upon the occurrence of an event we may not be the surviving entity, the occurrence of any similar event shall not be deemed to materially and adversely affect the rights, preferences, privileges or voting powers of this series of preferred stock; and provided, further, that (a) any increase in the number of authorized shares of preferred stock or the creation or issuance of any other series of preferred stock, or (b) any increase in the number of authorized shares of this series of preferred stock or any other series of preferred stock, in each case ranking on a parity with or junior to the preferred stock of this series with respect to payment of dividends or the distribution of assets upon liquidation, dissolution or winding up of our company, shall not be deemed to materially and adversely affect the rights, preferences, privileges or voting powers.

The foregoing voting provisions will not apply if, at or prior to the time when the act with respect to which the vote or consent would otherwise be required shall be effected, all outstanding shares of this series of preferred stock shall have been converted, redeemed or called for redemption and sufficient funds shall have been deposited in trust to effect the redemption.

**Conversion Rights**

The terms and conditions, if any, upon which any shares of any class or series of preferred stock are convertible into shares of common stock will be set forth in the applicable prospectus supplement. The terms will include the number of shares of common stock into which the shares of preferred stock are convertible, the conversion price, or manner of calculation thereof, the conversion period, provisions as to whether conversion will be at the option of the holders of such class or series of preferred stock or us, the events requiring an adjustment of the conversion price and provisions affecting conversion in the event of the redemption of such class or series of preferred stock.

**Power to Increase Authorized Stock and Issue Additional Shares of Our Preferred Stock**

Our board of directors has the power, without stockholder approval, to amend our charter from time to time to increase the number of authorized shares of stock, to cause us to issue additional authorized but unissued shares of our preferred stock and to classify or reclassify unissued shares of our preferred stock and thereafter to cause us to issue such classified or reclassified shares of stock. The additional classes or series will be available for issuance without further action by our stockholders, unless stockholder consent is required by applicable law or the rules of any stock exchange or automated quotation system on which our securities may be listed or traded. Although our board of directors does not currently intend to do so, it could authorize us to issue a class or series that could, depending upon the terms of the particular class or series, delay, defer or prevent a transaction or a change of control of our company that might involve a premium price for our stockholders or otherwise be in their best interest.

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**Restrictions on Ownership and Transfer**

To assist us in complying with certain United States federal income tax requirements applicable to REITs, we have adopted certain restrictions relating to the ownership and transfer of our common stock. We expect to adopt similar restrictions with respect to any class or series of preferred stock offered pursuant to this prospectus under the articles supplementary for each such class or series. The applicable prospectus supplement will specify any additional ownership limitation relating to such class or series. See "Restrictions on Ownership and Transfer."

**DESCRIPTION OF DEPOSITARY SHARES**

We may, at our option, elect to offer depositary shares rather than full shares of preferred stock. Each depositary share will represent ownership of and entitlement to all rights and preferences of a fraction of a share of preferred stock of a specified series (including dividend, voting, redemption and liquidation rights). The applicable fraction will be specified in a prospectus supplement. The shares of preferred stock represented by the depositary shares will be deposited with a depositary named in the applicable prospectus supplement, under a deposit agreement, among us, the depositary and the holders of the certificates evidencing depositary shares, or depositary receipts. Depositary receipts will be delivered to those persons purchasing depositary shares in the offering. The depositary will be the transfer agent, registrar and dividend disbursing agent for the depositary shares. Holders of depositary receipts agree to be bound by the deposit agreement, which requires holders to take certain actions such as filing proof of residence and paying certain charges.

The summary of the terms of the depositary shares contained in this prospectus does not purport to be complete and is subject to, and qualified in its entirety by, the provisions of the deposit agreement, our charter and the form of articles supplementary for the applicable class or series of preferred stock.

**Dividends**

The depositary will distribute all cash dividends or other cash distributions received in respect of the series of preferred stock represented by the depositary shares to the record holders of depositary receipts in proportion to the number of depositary shares owned by such holders on the relevant record date, which will be the same date as the record date fixed by us for the applicable series of preferred stock. The depositary, however, will distribute only such amount as can be distributed without attributing to any depositary share a fraction of one cent, and any balance not so distributed will be added to and treated as part of the next sum received by the depositary for distribution to record holders of depositary receipts then outstanding.

In the event of a distribution other than in cash, the depositary will distribute property received by it to the record holders of depositary receipts entitled thereto, in proportion, as nearly as may be practicable, to the number of depositary shares owned by such holders on the relevant record date, unless the depositary determines (after consultation with us) that it is not feasible to make such distribution, in which case the depositary may (with our approval) adopt any other method for such distribution as it deems equitable and appropriate, including the sale of such property (at such place or places and upon such terms as it may deem equitable and appropriate) and distribution of the net proceeds from such sale to such holders.

Any distribution made in respect of any depositary share to the extent that it represents any preferred stock transferred to a trust for the purpose of preserving our qualification as a REIT will be paid to the trustee of the trust for the exclusive benefit of a charitable beneficiary designated by us.



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**Liquidation Preference**

In the event of the liquidation, dissolution or winding up of the affairs of our company, whether voluntary or involuntary, the holders of each depositary share will be entitled to the fraction of the liquidation preference accorded each share of the applicable series of preferred stock as set forth in the applicable prospectus supplement.

**Conversion**

The depositary shares generally will not be convertible into our common stock or any of our other securities or property, except in connection with certain conversions to preserve our status as a REIT. Nevertheless, if so specified in the applicable prospectus supplement relating to an offering of depositary shares, the depositary receipts may be surrendered by holders thereof to the preferred stock depositary with written instructions to the preferred stock depositary to instruct us to cause conversion of a class or series of preferred stock represented by the depositary shares evidenced by those depositary receipts into whole shares of our common stock, other shares of a class or series of preferred stock or other shares of stock, and we have agreed that upon receipt of those instructions and any amounts payable in respect thereof, we will cause the conversion thereof utilizing the same procedures as those provided for delivery of preferred stock to effect that conversion. If the depositary shares evidenced by a depositary receipt are to be converted in part only, a new depositary receipt or receipts will be issued for any depositary shares not to be converted. No fractional shares of common stock will be issued upon conversion, and if that conversion would result in a fractional share being issued, an amount will be paid in cash by us equal to the value of the fractional interest based upon the closing price of the common stock on the last business day prior to the conversion.

**Redemption**

If the series of preferred stock represented by the applicable series of depositary shares is redeemable, such depositary shares will be redeemed from the proceeds received by the depositary resulting from the redemption, in whole or in part, of preferred stock held by the depositary. Whenever we redeem any preferred stock held by the depositary, the depositary will redeem as of the same redemption date the number of depositary shares representing the preferred stock so redeemed. The depositary will mail the notice of redemption promptly upon receipt of such notice from us and not less than 30 nor more than 60 days prior to the date fixed for redemption of the preferred stock and the depositary shares to the record holders of the depositary receipts.

**Voting**

Promptly upon receipt of notice of any meeting at which the holders of the series of preferred stock represented by the applicable series of depositary shares are entitled to vote, the depositary will mail the information contained in such notice of meeting to the record holders of the depositary receipts as of the record date for such meeting. Each such record holder of depositary receipts will be entitled to instruct the depositary as to the exercise of the voting rights pertaining to the number of shares of preferred stock represented by such record holder's depositary shares. The depositary will endeavor, insofar as practicable, to vote such preferred stock represented by such depositary shares in accordance with such instructions, and we will agree to take all action which may be deemed necessary by the depositary in order to enable the depositary to do so. The depositary will abstain from voting any of the preferred stock to the extent that it does not receive specific instructions from the holders of depositary receipts.

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**Withdrawal of Preferred Stock**

Upon surrender of depositary receipts at the principal office of the depositary and payment of any unpaid amount due the depositary, and subject to the terms of the deposit agreement, the owner of the depositary shares evidenced thereby is entitled to delivery of the number of whole shares of preferred stock and all money and other property, if any, represented by such depositary shares. Partial shares of preferred stock will not be issued. If the depositary receipts delivered by the holder evidence a number of depositary shares in excess of the number of depositary shares representing the number of whole shares of preferred stock to be withdrawn, the depositary will deliver to such holder at the same time a new depositary receipt evidencing such excess number of depositary shares. Holders of preferred stock thus withdrawn will not thereafter be entitled to deposit such shares under the deposit agreement or to receive depositary receipts evidencing depositary shares therefor.

**Amendment and Termination of Deposit Agreement**

The form of depositary receipt evidencing the depositary shares and any provision of the deposit agreement may at any time and from time to time be amended by agreement between us and the depositary. However, any amendment which materially and adversely alters the rights of the holders (other than any change in fees) of depositary shares will not be effective unless such amendment has been approved by at least a majority of the depositary shares then outstanding. No such amendment may impair the right, subject to the terms of the deposit agreement, of any owner of any depositary shares to surrender the depositary receipt evidencing such depositary shares with instructions to the depositary to deliver to the holder of the preferred stock and all money and other property, if any, represented thereby, except in order to comply with mandatory provisions of applicable law.

The deposit agreement will be permitted to be terminated by us upon not less than 30 days' prior written notice to the applicable depositary if (1) such termination is necessary to preserve our status as a REIT or (2) a majority of each series of preferred stock affected by such termination consents to such termination, whereupon such depositary will be required to deliver or make available to each holder of depositary receipts, upon surrender of the depositary receipts held by such holder, such number of whole or fractional shares of preferred stock as are represented by the depositary shares evidenced by such depositary receipts together with any other property held by such depositary with respect to such depositary receipts. We will agree that if the deposit agreement is terminated to preserve our status as a REIT, then we will use our best efforts to list the preferred stock issued upon surrender of the related depositary shares on a national securities exchange. In addition, the deposit agreement will automatically terminate if (a) all outstanding depositary shares thereunder shall have been redeemed, (b) there shall have been a final distribution in respect of the related preferred stock in connection with any liquidation, dissolution or winding-up of our company and such distribution shall have been distributed to the holders of depositary receipts evidencing the depositary shares representing such preferred stock or (c) each share of the related preferred stock shall have been converted into stock of our company not so represented by depositary shares.

**Charges of Depositary**

We will pay all transfer and other taxes and governmental charges arising solely from the existence of the depositary arrangements. We will pay charges of the depositary in connection with the initial deposit of the preferred stock and initial issuance of the depositary shares, and redemption of the preferred stock and all withdrawals of preferred stock by owners of depositary shares. Holders of depositary receipts will pay transfer, income and other taxes and governmental charges and certain other charges as are provided in the deposit agreement for their accounts. In certain circumstances, the depositary may refuse to transfer depositary shares, may withhold dividends and distributions and sell the depositary shares evidenced by such depositary receipt if such charges are not paid. The applicable prospectus supplement will include information with respect to fees and charges, if any, in connection

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with the deposit or substitution of the underlying securities, the receipt and distribution of dividends, the sale or exercise of rights, the withdrawal of the underlying security, and the transferring, splitting or grouping of receipts. The applicable prospectus supplement will also include information with respect to the right to collect the fees and charges, if any, against dividends received and deposited securities.

**Miscellaneous**

The depositary will forward to the holders of depositary receipts all notices, reports and proxy soliciting material from us which are delivered to the depositary and which we are required to furnish to the holders of the preferred stock. In addition, the depositary will make available for inspection by holders of depositary receipts at the principal office of the depositary, and at such other places as it may from time to time deem advisable, any notices, reports and proxy soliciting material received from us which are received by the depositary as the holder of preferred stock. The applicable prospectus supplement will include information about the rights, if any, of holders of receipts to inspect the transfer books of the depositary and the list of holders of receipts.

Neither the depositary nor our company assumes any obligation, or will be subject to any liability under the deposit agreement, to holders of depositary receipts other than for its negligence or willful misconduct. Neither the depositary nor our company will be liable if it is prevented or delayed by law or any circumstance beyond its control in performing its obligations under the deposit agreement. The obligations of our company and the depositary under the deposit agreement will be limited to performance in good faith of their duties thereunder, and they will not be obligated to prosecute or defend any legal proceeding in respect of any depositary shares or preferred stock unless satisfactory indemnity is furnished. Our company and the depositary may rely on written advice of counsel or accountants, on information provided by holders of the depositary receipts or other persons believed in good faith to be competent to give such information and on documents believed to be genuine and to have been signed or presented by the proper party or parties.

In the event the depositary shall receive conflicting claims, requests or instructions from any holders of depositary receipts, on the one hand, and us, on the other hand, the depositary shall be entitled to act on such claims, requests or instructions received from us.

**Resignation and Removal of Depositary**

The depositary may resign at any time by delivering to us notice of its election to do so, and we may at any time remove the depositary, any such resignation or removal to take effect upon the appointment of a successor depositary and its acceptance of such appointment. Such successor depositary must be appointed within 60 days after delivery of the notice for resignation or removal and must be a bank or trust company having its principal office in the United States and having a combined capital and surplus of at least \$150,000,000.

**DESCRIPTION OF WARRANTS**

We may issue warrants for the purchase of common stock, preferred stock or depositary shares and may issue warrants independently or together with common stock, preferred stock or depositary shares or attached to or separate from such securities. We will issue each series of warrants under a separate warrant agreement between us and a bank or trust company as warrant agent, as specified in the applicable prospectus supplement.

The warrant agent will act solely as our agent in connection with the warrants and will not act for or on behalf of warrant holders. The following sets forth certain general terms and provisions of the warrants that may be offered under this registration statement. Further terms of the warrants and the applicable warrant agreement will be set forth in the applicable prospectus supplement. To the extent

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information contained in the applicable prospectus supplement differs from this summary description, you should rely on the information in the prospectus supplement.

The applicable prospectus supplement will describe the terms of the warrants in respect of which this prospectus is being delivered, including, where applicable, the following:

the title of the warrants;

the aggregate number of the warrants;

the price or prices at which the warrants will be issued;

the type and number of securities purchasable upon exercise of the warrants;

the designation and terms of the other securities, if any, with which the warrants are issued and the number of the warrants issued with each such offered security;

the date, if any, on and after which the warrants and related securities will be separately transferable;

the price at which each security purchasable upon exercise of the warrants may be purchased;

the provisions, if any, for changes to or adjustments in the exercise price;

the date on which the right to exercise the warrants shall commence and the date on which such right shall expire;

the minimum or maximum amount of the warrants that may be exercised at any one time;

information with respect to book-entry procedures, if any;

any anti-dilution protection;

a discussion of any material United States federal income tax considerations applicable to the warrants; and

any other terms of the warrants, including terms, procedures and limitations relating to the transferability, exercise and exchange of such warrants.

Warrant certificates will be exchangeable for new warrant certificates of different denominations and warrants may be exercised at the corporate trust office of the warrant agent or any other office indicated in the applicable prospectus supplement. Prior to the exercise of their warrants, holders of warrants will not have any of the rights of holders of the securities purchasable upon such exercise or to any dividend payments or voting rights as to which holders of the depositary shares, shares of common stock or shares of preferred stock purchasable upon

such exercise may be entitled.

**Exercise of Warrants**

Each warrant will entitle the holder to purchase for cash such number of depositary shares, shares of common stock or shares of preferred stock, at such exercise price as shall, in each case, be set forth in, or be determinable as set forth in, the applicable prospectus supplement relating to the warrants offered thereby. Unless otherwise specified in the applicable prospectus supplement, warrants may be exercised at any time up to 5:00 p.m. New York City time on the expiration date set forth in applicable prospectus supplement. After 5:00 p.m. New York City time on the expiration date, unexercised warrants will be void.

Warrants may be exercised as set forth in the applicable prospectus supplement relating to the warrants. Upon receipt of payment and the warrant certificate properly completed and duly executed at the corporate trust office of the warrant agent or any other office indicated in the applicable prospectus supplement, we will, as soon as practicable, forward the securities purchasable upon such exercise. If

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less than all of the warrants are presented by such warrant certificate of exercise, a new warrant certificate will be issued for the remaining amount of warrants.

**DESCRIPTION OF RIGHTS**

We may issue rights to our stockholders for the purchase of shares of our common stock. Each series of rights will be issued under a separate rights agreement to be entered into between us and a bank or trust company, as rights agent, all as set forth in the applicable prospectus supplement relating to the particular issue of rights. The rights agent will act solely as our agent in connection with the certificates relating to the rights of such series and will not assume any obligation or relationship of agency or trust for or with any holders of rights certificates or beneficial owners of rights. The statements made in this section relating to the rights are summaries only. These summaries are not complete. To the extent information contained in the applicable prospectus supplement differs from this summary description, you should rely on the information in the prospectus supplement. For more detail, we refer you to the rights agreement and the rights certificates relating to each series of rights, which will be filed with the Securities and Exchange Commission as an exhibit to, or incorporated by reference in, the registration statement of which this prospectus is a part.

The applicable prospectus supplement will describe the terms of the rights to be issued, including the following, where applicable:

the date for determining the stockholders entitled to the rights distribution;

the aggregate number of shares of common stock purchasable upon exercise of the rights;

the exercise price;

the provisions, if any, for changes to or adjustments in the exercise price;

the aggregate number of rights issued;

the date, if any, on and after which the rights will be separately transferable;

the date on which the right to exercise the rights will commence, and the date on which the right will expire;

a discussion of any material United States federal income tax considerations applicable to an investment in the rights; and

any other terms of the rights, including terms, procedures and limitations relating to the distribution, exchange and exercise of the rights.

**Exercise of Rights**

Each right will entitle the holder of rights to purchase for cash the principal amount of shares of common stock at the exercise price provided in the applicable prospectus supplement. Rights may be exercised at any time up to the close of business on the expiration date for the rights provided in the applicable prospectus supplement. After the close of business on the expiration date, all unexercised rights will be void.

Holders may exercise rights as described in the applicable prospectus supplement. Upon receipt of payment and the rights certificate properly completed and duly executed at the corporate trust office of the rights agent or any other office indicated in the prospectus supplement,

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we will, as soon as practicable, forward the shares of common stock purchasable upon exercise of the rights. If less than all of the rights issued in any rights offering are exercised, we may offer any unsubscribed securities directly to persons other than stockholders, to or through agents, underwriters or dealers or through a

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combination of such methods, including pursuant to standby underwriting arrangements, as described in the applicable prospectus supplement.

**DESCRIPTION OF UNITS**

We may issue units consisting of two or more other constituent securities. These units may be issuable, and for a specified period of time may be transferable, only as a single security, rather than as the separate constituent securities comprising such units. The statements made in this section relating to the units are summaries only. These summaries are not complete. When we issue units, we will provide the specific terms of the units in a prospectus supplement. To the extent the information contained in the prospectus supplement differs from this summary description, you should rely on the information in the prospectus supplement.

When we issue units, we will provide in a prospectus supplement the following terms of the units being issued:

the title of any series of units;

identification and description of the separate constituent securities comprising the units;

the price or prices at which the units will be issued;

the date, if any, on and after which the constituent securities comprising the units will be separately transferable;

information with respect to any book-entry procedures;

a discussion of any material United States federal income tax considerations applicable to an investment in the units; and

any other terms of the units and their constituent securities.



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**RESTRICTIONS ON OWNERSHIP AND TRANSFER**

*The following is a summary of the general terms and provisions of our charter documents regarding restrictions on the ownership and transfer of our stock. This summary does not purport to be complete and is subject to and qualified in its entirety by reference to our charter. Copies of our charter documents are filed with the Securities and Exchange Commission and are incorporated by reference herein. See "Where You Can Find More Information" and "Incorporation of Certain Documents by Reference."*

To qualify as a REIT under the Internal Revenue Code of 1986, as amended, or the Code, our stock must be beneficially owned by 100 or more persons during at least 335 days of a taxable year of twelve months (other than the first year for which an election to be a REIT has been made) or during a proportionate part of a shorter taxable year. Also, not more than 50% of the value of our outstanding shares of stock may be owned, directly or indirectly, by five or fewer individuals (as defined in the Code to include certain entities such as qualified pension plans) during the last half of a taxable year (other than the first year for which an election to be a REIT has been made).

Our charter contains restrictions on the ownership and transfer of our common stock and outstanding capital stock which are intended to assist us in complying with these requirements and continuing to qualify as a REIT, among other purposes. The relevant sections of our charter provide that, subject to the exceptions described below, no person or entity (other than a designated investment entity) may beneficially own, or be deemed to own by virtue of the applicable constructive ownership provisions of the Code, more than 7.0% (by value or by number of shares, whichever is more restrictive) of our outstanding common stock (the common stock ownership limit) or 7.0% (by value or by number of shares, whichever is more restrictive) of our outstanding capital stock (the aggregate stock ownership limit). No designated investment entity (as defined in our charter) may beneficially own, or be deemed to own by virtue of the applicable constructive ownership provisions of the Code, more than 9.8% (by value or by number of shares, whichever is more restrictive) of our outstanding common stock or 9.8% (by value or by number of shares, whichever is more restrictive) of our outstanding capital stock. We refer to these restrictions as the "ownership limits." In addition, different excepted holder ownership limits apply to the family of Kenneth M. Woolley, a director and our former Chairman and Chief Executive Officer, certain of his affiliates, family members and estates and trusts formed for the benefit of the foregoing and Spencer F. Kirk, our current Chairman and Chief Executive Officer, certain of his affiliates, family members and estates and trusts formed for the benefit of the foregoing. A person or entity that becomes subject to the ownership limit by virtue of a violative transfer that results in a transfer to a trust, as set forth below, is referred to as a "purported beneficial transferee" if, had the violative transfer been effective, the person or entity would have been a record owner and beneficial owner or solely a beneficial owner of our common stock, or is referred to as a "purported record transferee" if, had the violative transfer been effective, the person or entity would have been solely a record owner of our common stock.

Our charter defines a "designated investment entity" as:

an entity that is a pension trust that qualifies for look-through treatment under Section 856(h) of the Code;

an entity that qualifies as a regulated investment company under Section 851 of the Code; or

an entity that (a) for compensation engages in the business of advising others as to the value of securities or as to the advisability of investing in, purchasing, or selling securities; (b) purchases securities in the ordinary course of its business and not with the purpose or effect of changing or influencing control of us, nor in connection with or as a participant in any transaction having such purpose or effect, including any transaction subject to Rule 13d-3(b) of the Exchange Act; and (c) has or shares voting power and investment power within the meaning of Rule 13d-3(a) under the Exchange Act, so long as such beneficial owner of such entity, or in the case of an

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investment management company, the individual account holders of the accounts managed by such entity, would satisfy the 7.0% ownership limit if such beneficial owner or account holder owned directly its proportionate share of the shares held by the entity.

The constructive ownership rules under the Code are complex and may cause stock owned actually or constructively by a group of related individuals and/or entities to be owned constructively by one individual or entity. As a result, the acquisition of less than 7.0% (by value or by number of shares, whichever is more restrictive) of our outstanding common stock or 7.0% (by value or by number of shares, whichever is more restrictive) of our outstanding capital stock (or the acquisition of an interest in an entity that owns, actually or constructively, our capital stock by an individual or entity), could, nevertheless, cause that individual or entity, or another individual or entity, to own constructively in excess of 7.0% (by value or by number of shares, whichever is more restrictive) of our outstanding common stock or 7.0% (by value or by number of shares, whichever is more restrictive) of our outstanding capital stock, and thereby violate one or more of the applicable ownership limits.

Our board of directors may, in its sole discretion, waive the applicable ownership limit with respect to a particular stockholder if:

our board of directors obtains such representations and undertakings from such stockholder as are reasonably necessary to ascertain that no individual's beneficial or constructive ownership of our stock will result in our being "closely held" under Section 856(h) of the Code or that any exemption from the ownership limit will not jeopardize our status as a REIT;

our board of directors determines that such stockholder does not own, and will not own, actually or constructively, an interest in a tenant of ours (or a tenant of any entity owned in whole or in part by us) that would cause us to own, actually or constructively, more than a 9.9% interest (as set forth in Section 856(d)(2)(B) of the Code) in such tenant (or our board of directors determines that revenue derived from such tenant will not affect our ability to qualify as a REIT) and our board of directors obtains such representations and undertakings from such stockholder as are reasonably necessary to ascertain this fact; and

such stockholder agrees that any violation or attempted violation of such representations or undertakings, or other action which is contrary to the restrictions described herein, will result in such shares of stock being automatically transferred to a charitable trust.

As a condition of our waiver, our board of directors may require an opinion of counsel or an Internal Revenue Service, or IRS, ruling satisfactory to our board of directors with respect to our REIT qualification. Notwithstanding the receipt of any such opinion or ruling, our board of directors may impose such conditions or restrictions as it deems appropriate in connection with granting such waiver.

In connection with the waiver of an ownership limit or at any other time, our board of directors may from time to time increase or decrease the ownership limit for all other persons and entities; provided, however, that any decrease may be made only prospectively as to subsequent holders (other than a decrease as a result of a retroactive change in existing law, in which case the decrease shall be effective immediately); and the ownership limit may not be increased if, after giving effect to such increase, five persons (other than a designated investment entity) could beneficially own or constructively own in the aggregate, more than 49.9% of the value of our shares then outstanding. A reduced ownership limit will not apply to any person or entity whose percentage ownership in our common stock or capital stock, as applicable, is in excess of such decreased ownership limit until such time as such person or entity's percentage of our common stock or our capital stock, as applicable, equals or falls below the decreased ownership limit, but any further acquisition of our common stock or capital stock, as applicable, in excess of such percentage ownership of our common stock or capital stock will be in violation of the ownership limit.

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Our charter provisions further prohibit:

any person from beneficially or constructively owning shares of our stock that would result in our being "closely held" under Section 856(h) of the Code or otherwise cause us to fail to qualify as a REIT; and

any person from transferring shares of our common stock if such transfer would result in shares of our common stock being beneficially owned by fewer than 100 persons (determined without reference to any rules of attribution).

Any person who acquires or attempts to acquire beneficial or constructive ownership of shares of our capital stock that will, or may, violate any of the foregoing restrictions on transferability and ownership, will be required to give written notice immediately to us and provide us with such other information as we may request in order to determine the effect of such transfer or attempted transfer on our qualification as a REIT. The foregoing provisions on transferability and ownership will not apply if our board of directors determines that it is no longer in our best interests to attempt to qualify, or to continue to qualify, as a REIT.

Pursuant to our charter, if any transfer of common stock would result in such shares being beneficially owned by fewer than 100 persons, such transfer will be null and void and the intended transferee will acquire no rights in such shares. In addition, if any purported transfer of our capital stock, or any other event would otherwise result in any person violating the ownership limits, or such other limit as established by our board of directors, or in our being "closely held" under Section 856(h) of the Code, or otherwise failing to qualify as a REIT, then that number of shares (rounded up to the nearest whole share) that would cause us to violate such restrictions will be automatically transferred to, and held by, a trust for the exclusive benefit of one or more charitable organizations selected by us and the intended transferees will acquire no rights in such shares. The trustee of the trust will have all of the voting rights and rights to dividends or other distributions with respect to shares held in the trust. These rights will be exercised for the exclusive benefit of the charitable beneficiary. The automatic transfer will be effective as of the close of business on the business day prior to the date of the violative transfer or other event that results in a transfer to the trust. Any dividend or other distribution paid to the purported record transferee, prior to our discovery that the shares had been automatically transferred to a trust as described above, must be repaid to the trustee upon demand for distribution to the beneficiary of the trust. If the transfer to the trust as described above is not automatically effective, for any reason, to prevent the violation, then our charter provides that the transfer of the shares will be null and void and the intended transferees will acquire no rights in such shares.

Shares of our capital stock transferred to the trustee are deemed offered for sale to us, or our designee, at a price per share equal to the lesser of (1) the price paid by the purported record transferee for the shares (or, if the event which resulted in the transfer to the trust did not involve a purchase of such shares of our stock at market price, the last reported sales price on the trading day immediately preceding the day of the event which resulted in the transfer of such shares of our stock to the trust) and (2) the market price on the date we accept, or our designee accepts, such offer. We have the right to accept such offer until the trustee has sold the shares of our capital stock held in the trust pursuant to the clauses discussed below. Upon a sale to us, the interest of the charitable beneficiary in the shares sold terminates and the trustee must distribute the net proceeds of the sale to the purported record transferee and any dividends or other distributions held by the trustee with respect to such capital stock will be paid to the charitable beneficiary.

If we do not buy the shares, the trustee must, within 20 days of receiving notice from us of the transfer of shares to the trust, sell the shares to a person or entity designated by the trustee who could own the shares without violating the ownership limits. After that, the trustee must distribute to the purported record transferee an amount equal to the lesser of (1) the price paid by the purported

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record transferee for the shares (or, if the event which resulted in the transfer to the trust did not involve a purchase of such shares at market price, the last reported sales price reported on the trading day immediately preceding the relevant date) and (2) the sales proceeds (net of commissions and other expenses of sale) received by the trust for the shares. The purported beneficial transferee or purported record transferee has no rights in the shares held by the trustee.

The trustee shall be designated by us and shall be unaffiliated with us and with any purported record transferee or purported beneficial transferee. Prior to the sale of any shares by the trust, the trustee will receive, in trust for the beneficiary, all dividends and other distributions paid by us with respect to the shares, and may also exercise all voting rights with respect to the shares.

Subject to Maryland law, effective as of the date that the shares have been transferred to the trust, the trustee shall have the authority, at the trustee's sole discretion:

to rescind as void any vote cast by a purported record transferee prior to our discovery that the shares have been transferred to the trust; and

to recast such vote in accordance with the desires of the trustee acting for the benefit of the beneficiary of the trust.

However, if we have already taken irreversible corporate action, then the trustee may not rescind and recast the vote.

Any beneficial owner or constructive owner of shares of our capital stock and any person or entity (including the stockholder of record) who is holding shares of our capital stock for a beneficial owner must, within 30 days after the end of each taxable year, provide us with a completed questionnaire containing the information regarding their ownership of such shares, as set forth in the applicable Treasury regulations. In addition, any person or entity that is a beneficial owner or constructive owner of shares of our capital stock and any person or entity (including the stockholder of record) who is holding shares of our capital stock for a beneficial owner or constructive owner shall, on request, be required to disclose to us in writing such information as we may request in order to determine the effect, if any, of such stockholder's actual and constructive ownership of shares of our capital stock on our qualification as a REIT and to ensure compliance with the ownership limit, or as otherwise permitted by our board of directors.

All certificates, if any, representing shares of our capital stock bear a legend referring to the restrictions described above.

These ownership limits could delay, defer or prevent a transaction or a change of control of our company that might involve a premium price for our stock or otherwise be in the best interests of our stockholders.

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**DESCRIPTION OF THE  
PARTNERSHIP AGREEMENT OF EXTRA SPACE STORAGE LP**

*The following is a summary of the material provisions in the partnership agreement of our operating partnership. For more detail, you should refer to the partnership agreement itself, a copy of which is filed as an exhibit to the registration statement of which this prospectus is a part. See "Where You Can Find More Information." For purposes of this section, references to "we," "our," "us," and "our company" refer to Extra Space Storage Inc.*

**General; Management**

Our operating partnership was formed on May 5, 2004. As of June 30, 2011, our operating partnership had outstanding 97,293,238 common OP units and 989,980 Series A Participating Redeemable Preferred Units, which we refer to as preferred OP units. Of the common OP units, we hold 94,243,303 through two wholly owned Massachusetts business trusts, one of which is the sole general partner of the operating partnership and the other is a limited partner. The remaining 3,049,935 common OP units are held by other limited partners. Pursuant to the partnership agreement, through our ownership of the operating partnership's sole general partner, we have, subject to certain protective rights of limited partners described below, full, exclusive and complete responsibility and discretion in the management and control of the operating partnership, including the ability to cause the operating partnership to enter into certain major transactions, including a merger of the operating partnership or a sale of substantially all of its assets.

Our operating partnership's limited partners expressly acknowledged that, as the sole owner of the general partner interests through a wholly owned Massachusetts business trust, we are acting for the benefit of the operating partnership, the limited partners and our stockholders collectively. We are under no obligation to give priority to the separate interests of the limited partners or our stockholders in deciding whether to cause the operating partnership to take, or decline to take, any actions.

**Management Liability and Indemnification**

The general partner and its trustees and officers are not liable to the operating partnership for losses sustained, liabilities incurred or benefits not derived as a result of errors in judgment or mistakes of fact or law or of any act or omission, so long as it acted in good faith. The partnership agreement provides for indemnification of us, any of our directors, and both our operating partnership's and our officers or employees and other persons as our operating partnership may designate from and against all losses, claims, damages, liabilities, expenses, fines, settlements and other amounts incurred in connection with any actions relating to our operating partnership's operations, as set forth in the partnership agreement (subject to the exceptions described below under "Fiduciary Responsibilities").

**Fiduciary Responsibilities**

Our directors and officers have duties under applicable Maryland law to manage our company in a manner reasonably believed to be in the best interests of our company. At the same time, our operating partnership's general partner has fiduciary duties to manage our operating partnership in a manner beneficial to the operating partnership and its limited partners. Our duties, through the general partner, to our operating partnership and its limited partners, therefore, may come into conflict with the duties of our directors and officers to our company.

The partnership agreement expressly limits our liability and that of the general partner by providing that we and our officers and directors and the general partner and its officers and trustees are not liable or accountable in damages to the operating partnership, its limited partners or assignees for errors in judgment or mistakes of fact or law or of any act or omission if we or our director or officer acted in good faith. In addition, our operating partnership is required to indemnify us, the

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general partner, a trustee of the general partner, our directors, officers and employees and the directors, officers and employees of our operating partnership to the maximum extent permitted by applicable law, against any and all losses, claims, damages, liabilities, expenses, judgments, fines and other actions incurred by our operating partnership or the other persons in connection with any actions relating to our operating partnership's operations, provided that our operating partnership will not indemnify for willful misconduct or a knowing violation of the law or any transaction for which the person received an improper personal benefit in violation or breach of any provision of the partnership agreement.

**Distributions**

The partnership agreement provides that holders of OP units are entitled to receive quarterly distributions of available cash (1) first, to holders of preferred OP units (a) pro rata in proportion to their respective percentage interests, an amount equal to a fixed priority return of 5.0% on a stated amount of \$115.0 million, and (b) the distributions that holders of preferred OP units would be entitled to receive if the preferred OP units were treated as part of a single class of units with common OP units and the preferred OP units shared in distribution with the common OP units pursuant to clause (3) below proportionately based on the total aggregate number of outstanding preferred OP units and common OP units, (2) second, with respect to any OP units that are entitled to any preference, other than the preferred OP units, with their respective percentage interests and (3) third, with respect to any OP units that are not entitled to any preference in distribution, in accordance with the rights of such class of OP unit (and, within such class, pro rata in accordance with their respective percentage interests).

**Allocations of Net Income and Net Loss**

Net income and net loss of our operating partnership are determined and allocated with respect to each fiscal year of our operating partnership as of the end of the year. Except as otherwise provided in the partnership agreement, an allocation of a share of net income or net loss is treated as an allocation of the same share of each item of income, gain, loss or deduction that is taken into account in computing net income or net loss. Except as otherwise provided in the partnership agreement, (1) net income generally is allocated first to the partners to the extent they have been allocated net loss previously, then to partners holding preferred OP units until such partners have been allocated net income equal to their preferred return, and finally to partners holding common OP units pro rata in accordance with such partners' percentage interests; and (2) net loss generally is allocated in the reverse order of net income, but only to the extent such allocation of net loss will not cause a partner to have an adjusted capital account deficit or increase any existing adjusted capital account deficit, with any residual net loss being allocated to us as the general partner of our operating partnership. The partnership agreement contains provisions for special allocations intended to comply with certain regulatory requirements, including the requirements of Treasury Regulations Sections 1.704-1(b) and 1.704-2. Except as otherwise provided in the partnership agreement, for U.S. federal income tax purposes under the Code and the Treasury Regulations, each operating partnership item of income, gain, loss and deduction is allocated among the operating partnership's limited partners in the same manner as its correlative item of book income, gain, loss or deduction is allocated pursuant to the partnership agreement.

**Redemption Rights**

After the first anniversary of becoming a holder of common OP units, each of the limited partners of our operating partnership has the right, subject to the terms and conditions set forth in the partnership agreement, to require our operating partnership to redeem all or a portion of the common OP units held by the party in exchange for a cash amount equal to the value of its common OP units,

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unless the terms of such common OP units or a separate agreement entered into between our operating partnership and the holder of such OP units provide that they are not entitled to a right of redemption. On or before the close of business on the tenth business day after our operating partnership receives a notice of redemption, we may, in our sole and absolute discretion, but subject to the restrictions on the ownership of our common stock imposed under our charter and the transfer restrictions and other limitations thereof, elect to acquire some or all of the tendered common OP units from the tendering party in exchange for shares of our common stock, based on an exchange ratio of one share of our common stock for each common OP unit (subject to antidilution adjustments provided in the partnership agreement).

Each holder of preferred OP units has the right, subject to the terms and conditions set forth in the partnership agreement or in any separate agreement that provides otherwise, to require our operating partnership to redeem all or a portion of its preferred OP units in exchange for a cash amount equal to, per preferred OP unit, the sum of (1) \$115.0 million divided by the total number of preferred OP units outstanding, (2) any unpaid distributions with respect to such preferred OP unit and (3) the average closing price of our common stock on the NYSE for the ten consecutive trading days prior to the date of determination, multiplied by a factor that is adjusted for stock dividends, splits (reverse or otherwise) or subdivisions, which sum we refer to as the preferred OP unit redemption amount. We may, in our sole and absolute discretion, but subject to the restrictions on the ownership of our common stock imposed under our charter and the transfer restrictions and other limitations thereof, elect to acquire some or all of the tendered preferred OP units from the tendering party in exchange for the number of shares of our common stock equal to the preferred OP unit redemption amount divided by the average closing price of our common stock on the NYSE for the ten consecutive trading days prior to the date of determination. Pursuant to a separate agreement with the holders of our preferred OP units, a maximum of 116.0 million shares of our common stock may be issued upon redemption of the preferred OP units, after which we will have no further obligations with respect to the redeemed or any other remaining preferred OP units.

**Transferability of OP Units**

In general, the general partner may not voluntarily withdraw from our operating partnership or transfer all or a portion of its interest in our operating partnership unless the holders of limited partnership interests entitled to vote consent by approval of a majority in interest or immediately after a merger of us into another entity. With certain limited exceptions, the limited partners may not transfer their interests, in whole or in part, without the written consent of the general partner, which consent may be withheld in the general partner's sole discretion.

**Issuance of OP Units or Our Stock**

We, through our ownership of our operating partnership's sole general partner, have the ability to cause our operating partnership to issue additional partnership interests in the form of OP units. These additional OP units may include preference terms with provisions and rights that are preferential to those of common OP units. However, so long as the preferred OP units remain issued and outstanding, our operating partnership may not (1) (a) authorize or issue any securities, (b) reclassify any OP units into interests or (c) authorize or issue any debt convertible into or exchangeable for OP units, in each case having any preference as to or on parity with the dividend or redemption rights, liquidation preferences, conversion rights, voting rights or any other rights or privileges of the preferred OP units, or (2) amend or repeal any provision of, or add any provision to the partnership agreement if such actions would alter or change the preferences, rights, privileges or restrictions provided for the benefit of the preferred OP units.

In addition, upon the issuance of our stock other than in connection with a redemption of OP units, we will generally be obligated to contribute or cause to be contributed the cash proceeds or

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other consideration received from the issuance to our operating partnership in exchange for, in the case of common stock, OP units, or in the case of an issuance of preferred stock, preferred OP units with designations, preferences and other rights, terms and provisions that are substantially the same as the designations, preferences and other rights, terms and provisions of the preferred stock.

**Tax Matters**

Pursuant to the partnership agreement, the general partner is the operating partnership's tax matters partner. Accordingly, through its role as the general partner, it has the authority to handle or cause to be handled tax audits and to make or cause to be made tax elections under the Code on the operating partnership's behalf.

**Term**

The term of the operating partnership commenced on May 5, 2004 and will continue until December 31, 2104, unless one of the following events takes place:

the general partner's bankruptcy, judicial dissolution or withdrawal (unless, in the case of a withdrawal, a majority-in-interest of the remaining limited partners agree to continue the partnership and to the appointment of a successor general partner);

the sale or other disposition of all or substantially all of the operating partnership's assets;

redemption (or acquisition by us) of all OP units other than OP units held by the general partner; or

an election by the general partner in its capacity as the operating partnership's sole general partner.

Upon the occurrence of any of the foregoing events, and subject to the terms of the partnership agreement, after any appropriate allocation of net income and net loss, distributions to the partners of our operating partnership will be made first to the holders of preferred OP units (and proportionately among those holders) in an amount equal to the preferred OP unit redemption amount for each preferred OP unit, and thereafter to the holders of other OP units. However, the voluntary sale, conveyance, lease, exchange or transfer (for cash, shares of stock, securities or other consideration) of all or substantially all of the property or assets of the operating partnership to, or the consolidation or merger or other business combination of the operating partnership with or into, any corporation, trust or other entity (or of any corporation, trust or other entity with or into the operating partnership) will not be deemed to constitute a liquidation, dissolution or winding-up of the operating partnership for these purposes.



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**CERTAIN PROVISIONS OF MARYLAND LAW AND OF OUR CHARTER AND BYLAWS**

*The following summary of certain provisions of Maryland law and of our charter and bylaws is subject to and qualified in its entirety by reference to Maryland law and our charter and bylaws, copies of which are filed as exhibits to the registration statement of which this prospectus is a part. See "Where You Can Find More Information."*

**Our Board of Directors**

Our bylaws provide that the number of directors of our company may be established by our board of directors but may not be fewer than the minimum number permitted under the MGCL nor more than 15. Except as may be provided by our board of directors in setting the terms of any class or series of preferred stock, any vacancy may be filled, at any regular meeting or at any special meeting called for that purpose, only by a majority of the remaining directors, even if the remaining directors do not constitute a quorum, and the director elected to fill the vacancy will serve for the remainder of the full directorship in which the vacancy occurred and until a successor is elected and qualifies.

Each of our directors is elected by our common stockholders entitled to vote to serve until the next annual meeting and until their successors are duly elected and qualify. Holders of shares of our common stock will have no right to cumulative voting in the election of directors. Consequently, at each annual meeting of stockholders, the holders of a majority of the shares of our common stock entitled to vote will be able to elect all of our directors (subject to the rights of our preferred stock and any other class or series of stock to elect directors).

**Removal of Directors**

Our charter provides that, subject to the rights of holders of one or more classes or series of preferred stock to elect or remove one or more directors, a director may be removed only for cause (as defined in our charter) and only by the affirmative vote of at least two-thirds of the votes of stockholders entitled to be cast generally in the election of directors. This provision, when coupled with the exclusive power of our board of directors to fill vacant directorships, precludes stockholders from removing incumbent directors except upon the existence of cause for removal and a substantial affirmative vote, and filling the vacancies created by such removal with their own nominees.

**Business Combinations**

Under the MGCL, certain "business combinations" (including a merger, consolidation, statutory share exchange or, in certain circumstances, an asset transfer or issuance or reclassification of equity securities) between a Maryland corporation and an interested stockholder (i.e., any person who beneficially owns 10% or more of the voting power of the corporation's outstanding voting stock or an affiliate or associate of the corporation who, at any time within the two-year period immediately prior to the date in question, was the beneficial owner of 10% or more of the voting power of the then outstanding stock of the corporation) or an affiliate of such an interested stockholder are prohibited for five years after the most recent date on which the interested stockholder becomes an interested stockholder. Thereafter, any such business combination must be recommended by the board of directors of such corporation and approved by the affirmative vote of at least (1) 80% of the votes entitled to be cast by holders of outstanding shares of voting stock of the corporation and (2) two-thirds of the votes entitled to be cast by holders of voting stock of the corporation other than shares held by the interested stockholder with whom (or with whose affiliate) the business combination is to be effected or held by an affiliate or associate of the interested stockholder, unless, among other conditions, the corporation's common stockholders receive a minimum price (as defined in the MGCL) for their shares and the consideration is received in cash or in the same form as previously paid by the interested stockholder for its shares. A person is not an interested stockholder under the statute if the

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board of directors approved in advance the transaction by which the person otherwise would have become an interested stockholder. Our board of directors may provide that its approval is subject to compliance with any terms and conditions determined by it.

These provisions of the MGCL do not apply, however, to business combinations that are approved or exempted by a board of directors prior to the time that the interested stockholder becomes an interested stockholder. Pursuant to the statute, our board of directors has by resolution exempted Kenneth M. Woolley, his affiliates and associates and all persons acting in concert with the foregoing, and Spencer F. Kirk, his affiliates and associates and all persons acting in concert with the foregoing, from these provisions of the MGCL and, consequently, the five-year prohibition and the supermajority vote requirements will not apply to business combinations between us and any person described above. As a result, any person described above may be able to enter into business combinations with us that may not be in the best interests of our stockholders without compliance by our company with the supermajority vote requirements and the other provisions of the statute.

**Control Share Acquisitions**

The MGCL provides that holders of "control shares" of a Maryland corporation acquired in a "control share acquisition" have no voting rights with respect to the control shares except to the extent approved at a special meeting by the affirmative vote of two-thirds of the votes entitled to be cast on the matter, excluding shares of stock in a corporation in respect of which any of the following persons is entitled to exercise or direct the exercise of the voting power of shares of stock of the corporation in the election of directors: (1) a person who makes or proposes to make a control share acquisition, (2) an officer of the corporation or (3) an employee of the corporation who is also a director of the corporation. "Control shares" are voting shares of stock which, if aggregated with all other such shares of stock owned by the acquirer or in respect of which the acquirer is able to exercise or direct the exercise of voting power (except solely by virtue of a revocable proxy), would entitle the acquirer to exercise voting power in electing directors within one of the following ranges of voting power: (a) one-tenth or more but less than one-third, (b) one-third or more but less than a majority, or (c) a majority or more of all voting power. Control shares do not include shares the acquiring person is then entitled to vote as a result of having previously obtained stockholder approval. A "control share acquisition" means the acquisition of issued and outstanding control shares, subject to certain exceptions.

A person who has made, or proposes to make, a control share acquisition, upon satisfaction of certain conditions (including an undertaking to pay expenses), may compel our board of directors to call a special meeting of stockholders to be held within 50 days of demand and undertaking to pay expenses to consider the voting rights of the shares. If no request for a meeting is made, the corporation may itself present the question at any stockholders meeting.

If voting rights are not approved at the meeting or if the acquiring person does not deliver an acquiring person statement as required by the statute, then, subject to certain conditions and limitations, the corporation may redeem any or all of the control shares (except those for which voting rights have previously been approved) for fair value determined, without regard to the absence of voting rights for the control shares, as of the date of the last control share acquisition by the acquirer or of any meeting of stockholders at which the voting rights of such shares are considered and not approved. If voting rights for control shares are approved at a stockholders meeting and the acquirer becomes entitled to vote a majority of the shares entitled to vote, all other stockholders may exercise appraisal rights. The fair value of the shares as determined for purposes of such appraisal rights may not be less than the highest price per share paid by the acquirer in the control share acquisition.

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The control share acquisition statute does not apply (1) to shares acquired in a merger, consolidation or statutory share exchange if the corporation is a party to the transaction or (2) to acquisitions approved or exempted by the charter or bylaws of the corporation.

Our bylaws contain a provision exempting from the control share acquisition statute any and all acquisitions by any person of our stock. There can be no assurance that such provision will not be amended or eliminated at any time in the future.

**Other Anti-Takeover Provisions of Maryland Law**

Subtitle 8 of Title 3 of the MGCL permits a Maryland corporation with a class of equity securities registered under the Exchange Act and with at least three independent directors to elect to be subject by provision in its charter or bylaws or a resolution of its board of directors and notwithstanding any contrary provision in the charter or bylaws, to any or all of five provisions:

a classified board;

a two-thirds vote requirement to remove a director;

a requirement that the number of directors be fixed only by the vote of the directors;

a requirement that a vacancy on the board be filled only by the remaining directors and for the remainder of the full term of class of directors in which the vacancy occurred and until a successor is elected and qualifies; and

a majority requirement for the calling of a special meeting of stockholders.

Pursuant to Subtitle 8, we have elected to provide that vacancies on our board be filled only by the remaining directors and for the remainder of the full term of the directorship in which the vacancy occurred. Through provisions in our charter and bylaws unrelated to Subtitle 8, we already (1) require the affirmative vote of the holders of not less than two-thirds of all of the votes entitled to be cast on the matter for the removal of any director from the board, which removal is only allowed for cause, (2) vest in the board the exclusive power to fix the number of directorships and (3) require the request of stockholders entitled to cast not less than a majority of all votes entitled to be cast at such meeting to call a special meeting of our stockholders, unless such meeting is called by our chairman of the board, our president, our chief executive officer or the board.

**Amendment to Our Charter and Bylaws**

Except for amendments relating to removal of directors and the restrictions on ownership and transfer of our stock and amendments relating to the vote required to amend these provisions (which each require the affirmative vote of the holders of not less than two-thirds of all the votes entitled to be cast on the matter), our charter may be amended only if declared advisable by our board of directors and approved by the affirmative vote of the holders of not less than a majority of all of the votes entitled to be cast on the matter.

Our board of directors has the exclusive power to adopt, alter or repeal any provision of our bylaws and to make new bylaws.

**Dissolution of Our Company**

The dissolution of our company must be declared advisable by a majority of our entire board of directors and approved by the affirmative vote of the holders of not less than a majority of all of the votes entitled to be cast on the matter.

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**Advance Notice of Director Nominations and New Business**

Our bylaws provide that with respect to an annual meeting of stockholders, nominations of individuals for election to our board of directors and the proposal of business to be considered by stockholders may be made only (1) pursuant to our notice of the meeting, (2) by or at the direction of our board of directors or (3) by a stockholder who was a stockholder of record both at the time of giving of notice and at the time of the annual meeting, who is entitled to vote at the meeting and has complied with the advance notice procedures set forth in our bylaws.

With respect to special meetings of stockholders, only the business specified in our notice of meeting may be brought before the meeting. Nominations of individuals for election to our board of directors may be made only (1) pursuant to our notice of the meeting, (2) by or at the direction of our board of directors or (3) provided that our board of directors has determined that directors shall be elected at such meeting, by a stockholder who was a stockholder of record both at the time of giving of notice and at the time of the special meeting, who is entitled to vote at the meeting and has complied with the advance notice provisions set forth in our bylaws.

Generally, under our bylaws, a stockholder seeking to nominate a director or bring other business before our annual meeting of stockholders must deliver a notice to our secretary not later than the close of business on the 120<sup>th</sup> day, nor earlier than the 150<sup>th</sup> day, prior to the first anniversary of the date of the proxy statement for the prior year's annual meeting. In addition, a stockholder seeking to nominate a director at a special meeting of stockholders must deliver notice to our secretary not earlier than the 150<sup>th</sup> day prior to such special meeting nor later than the later of the 120<sup>th</sup> day prior to such special meeting or the tenth day following the day on which public announcement is first made of the date of the special meeting and of the nominees proposed by our board of directors to be elected at such meeting. For a stockholder seeking to nominate a candidate for our board of directors, the notice must describe various matters regarding the nominee, including name, address, occupation and number of shares held, and other specified matters. For a stockholder seeking to propose other business, the notice must include a description of the proposed business, the reasons for the proposal and other specified matters.

**Anti-Takeover Effect of Certain Provisions of Maryland Law and of Our Charter and Bylaws**

Our charter and bylaws and Maryland law contain provisions that may delay, defer or prevent a change of control or other transaction that might involve a premium price for our stock or otherwise be in the best interests of our stockholders, including business combination provisions, supermajority vote and cause requirements for removal of directors and advance notice requirements for director nominations and stockholder proposals. Likewise, if the provision in the bylaws opting out of the control share acquisition provisions of the MGCL were rescinded, these provisions of the MGCL could have similar anti-takeover effects.

**Indemnification and Limitation of Directors' and Officers' Liability**

Maryland law permits a Maryland corporation to include in its charter a provision limiting the liability of its directors and officers to the corporation and its stockholders for money damages except for liability resulting from (1) actual receipt of an improper benefit or profit in money, property or services or (2) active and deliberate dishonesty established by a final judgment and which is material to the cause of action. Our charter contains such a provision which eliminates such liability to the maximum extent permitted by Maryland law.

The MGCL requires a corporation (unless its charter provides otherwise, which our company's charter does not) to indemnify a director or officer who has been successful, on the merits or otherwise, in the defense of any proceeding to which he or she is made, or threatened to be made, a party by reason of his or her service in that capacity. The MGCL permits a corporation to indemnify its

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present and former directors and officers, among others, against judgments, penalties, fines, settlements and reasonable expenses actually incurred by them in connection with any proceeding to which they may be made, or threatened to be made, a party by reason of their service in those or other capacities unless it is established that:

the act or omission of the director or officer was material to the matter giving rise to the proceeding and (1) was committed in bad faith or (2) was the result of active and deliberate dishonesty;

the director or officer actually received an improper personal benefit in money, property or services; or

in the case of any criminal proceeding, the director or officer had reasonable cause to believe that the act or omission was unlawful.

However, under the MGCL, a Maryland corporation may not indemnify for an adverse judgment in a suit by or in the right of the corporation or for a judgment of liability on the basis that personal benefit was improperly received, unless in either case a court orders indemnification and then only for expenses. In addition, the MGCL permits a corporation to advance reasonable expenses to a director or officer upon the corporation's receipt of:

a written affirmation by the director or officer of his or her good faith belief that he or she has met the standard of conduct necessary for indemnification by the corporation; and

a written undertaking by him or her or on his or her behalf to repay the amount paid or reimbursed by the corporation if it is ultimately determined that the standard of conduct was not met.

Our charter authorizes us to obligate us and our bylaws obligate us, to the maximum extent permitted by Maryland law in effect from time to time, to indemnify and, without requiring a preliminary determination of the ultimate entitlement to indemnification, pay or reimburse reasonable expenses in advance of final disposition of a proceeding to:

any present or former director or officer who is made, or threatened to be made, a party to the proceeding by reason of his or her service in that capacity; or

any individual who, while a director or officer of our company and at our request, serves or has served as a director, officer, partner or trustee of another corporation, REIT, partnership, joint venture, trust, employee benefit plan or other enterprise and who is made, or threatened to be made, a party to the proceeding by reason of his or her service in that capacity.

Our charter and bylaws also permit us, with the approval of our board of directors, to indemnify and advance expenses to any person who served a predecessor of ours in any of the capacities described above and to any employee or agent of our company or a predecessor of our company.

The partnership agreement provides that we, as general partner, and our officers and directors are indemnified to the maximum extent permitted by law. See "Description of the Partnership Agreement of Extra Space Storage LP Management Liability and Indemnification."

We have entered into indemnification agreements with each of our directors and executive officers. The indemnification agreements require, among other matters, that we indemnify our directors and executive officers to the maximum extent permitted by law and advance to the directors and executive officers all related expenses, subject to reimbursement if it is subsequently determined that indemnification is not permitted. Under these agreements, we must also indemnify and advance all expenses incurred by directors and executive officers seeking to enforce their rights under the indemnification agreements and may cover directors and executive officers under our directors' and officers' liability insurance. Although indemnification agreements offer substantially the same scope of



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coverage afforded under the bylaws, they provide greater assurance to directors and executive officers that indemnification will be available, because, as contracts, they cannot be modified unilaterally in the future by the board of directors to eliminate the rights they provide.

Insofar as the foregoing provisions permit indemnification of directors, officers or persons controlling us for liability arising under the Securities Act, we have been informed that in the opinion of the Securities and Exchange Commission, this indemnification is against public policy as expressed in the Securities Act and is therefore unenforceable.

**REIT Qualification**

Our charter provides that our board of directors may revoke or otherwise terminate our REIT election, without approval of our stockholders, if it determines that it is no longer in our best interests to continue to qualify as a REIT.

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**U.S. FEDERAL INCOME TAX CONSEQUENCES**

The following is a general summary of certain material U.S. federal income tax consequences regarding our company and to holders of our capital stock. For purposes of this discussion, references to "we," "our" and "us" mean only Extra Space Storage Inc., and do not include any of its subsidiaries, except as otherwise indicated. This summary is for general information only and is not tax advice. The information in this summary is based on:

the Code;

current, temporary and proposed Treasury Regulations promulgated under the Code;

the legislative history of the Code;

administrative interpretations and practices of the IRS; and

court decisions;

in each case, as of the date of this prospectus. In addition, the administrative interpretations and practices of the IRS include its practices and policies as expressed in private letter rulings that are not binding on the IRS except with respect to the particular taxpayers who requested and received those rulings. Future legislation, Treasury Regulations, administrative interpretations and practices and/or court decisions may adversely affect the tax considerations contained in this discussion. Any such change could apply retroactively to transactions preceding the date of the change. We have not requested and do not intend to request a ruling from the IRS that we qualify as a REIT, and the statements in this prospectus are not binding on the IRS or any court. Thus, we can provide no assurance that the tax considerations contained in this discussion will not be challenged by the IRS or will be sustained by a court if challenged by the IRS. This summary does not discuss any state, local or non-U.S. tax consequences, or any tax consequences arising under any federal tax other than the income tax, associated with the purchase, ownership, or disposition of our capital stock or our election to be taxed as a REIT.

**You are urged to consult your tax advisors regarding the tax consequences to you of:**

**the purchase, ownership or disposition of our capital stock, including the federal, state, local, non-U.S. and other tax consequences;**

**our election to be taxed as a REIT for U.S. federal income tax purposes; and**

**potential changes in applicable tax laws.**

**Taxation of Our Company**

***General***

We elected to be taxed as a REIT under Sections 856 through 860 of the Code commencing with our taxable year ended December 31, 2004. We believe that we have been organized and have operated in a manner which has allowed us to qualify for taxation as a REIT under the Code commencing with our taxable year ended December 31, 2004, and we intend to continue to be organized and operate in this manner. However, qualification and taxation as a REIT depend upon our ability to meet the various qualification tests imposed under the Code, including through actual annual operating results, asset composition, distribution levels and diversity of stock ownership. Accordingly, no assurance can be given that we have been organized or have operated in a manner so as to qualify or remain qualified as a REIT. See " Failure to Qualify."



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The sections of the Code and the corresponding Treasury Regulations that relate to qualification and taxation as a REIT are highly technical and complex. The following discussion sets forth certain

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material aspects of the sections of the Code that govern the U.S. federal income tax treatment of a REIT and its stockholders. This summary is qualified in its entirety by the applicable Code provisions, Treasury Regulations promulgated under the Code, and administrative and judicial interpretations thereof.

Latham & Watkins LLP has acted as our tax counsel in connection with this prospectus. Latham & Watkins LLP has rendered an opinion to us to the effect that, commencing with our taxable year ended December 31, 2004, we have been organized and have operated in conformity with the requirements for qualification and taxation as a REIT under the Code, and our proposed method of operation will enable us to continue to meet the requirements for qualification and taxation as a REIT under the Code. It must be emphasized that this opinion was based on various assumptions and representations as to factual matters, including representations made by us in a factual certificate provided by one of our officers. In addition, this opinion was based upon our factual representations set forth in this prospectus. Moreover, our qualification and taxation as a REIT depend upon our ability to meet the various qualification tests imposed under the Code, which are discussed below, including through actual annual operating results, asset composition, distribution levels and diversity of stock ownership, the results of which have not been, and will not be, reviewed by Latham & Watkins LLP. Accordingly, no assurance can be given that our actual results of operation for any particular taxable year will satisfy those requirements. Further, the anticipated U.S. federal income tax treatment described in this discussion may be changed, perhaps retroactively, by legislative, administrative or judicial action at any time. Latham & Watkins LLP has no obligation to update its opinion subsequent to the date of such opinion.

Provided we qualify for taxation as a REIT, we generally will not be required to pay federal corporate income taxes on our net income that is currently distributed to our stockholders. This treatment substantially eliminates the "double taxation" that ordinarily results from investment in a C corporation. A C corporation is a corporation that generally is required to pay tax at the corporate level. Double taxation means taxation once at the corporate level when income is earned and once again at the stockholder level when the income is distributed. We will, however, be required to pay U.S. federal income tax as follows:

First, we will be required to pay tax at regular corporate rates on any undistributed REIT taxable income, including undistributed net capital gains.

Second, we may be required to pay the "alternative minimum tax" on our items of tax preference under some circumstances.

Third, if we have (1) net income from the sale or other disposition of "foreclosure property" held primarily for sale to customers in the ordinary course of business or (2) other nonqualifying income from foreclosure property, we will be required to pay tax at the highest corporate rate on this income. To the extent that income from foreclosure property is otherwise qualifying income for purposes of the 75% gross income test, this tax is not applicable. Subject to certain other requirements, foreclosure property generally is defined as property we acquired through foreclosure or after a default on a loan secured by the property or a lease of the property.

Fourth, we will be required to pay a 100% tax on any net income from prohibited transactions. Prohibited transactions are, in general, sales or other taxable dispositions of property, other than foreclosure property, held primarily for sale to customers in the ordinary course of business.

Fifth, if we fail to satisfy the 75% gross income test or the 95% gross income test, as described below, but our failure is due to reasonable cause and not due to willful neglect and we have otherwise maintained our qualification as a REIT because certain other requirements are met, we will be required to pay a tax on an amount equal to (1) the greater of (a) the amount by

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which we fail to satisfy the 75% gross income test and (b) the amount by which we fail to satisfy the 95% gross income test, multiplied by (2) a fraction intended to reflect our profitability.

Sixth, if we fail to satisfy any of the asset tests (other than a *de minimis* failure of the 5% or 10% asset test), as described below, due to reasonable cause and not due to willful neglect, and we nonetheless maintain our REIT qualification because of specified cure provisions, we will be required to pay a tax equal to the greater of \$50,000 or the highest corporate tax rate multiplied by the net income generated by the nonqualifying assets that caused us to fail such test.

Seventh, if we fail to satisfy any provision of the Code that would result in our failure to qualify as a REIT (other than a violation of the gross income tests or certain violations of the asset tests, as described below) and the violation is due to reasonable cause and not due to willful neglect, we may retain our REIT qualification but we will be required to pay a penalty of \$50,000 for each such failure.

Eighth, we will be required to pay a 4% excise tax to the extent we fail to distribute during each calendar year at least the sum of (1) 85% of our ordinary income for the year, (2) 95% of our capital gain net income for the year, and (3) any undistributed taxable income from prior periods.

Ninth, if we acquire any asset from a corporation that is, or has been, a C corporation in a transaction in which our basis in the asset is determined by reference to the C corporation's basis in the asset, and we subsequently recognize gain on the disposition of the asset during the ten-year period beginning on the date on which we acquired the asset, then we will be required to pay tax at the highest regular corporate tax rate on this gain to the extent of the excess of (1) the fair market value of the asset over (2) our adjusted basis in the asset, in each case determined as of the date on which we acquired the asset. The results described in this paragraph with respect to the recognition of gain assume that the C corporation will refrain from making an election to receive different treatment under applicable Treasury Regulations on its tax return for the year in which we acquire the asset from the C corporation.

Tenth, our subsidiaries that are C corporations, including our "taxable REIT subsidiaries," generally will be required to pay federal corporate income tax on their earnings.

Eleventh, we will be required to pay a 100% tax on any "redetermined rents," "redetermined deductions" or "excess interest." See "Penalty Tax." In general, redetermined rents are rents from real property that are overstated as a result of services furnished to any of our tenants by a taxable REIT subsidiary of ours. Redetermined deductions and excess interest generally represent amounts that are deducted by a taxable REIT subsidiary of ours for amounts paid to us that are in excess of the amounts that would have been deducted based on arm's length negotiations.

Twelfth, we may elect to retain and pay income tax on our net capital gain. In that case, a stockholder would include its proportionate share of our undistributed net capital gain (to the extent we make a timely designation of such gain to the stockholder) in its income, would be deemed to have paid the tax that we paid on such gain, and would be allowed a credit for its proportionate share of the tax deemed to have been paid, and an adjustment would be made to increase the basis of the stockholder in our capital stock.

Thirteenth, if we fail to comply with the requirement to send annual letters to our stockholders requesting information regarding the actual ownership of our stock, and the failure is not due to reasonable cause or due to willful neglect, we will be subject to a \$25,000 penalty, or if the failure is intentional, a \$50,000 penalty.

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We and our subsidiaries may be subject to a variety of taxes other than U.S. federal income tax, including payroll taxes and state and local income, property and other taxes on our assets and operations. In addition, other countries may impose taxes on our property or operations within their jurisdictions. To the extent possible, we will structure our activities to minimize our foreign tax liability. However, there can be no assurance that we will always be able to eliminate or reduce our foreign tax liability. Furthermore, as a REIT, neither we nor our stockholders are likely to derive any significant benefit from any foreign tax credits arising from the payment of those taxes.

*Requirements for Qualification as a REIT.* The Code defines a REIT as a corporation, trust or association:

- (1) that is managed by one or more trustees or directors;
- (2) that issues transferable shares or transferable certificates to evidence its beneficial ownership;
- (3) that would be taxable as a domestic corporation, but for Sections 856 through 859 of the Code;
- (4) that is not a financial institution or an insurance company within the meaning of certain provisions of the Code;
- (5) that is beneficially owned by 100 or more persons;
- (6) not more than 50% in value of the outstanding stock of which is owned, actually or constructively, by five or fewer individuals, including certain specified entities, during the last half of each taxable year; and
- (7) that meets other tests, described below, regarding the nature of its income and assets and the amount of its distributions.

The Code provides that conditions (1) to (4), inclusive, must be met during the entire taxable year and that condition (5) must be met during at least 335 days of a taxable year of 12 months, or during a proportionate part of a taxable year of less than 12 months. Conditions (5) and (6) do not apply until after the first taxable year for which an election is made to be taxed as a REIT. For purposes of condition (6), the term "individual" includes a supplemental unemployment compensation benefit plan, a private foundation or a portion of a trust permanently set aside or used exclusively for charitable purposes, but generally does not include a qualified pension plan or profit sharing trust.

We believe that we have been organized and have operated in a manner that has allowed us to satisfy conditions (1) through (7) inclusive, during the relevant time periods. In addition, our charter provides for restrictions regarding ownership and transfer of our shares which are intended to assist us in continuing to satisfy the share ownership requirements described in (5) and (6) above. A description of the share ownership and transfer restrictions relating to our capital stock is contained in the discussion under the heading "Restrictions on Ownership and Transfer." These restrictions, however, may not ensure that we will, in all cases, be able to satisfy the share ownership requirements described in (5) and (6) above. If we fail to satisfy these share ownership requirements, except as provided in the next sentence, our status as a REIT will terminate. If, however, we comply with the rules contained in applicable Treasury Regulations that require us to ascertain the actual ownership of our shares and we do not know, or would not have known through the exercise of reasonable diligence, that we failed to meet the requirement described in condition (6) above, we will be treated as having met this requirement. See " Failure to Qualify."

In addition, we may not maintain our status as a REIT unless our taxable year is the calendar year. We have, and will continue to have, a calendar taxable year.

*Ownership of Interests in Partnerships, Limited Liability Companies.* In the case of a REIT that is a partner in a partnership or a member in a limited liability company treated as a partnership for U.S.

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federal income tax purposes, Treasury Regulations provide that the REIT will be deemed to own its proportionate share of the assets of the partnership or limited liability company, as the case may be, based on its interest in partnership capital, subject to special rules relating to the 10% asset test described below. Also, the REIT will be deemed to be entitled to its proportionate share of the income of that entity. The assets and gross income of the partnership or limited liability company retain the same character in the hands of the REIT for purposes of Section 856 of the Code, including satisfying the gross income tests and the asset tests. Thus, our pro rata share of the assets and items of income of our operating partnership, including our operating partnership's share of these items of any partnership or limited liability company treated as a partnership or disregarded entity for U.S. federal income tax purposes in which it owns an interest, is treated as our assets and items of income for purposes of applying the requirements described in this discussion, including the gross income and asset tests described below. A brief summary of the rules governing the U.S. federal income taxation of partnerships and limited liability companies is set forth below in " Tax Aspects of Our Operating Partnership, the Subsidiary Partnerships and the Limited Liability Companies."

We have control of our operating partnership and most of the subsidiary partnerships and limited liability companies and intend to operate them in a manner consistent with the requirements for our qualification as a REIT. We are a limited partner or non-managing member in some of our partnerships and limited liability companies. If a partnership or limited liability company in which we own an interest takes, or expects to take, actions that could jeopardize our status as a REIT or require us to pay tax, we may be forced to dispose of our interest in such entity. In addition, it is possible that a partnership or limited liability company could take an action which could cause us to fail a gross income or asset test, and that we would not become aware of such action in time to dispose of our interest in the partnership or limited liability company or take other corrective action on a timely basis. In that case, we could fail to qualify as a REIT unless we were entitled to relief, as described below.

*Qualified REIT Subsidiaries.* We own and operate certain properties through subsidiaries that we intend to be treated as "qualified REIT subsidiaries" under the Code. A corporation will qualify as our qualified REIT subsidiary if we own 100% of the corporation's outstanding stock and do not elect with the subsidiary to treat it as a "taxable REIT subsidiary," as described below. A qualified REIT subsidiary is not treated as a separate corporation, and all assets, liabilities and items of income, gain, loss, deduction and credit of a qualified REIT subsidiary are treated as assets, liabilities and items of income, gain, loss, deduction and credit of the parent REIT for all purposes under the Code, including all REIT qualification tests. Thus, in applying the federal tax requirements described in this discussion, any qualified REIT subsidiaries we own are ignored, and all assets, liabilities and items of income, gain, loss, deduction and credit of such corporations are treated as our assets, liabilities and items of income, gain, loss, deduction and credit. A qualified REIT subsidiary is not subject to U.S. federal income tax, and our ownership of the stock of a qualified REIT subsidiary will not violate the restrictions on ownership of securities, as described below under " Asset Tests." This treatment also applies to other subsidiaries of a REIT that are treated as corporations for U.S. federal income tax purposes, such as the business trusts we own.

*Ownership of Interests in Taxable REIT Subsidiaries.* We currently hold an interest in a number of taxable REIT subsidiaries and may acquire securities in additional taxable REIT subsidiaries in the future. A taxable REIT subsidiary is a corporation other than a REIT in which a REIT directly or indirectly holds stock, and that has made a joint election with such REIT to be treated as a taxable REIT subsidiary. If a taxable REIT subsidiary owns more than 35% of the total voting power or value of the outstanding securities of another corporation, such other corporation will also be treated as a taxable REIT subsidiary. Other than some activities relating to lodging and health care facilities, a taxable REIT subsidiary may generally engage in any business, including the provision of customary or non-customary services to tenants of its parent REIT. A taxable REIT subsidiary is subject to U.S. federal income tax as a regular C corporation. In addition, a taxable REIT subsidiary may be prevented

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from deducting interest on debt funded directly or indirectly by its parent REIT if certain tests regarding the taxable REIT subsidiary's debt to equity ratio and interest expense are not satisfied. A REIT's ownership of securities of a taxable REIT subsidiary is not subject to the 5% or 10% asset test described below. See " Asset Tests."

***Income Tests***

We must satisfy two gross income requirements annually to maintain our qualification as a REIT. First, in each taxable year we must derive directly or indirectly at least 75% of our gross income (excluding gross income from prohibited transactions, certain hedging transactions, and certain foreign currency gains) from investments relating to real property or mortgages on real property, including "rents from real property" and, in certain circumstances, interest, or certain types of temporary investments. Second, in each taxable year we must derive at least 95% of our gross income (excluding gross income from prohibited transactions, certain hedging transactions, and certain foreign currency gains) from the real property investments described above or dividends, interest and gain from the sale or disposition of stock or securities, or any combination of the foregoing. For these purposes, the term "interest" generally does not include any amount received or accrued, directly or indirectly, if the determination of all or some of the amount depends in any way on the income or profits of any person. However, an amount received or accrued generally will not be excluded from the term "interest" solely by reason of being based on a fixed percentage or percentages of receipts or sales.

Rents we receive from a tenant will qualify as "rents from real property" for the purpose of satisfying the gross income requirements for a REIT described above only if all of the following conditions are met:

The amount of rent is not based in any way on the income or profits of any person. However, an amount we receive or accrue generally will not be excluded from the term "rents from real property" solely because it is based on a fixed percentage or percentages of receipts or sales;

Neither we nor an actual or constructive owner of 10% or more of our capital stock actually or constructively owns 10% or more of the interests in the assets or net profits of a non-corporate tenant, or, if the tenant is a corporation, 10% or more of the voting power or value of all classes of stock of the tenant. Rents we receive from such a tenant that is a taxable REIT subsidiary of ours, however, will not be excluded from the definition of "rents from real property" as a result of this condition if at least 90% of the space at the property to which the rents relate is leased to third parties, and the rents paid by the taxable REIT subsidiary are substantially comparable to rents paid by our other tenants for comparable space. Whether rents paid by a taxable REIT subsidiary are substantially comparable to rents paid by other tenants is determined at the time the lease with the taxable REIT subsidiary is entered into, extended, and modified, if such modification increases the rents due under such lease. Notwithstanding the foregoing, however, if a lease with a "controlled taxable REIT subsidiary" is modified and such modification results in an increase in the rents payable by such taxable REIT subsidiary, any such increase will not qualify as "rents from real property." For purposes of this rule, a "controlled taxable REIT subsidiary" is a taxable REIT subsidiary in which the parent REIT owns stock possessing more than 50% of the voting power or more than 50% of the total value of the outstanding stock of such taxable REIT subsidiary;

Rent attributable to personal property, leased in connection with a lease of real property, is not greater than 15% of the total rent received under the lease. If this condition is not met, then the portion of the rent attributable to personal property will not qualify as "rents from real property." To the extent that rent attributable to personal property, leased in connection with a lease of real property, exceeds 15% of the total rent received under the lease, we may transfer a portion of such personal property to a taxable REIT subsidiary; and

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We generally do not operate or manage the property or furnish or render services to our tenants, subject to a 1% *de minimis* exception and except as provided below. We may, however, perform services that are "usually or customarily rendered" in connection with the rental of space for occupancy only and are not otherwise considered "rendered to the occupant" of the property. Examples of these services include the provision of light, heat, or other utilities, trash removal and general maintenance of common areas. In addition, we may employ an independent contractor from whom we derive no revenue to provide customary services, or a taxable REIT subsidiary (which may be wholly or partially owned by us) to provide both customary and non-customary services to our tenants without causing the rent we receive from those tenants to fail to qualify as "rents from real property."

We generally do not intend, and as a general partner of our operating partnership, do not intend to permit our operating partnership, to take actions we believe will cause us to fail to satisfy the rental conditions described above. However, we may intentionally fail to satisfy some of these conditions to the extent we determine, based on the advice of our tax counsel, that the failure will not jeopardize our tax status as a REIT. In addition, with respect to the limitation on the rental of personal property, we have not obtained appraisals of the real property and personal property leased to tenants. Accordingly, there can be no assurance that the IRS will not disagree with our determinations of value.

From time to time, we may enter into hedging transactions with respect to one or more of our assets or liabilities. Our hedging activities may include entering into interest rate swaps, caps, and floors, options to purchase these items, and futures and forward contracts. Income from a hedging transaction, including gain from the sale or disposition of such a transaction, that is clearly identified as a hedging transaction as specified in the Code will not constitute gross income and thus will be exempt from the 95% gross income test to the extent such a hedging transaction is entered into on or after January 1, 2005, and will not constitute gross income and thus will be exempt from the 75% gross income test to the extent such hedging transaction is entered into after July 30, 2008. Income and gain from a hedging transaction, including gain from the sale or disposition of such a transaction, entered into on or prior to July 30, 2008 will be treated as nonqualifying income for purposes of the 75% gross income test. Income and gain from a hedging transaction, including gain from the sale or disposition of such a transaction, entered into prior to January 1, 2005 will be qualifying income for purposes of the 95% gross income test. The term "hedging transaction," as used above, generally means any transaction we enter into in the normal course of our business primarily to manage risk of (1) interest rate changes or fluctuations with respect to borrowings made, or to be made, by us to acquire or carry real estate assets, or (2) for hedging transactions, currency fluctuations with respect to an item of qualifying income under the 75% or 95% gross income test (or any property which generates such income). To the extent that we do not properly identify such transactions as hedges or we hedge with other types of financial instruments, the income from those transactions is not likely to be treated as qualifying income for purposes of the gross income tests. We intend to structure any hedging transactions in a manner that does not jeopardize our status as a REIT.

We have made an investment in certain entities located in Mexico. In addition, from time to time we may acquire additional properties outside of the United States, through a taxable REIT subsidiary or otherwise. These acquisitions could cause us to incur foreign currency gains or losses. Prior to July 30, 2008, the characterization of any such foreign currency gains for purposes of the REIT gross income tests was unclear, though the IRS had indicated that REITs may apply the principles of proposed Treasury Regulations to determine whether such foreign currency gain constitutes qualifying income under the REIT income tests. As a result, we anticipated that any foreign currency gain we recognized relating to rents we receive from any property located in Mexico were qualifying income for purposes of the 75% and 95% gross income tests. Any foreign currency gains recognized after July 30, 2008, to the extent attributable to specified items of qualifying income or gain, or specified qualifying

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assets, however, generally will not constitute gross income for purposes of the 75% and 95% gross income tests, and therefore will be excluded from these tests.

To the extent our taxable REIT subsidiaries pay dividends, we generally will derive our allocable share of such dividend income through our interest in our operating partnership. Such dividend income will qualify under the 95%, but not the 75%, gross income test.

We will monitor the amount of the dividend and other income from our taxable REIT subsidiaries and will take actions intended to keep this income, and any other nonqualifying income, within the limitations of the gross income tests. Although we expect these actions will be sufficient to prevent a violation of the gross income tests, we cannot guarantee that such actions will in all cases prevent such a violation.

If we fail to satisfy one or both of the 75% or 95% gross income tests for any taxable year, we may nevertheless qualify as a REIT for the year if we are entitled to relief under certain provisions of the Code. We generally may make use of the relief provisions if:

following our identification of the failure to meet the 75% or 95% gross income tests for any taxable year, we file a schedule with the IRS setting forth each item of our gross income for purposes of the 75% or 95% gross income tests for such taxable year in accordance with Treasury Regulations to be issued; and

our failure to meet these tests was due to reasonable cause and not due to willful neglect.

It is not possible, however, to state whether in all circumstances we would be entitled to the benefit of these relief provisions. For example, if we fail to satisfy the gross income tests because nonqualifying income that we intentionally accrue or receive exceeds the limits on nonqualifying income, the IRS could conclude that our failure to satisfy the tests was not due to reasonable cause. If these relief provisions do not apply to a particular set of circumstances, we will not qualify as a REIT. As discussed above in "Taxation of Our Company General," even if these relief provisions apply, and we retain our status as a REIT, a tax would be imposed with respect to our nonqualifying income. We may not always be able to comply with the gross income tests for REIT qualification despite periodic monitoring of our income.

*Prohibited Transaction Income.* Any gain that we realize (including net foreign currency gain recognized after July 30, 2008) on the sale of property held as inventory or otherwise held primarily for sale to customers in the ordinary course of business, including our share of any such gain realized by our operating partnership, either directly or through its subsidiary partnerships and limited liability companies, will be treated as income from a prohibited transaction that is subject to a 100% penalty tax, unless certain safe harbor exceptions apply. This prohibited transaction income may also adversely affect our ability to satisfy the gross income tests for qualification as a REIT. Under existing law, whether property is held as inventory or primarily for sale to customers in the ordinary course of a trade or business is a question of fact that depends on all the facts and circumstances surrounding the particular transaction. Our operating partnership intends to hold its properties for investment with a view to long-term appreciation, to engage in the business of acquiring, developing and owning its properties and to make occasional sales of the properties as are consistent with our operating partnership's investment objectives. Except as provided below, we do not intend to permit our operating partnership to enter into any sales that are prohibited transactions. However, the IRS may successfully contend that some or all of the sales made by our operating partnership or its subsidiary partnerships or limited liability companies are prohibited transactions. We would be required to pay the 100% penalty tax on our allocable share of the gains resulting from any such sales. We are an indirect partner or member in certain partnerships or limited liability companies which sell locks, boxes and packing materials to tenants. We report our allocable share of the income from these activities as prohibited transaction income.



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*Penalty Tax.* Any redetermined rents, redetermined deductions or excess interest we generate will be subject to a 100% penalty tax. In general, redetermined rents are rents from real property that are overstated as a result of any services furnished to any of our tenants by one of our taxable REIT subsidiaries, and redetermined deductions and excess interest represent any amounts that are deducted by a taxable REIT subsidiary of ours for amounts paid to us that are in excess of the amounts that would have been deducted based on arm's length negotiations. Rents we receive will not constitute redetermined rents if they qualify for certain safe harbor provisions contained in the Code.

From time to time our taxable REIT subsidiaries may provide services to our tenants. We believe we have set, and we intend to continue to set, any fees paid to our taxable REIT subsidiaries for such services at arm's length rates, although the amounts paid may not satisfy the safe-harbor provisions described above. These determinations are inherently factual, and the IRS has broad discretion to assert that amounts paid between related parties should be reallocated to clearly reflect their respective incomes. If the IRS successfully made such an assertion, we would be required to pay a 100% penalty tax on the excess of an arm's length fee for tenant services over the amount actually paid.

*Asset Tests*

At the close of each calendar quarter of our taxable year, we must also satisfy four tests relating to the nature and diversification of our assets. First, at least 75% of the value of our total assets must be represented by real estate assets, cash, cash items and government securities. For purposes of this test, the term "real estate assets" generally means real property (including interests in real property and interests in mortgages on real property) and shares (or transferable certificates of beneficial interest) in other REITs, as well as any stock or debt instrument attributable to the investment of the proceeds of a stock offering or a public offering of debt with a term of at least five years, but only for the one-year period beginning on the date the REIT receives such proceeds.

Second, not more than 25% of the value of our total assets may be represented by securities, other than those securities includable in the 75% asset test.

Third, of the investments included in the 25% asset class, and except for investments in other REITs, our qualified REIT subsidiaries and taxable REIT subsidiaries, the value of any one issuer's securities may not exceed 5% of the value of our total assets, and we may not own more than 10% of the total vote or value of the outstanding securities of any one issuer except, in the case of the 10% value test, securities satisfying the "straight debt" safe-harbor or securities issued by a partnership that itself would satisfy the 75% income test if it were a REIT. Certain types of securities we may own are disregarded as securities solely for purposes of the 10% value test, including, but not limited to, any loan to an individual or an estate, any obligation to pay rents from real property and any security issued by a REIT. In addition, commencing with the taxable year beginning January 1, 2005, solely for purposes of the 10% value test, the determination of our interest in the assets of a partnership or limited liability company in which we own an interest will be based on our proportionate interest in any securities issued by the partnership or limited liability company, excluding for this purpose certain securities described in the Code.

Fourth, not more than 25% (20% for our taxable years ending on or before December 21, 2008) of the value of our total assets may be represented by the securities of one or more taxable REIT subsidiaries.

Our operating partnership currently owns, directly and indirectly, the stock of certain corporations, including Extra Space Management, Inc., that have elected, together with us, to be treated as our taxable REIT subsidiaries. So long as each of these corporations qualifies as a taxable REIT subsidiary, we will not be subject to the 5% asset test, the 10% voting securities limitation or the 10% value limitation with respect to our indirect ownership of such company's securities. We may acquire securities in additional taxable REIT subsidiaries in the future. We believe that the aggregate value of

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our taxable REIT subsidiaries has not exceeded, and in the future will not exceed, 25% of the aggregate value of our gross assets (20% for our taxable years ending on or before December 31, 2008). No independent appraisals have been obtained to support these conclusions. In addition, there can be no assurance that the IRS will not disagree with our determination of values.

The asset tests must be satisfied at the close of each calendar quarter of our taxable year in which we (directly or through our operating partnership) acquire securities in the applicable issuer, and also at the close of each calendar quarter in which we increase our ownership of securities of such issuer (including as a result of increasing our interest in our operating partnership). For example, our indirect ownership of securities of each issuer will increase as a result of our capital contributions to our operating partnership or as limited partners exercise their redemption/exchange rights. However, after initially meeting the asset tests at the close of any quarter, we will not lose our status as a REIT for failure to satisfy the asset tests at the end of a later quarter solely by reason of changes in asset values. If we fail to satisfy an asset test because we acquire securities or other property during a quarter (including as a result of an increase in our interest in our operating partnership), we may cure this failure by disposing of sufficient nonqualifying assets within 30 days after the close of that quarter. We believe that we have maintained, and we intend to maintain, adequate records of the value of our assets to ensure compliance with the asset tests. If we fail to cure any noncompliance with the asset tests within the 30 day cure period, we would cease to qualify as a REIT unless we are eligible for certain relief provisions discussed below.

Certain relief provisions may be available to us if we discover a failure to satisfy the asset tests described above after the 30-day cure period. Under these provisions, we will be deemed to have met the 5% and 10% asset tests if the value of our nonqualifying assets (1) does not exceed the lesser of (a) 1% of the total value of our assets at the end of the applicable quarter or (b) \$10,000,000, and (2) we dispose of the nonqualifying assets or otherwise satisfy such tests within (a) six months after the last day of the quarter in which the failure to satisfy the asset tests is discovered or (b) the period of time prescribed by Treasury Regulations to be issued. For violations of any of the asset tests due to reasonable cause and not due to willful neglect and that are, in the case of the 5% and 10% asset tests, in excess of the *de minimis* exception described above, we may avoid disqualification as a REIT after the 30-day cure period by taking steps including (1) the disposition of sufficient nonqualifying assets, or the taking of other actions, which allow us to meet the asset tests within (a) six months after the last day of the quarter in which the failure to satisfy the asset tests is discovered or (b) the period of time prescribed by Treasury Regulations to be issued, (2) paying a tax equal to the greater of (a) \$50,000 or (b) the highest corporate tax rate multiplied by the net income generated by the nonqualifying assets, and (3) disclosing certain information to the IRS.

Although we believe we have satisfied the asset tests described above and plan to take steps to ensure that we satisfy such tests for any quarter with respect to which retesting is to occur, there can be no assurance that we will always be successful, or will not require a reduction in our operating partnership's overall interest in an issuer (including in a taxable REIT subsidiary). If we fail to cure any noncompliance with the asset tests in a timely manner, and the relief provisions described above are not available, we would cease to qualify as a REIT.

***Annual Distribution Requirements***

To maintain our qualification as a REIT, we are required to distribute dividends, other than capital gain dividends, to our stockholders in an amount at least equal to the sum of:

90% of our "REIT taxable income"; and

90% of our after-tax net income, if any, from foreclosure property; minus

the excess of the sum of certain items of non-cash income over 5% of our "REIT taxable income."

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For these purposes, our "REIT taxable income" is computed without regard to the dividends paid deduction and our net capital gain. In addition, for purposes of this test, non-cash income means income attributable to leveled stepped rents, original issue discount on purchase money debt, cancellation of indebtedness, or a like-kind exchange that is later determined to be taxable.

In addition, if we dispose of any asset we acquired from a corporation which is or has been a C corporation in a transaction in which our basis in the asset is determined by reference to the basis of the asset in the hands of that C corporation, within the ten-year period following our acquisition of such asset, we would be required to distribute at least 90% of the after-tax gain, if any, we recognized on the disposition of the asset, to the extent that gain does not exceed the excess of (1) the fair market value of the asset over (2) our adjusted basis in the asset, in each case, on the date we acquired the asset.

We generally must pay, or be treated as paying, the distributions described above in the taxable year to which they relate. At our election, a distribution will be treated as paid in a taxable year if it is declared before we timely file our tax return for such year and paid on or before the first regular dividend payment after such declaration, provided such payment is made during the 12-month period following the close of such year. These distributions are treated as received by our stockholders in the year in which paid. This is so even though these distributions relate to the prior year for purposes of the 90% distribution requirement. In order to be taken into account for purposes of our distribution requirement, the amount distributed must not be preferential *i.e.*, every stockholder of the class of stock to which a distribution is made must be treated the same as every other stockholder of that class, and no class of stock may be treated other than according to its dividend rights as a class. To the extent that we do not distribute all of our net capital gain, or distribute at least 90%, but less than 100%, of our "REIT taxable income," as adjusted, we will be required to pay tax on the undistributed amount at regular corporate tax rates. We believe that we have made, and we intend to continue to make, timely distributions sufficient to satisfy these annual distribution requirements and to minimize our corporate tax obligations. In this regard, the partnership agreement of our operating partnership authorizes ESS Holding Business Trust I, our wholly-owned subsidiary and the general partner of our operating partnership, and us, as the indirect general partner of our operating partnership, to take such steps as may be necessary to cause our operating partnership to distribute to its partners an amount sufficient to permit us to meet these distribution requirements and to minimize our corporate tax obligation.

We expect that our REIT taxable income will typically be less than our cash flow because of depreciation and other non-cash charges included in computing REIT taxable income. Accordingly, we anticipate that we generally will have sufficient cash or liquid assets to enable us to satisfy the distribution requirements described above. However, from time to time, we may not have sufficient cash or other liquid assets to meet these distribution requirements due to timing differences between the actual receipt of income and actual payment of deductible expenses, and the inclusion of income and deduction of expenses in determining our taxable income. In addition, we may decide to retain our cash, rather than distribute it, in order to repay debt or for other reasons. If these timing differences occur, we may borrow funds to pay dividends or pay dividends in the form of taxable stock dividends in order to meet the distribution requirements, while preserving our cash.

Pursuant to recent guidance issued by the IRS, certain part-stock and part-cash dividends distributed by publicly-traded REITs with respect to calendar years 2008 through 2011, and in some cases declared as late as December 31, 2012, will be treated as distributions for purposes of the REIT distribution requirements. Under the terms of this guidance, up to 90% of distributions by a REIT could be paid in shares of its stock. If we make such a distribution, taxable stockholders would be required to include the full amount of the dividend (*i.e.*, the cash and the stock portion) as ordinary income (subject to limited exceptions), to the extent of our current and accumulated earnings and profits for U.S. federal income tax purposes, as described under the headings " U.S. Federal Income Tax Considerations for Holders of Our Capital Stock Taxation of Taxable

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U.S. Stockholders Distributions Generally" and " U.S. Federal Income Tax Considerations for Holders of Our Capital Stock Taxation of Non-U.S. Stockholders Distributions Generally." As a result, our stockholders could recognize taxable income in excess of the cash received and may be required to pay tax with respect to such dividends in excess of the cash received. If a taxable stockholder sells the stock it receives as a dividend, the sales proceeds may be less than the amount included in income with respect to the dividend, depending on the market price of the stock at the time of the sale. Furthermore, with respect to non-U.S. stockholders, we may be required to withhold U.S. tax with respect to such dividends, including in respect of all or a portion of such dividend that is payable in stock.

Under some circumstances, we may be able to rectify an inadvertent failure to meet the 90% distribution requirement for a year by paying "deficiency dividends" to our stockholders in a later year, which may be included in our deduction for dividends paid for the earlier year. Thus, we may be able to avoid being taxed on amounts distributed as deficiency dividends, subject to the 4% excise tax described below. However, we will be required to pay interest to the IRS based upon the amount of any deduction claimed for deficiency dividends.

Furthermore, we will be required to pay a 4% excise tax to the extent we fail to distribute during each calendar year at least the sum of 85% of our ordinary income for such year, 95% of our capital gain net income for the year and any undistributed taxable income from prior periods. Any ordinary income and net capital gain on which this excise tax is imposed for any year is treated as an amount distributed during that year for purposes of calculating such tax.

For purposes of the 90% distribution requirement and excise tax described above, dividends declared during the last three months of the taxable year, payable to stockholders of record on a specified date during such period and paid during January of the following year, will be treated as paid by us and received by our stockholders on December 31 of the year in which they are declared.

***Like-Kind Exchanges***

Our operating partnership may dispose of properties in transactions intended to qualify as like-kind exchanges under the Code. Such like-kind exchanges are intended to result in the deferral of gain for U.S. federal income tax purposes. The failure of any such transaction to qualify as a like-kind exchange could require us to pay U.S. federal income tax, possibly including the 100% prohibited transaction tax, depending on the facts and circumstances surrounding the particular transaction.

***Failure To Qualify***

If we discover a violation of a provision of the Code that would result in our failure to qualify as a REIT, certain specified cure provisions may be available to us. Except with respect to violations of the gross income tests and asset tests (for which the cure provisions are described above), and provided the violation is due to reasonable cause and not due to willful neglect, these cure provisions generally impose a \$50,000 penalty for each violation in lieu of a loss of REIT status. If we fail to satisfy the requirements for taxation as a REIT in any taxable year, and the relief provisions do not apply, we will be required to pay tax, including any applicable alternative minimum tax, on our taxable income at regular corporate rates. Distributions to stockholders in any year in which we fail to qualify as a REIT will not be deductible by us, and we will not be required to distribute any amounts to our stockholders. As a result, we anticipate that our failure to qualify as a REIT would reduce the cash available for distribution by us to our stockholders. In addition, if we fail to qualify as a REIT, all distributions to stockholders would be taxable as regular corporate dividends to the extent of our current and accumulated earnings and profits. In such event, corporate distributees may be eligible for the dividends-received deduction. In addition, non-corporate stockholders, including individuals, may be eligible for the preferential tax rates on qualified dividend income. See " U.S. Federal Income Tax

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Considerations for Holders of Our Capital Stock Taxation of Taxable U.S. Stockholders Tax Rates." Unless entitled to relief under specific statutory provisions, we would also be ineligible to elect to be treated as a REIT for the four taxable years following the year for which we lose our qualification. It is not possible to state whether in all circumstances we would be entitled to this statutory relief.

***Tax Aspects of Our Operating Partnership, the Subsidiary Partnerships and the Limited Liability Companies***

*General.* All of our investments are held indirectly through our operating partnership. In addition, our operating partnership holds certain of its investments indirectly through subsidiary partnerships and limited liability companies which we believe have been, and will continue to be, treated as partnerships or disregarded entities for U.S. federal income tax purposes. In general, entities that are treated as partnerships or disregarded entities for U.S. federal income tax purposes are "pass-through" entities which are not required to pay U.S. federal income tax. Rather, partners or members of such entities are allocated their shares of the items of income, gain, loss, deduction and credit of the partnership or limited liability company, and are potentially required to pay tax on this income, without regard to whether they receive a distribution from the partnership or limited liability company. We will include in our income our share of these partnership and limited liability company items for purposes of the various gross income tests, the computation of our REIT taxable income, and the REIT distribution requirements. Moreover, for purposes of the asset tests, we will include our pro rata share of assets held by our operating partnership, including its share of its subsidiary partnerships and limited liability companies, based on our capital interests in each such entity. See " Taxation of Our Company."

*Entity Classification.* Our interests in our operating partnership and the subsidiary partnerships and limited liability companies involve special tax considerations, including the possibility that the IRS might challenge the status of these entities as partnerships (or disregarded entities). For example, an entity that would otherwise be treated as a partnership for U.S. federal income tax purposes may nonetheless be taxable as a corporation if it is a "publicly traded partnership" and certain other requirements are met. A partnership or limited liability company would be treated as a publicly traded partnership if its interests are traded on an established securities market or are readily tradable on a secondary market or a substantial equivalent thereof, within the meaning of applicable Treasury Regulations. We do not anticipate that our operating partnership or any subsidiary partnership or limited liability company will be treated as a publicly traded partnership that is taxable as a corporation. However, if any such entity were treated as a corporation, it would be required to pay an entity-level tax on its income. In this situation, the character of our assets and items of gross income would change and could prevent us from satisfying the REIT asset tests and possibly the REIT income tests. See " Asset Tests" and " Income Tests." This, in turn, could prevent us from qualifying as a REIT. See " Failure to Qualify" for a discussion of the effect of our failure to meet these tests. In addition, a change in the tax status of our operating partnership or a subsidiary partnership or limited liability company might be treated as a taxable event. If so, we might incur a tax liability without any related cash payment. We believe our operating partnership and each of our other partnerships and limited liability companies have been and will continue to be treated as partnerships or disregarded entities for U.S. federal income tax purposes.

*Allocations of Income, Gain, Loss and Deduction.* The operating partnership agreement generally provides that allocations of net income will be made first to holders of series A preferred units to the extent of the accrued preferred return on such units. Any remaining net income will be allocated to holders of common units. Allocations to holders of common units will generally be made proportionately to all such holders in respect of such units. Certain limited partners may guaranty debt of our operating partnership. As a result of these guaranties, and notwithstanding the foregoing discussion of allocations of income and loss of our operating partnership to holders of units, such limited partners could under limited circumstances be allocated a disproportionate amount of net loss

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upon a liquidation of our operating partnership, which net loss would have otherwise been allocable to us.

If an allocation of partnership income or loss does not comply with the requirements of Section 704(b) of the Code and the Treasury Regulations thereunder, the item subject to the allocation will be reallocated in accordance with the partners' interests in the partnership. This reallocation will be determined by taking into account all of the facts and circumstances relating to the economic arrangement of the partners with respect to such item. Our operating partnership's allocations of taxable income and loss are intended to comply with the requirements of Section 704(b) of the Code and the Treasury Regulations thereunder.

*Tax Allocations With Respect to the Properties.* Under Section 704(c) of the Code, income, gain, loss and deduction attributable to appreciated or depreciated property that is contributed to a partnership in exchange for an interest in the partnership, must be allocated in a manner so that the contributing partner is charged with the unrealized gain or benefits from the unrealized loss associated with the property at the time of the contribution. The amount of the unrealized gain or unrealized loss generally is equal to the difference between the fair market value or book value and the adjusted tax basis of the contributed property at the time of contribution, as adjusted from time to time. These allocations are solely for U.S. federal income tax purposes and do not affect the book capital accounts or other economic or legal arrangements among the partners.

Our operating partnership may, from time to time, acquire interests in property in exchange for interests in our operating partnership. In that case, the tax basis of these property interests generally carries over to the operating partnership, notwithstanding their different book (*i.e.*, fair market) value (this difference is referred to as a book-tax difference). The partnership agreement requires that income and loss allocations with respect to these properties be made in a manner consistent with Section 704(c) of the Code. Treasury Regulations issued under Section 704(c) of the Code provide partnerships with a choice of several methods of accounting for book-tax differences. Depending on the method we choose in connection with any particular contribution, the carryover basis of each of the contributed interests in the properties in the hands of our operating partnership (1) will or could cause us to be allocated lower amounts of depreciation deductions for tax purposes than would be allocated to us if any of the contributed properties were to have a tax basis equal to its respective fair market value at the time of the contribution and (2) could cause us to be allocated taxable gain in the event of a sale of such contributed interests or properties in excess of the economic or book income allocated to us as a result of such sale, with a corresponding benefit to the other partners in our operating partnership. An allocation described in clause (2) above might cause us or the other partners to recognize taxable income in excess of cash proceeds in the event of a sale or other disposition of property, which might adversely affect our ability to comply with the REIT distribution requirements. See " General Requirements for Qualification as a REIT" and " Annual Distribution Requirements."

Any property acquired by our operating partnership in a taxable transaction will initially have a tax basis equal to its fair market value, and Section 704(c) of the Code generally will not apply.

**U.S. Federal Income Tax Considerations for Holders of Our Capital Stock**

The following summary describes the principal U.S. federal income tax consequences to you of purchasing, owning and disposing of our capital stock. This summary assumes you hold shares of our capital stock as a "capital asset" (generally, property held for investment within the meaning of Section 1221 of the Code). It does not address all the tax consequences that may be relevant to you in light of your particular circumstances. In addition, this discussion does not address the tax

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consequences relevant to persons who receive special treatment under the U.S. federal income tax law, except where specifically noted. Holders receiving special treatment include, without limitation:

financial institutions, banks and thrifts;

insurance companies;

tax-exempt organizations;

"S" corporations;

traders in securities that elect to mark to market;

partnerships, pass-through entities and persons holding our capital stock through a partnership or other pass-through entity;

stockholders subject to the alternative minimum tax;

regulated investment companies and REITs;

non-U.S. governments and international organizations;

non-U.S. stockholders that are passive foreign investment companies or controlled foreign corporations;

broker-dealers or dealers in securities or currencies;

U.S. expatriates;

persons holding our capital stock as part of a hedge, straddle, conversion, integrated or other risk reduction or constructive sale transaction; or

U.S. stockholders (as defined below) whose functional currency is not the U.S. dollar.

If you are considering purchasing our capital stock, you should consult your tax advisors concerning the application of U.S. federal income tax laws to your particular situation as well as any consequences of the purchase, ownership and disposition of our capital stock arising under the laws of any state, local or non-U.S. taxing jurisdiction.

When we use the term "U.S. stockholder," we mean a holder of shares of our capital stock who, for U.S. federal income tax purposes, is:

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an individual who is a citizen or resident of the United States;

a corporation, including an entity treated as a corporation for U.S. federal income tax purposes, created or organized in or under the laws of the United States or of any state thereof or in the District of Columbia;

an estate the income of which is subject to U.S. federal income taxation regardless of its source; or

a trust that (1) is subject to the primary supervision of a U.S. court and the control of one or more U.S. persons or (2) has a valid election in effect under applicable Treasury Regulations to be treated as a U.S. person.

If you hold shares of our capital stock and are not a partnership (or entity treated as a partnership for U.S. federal income tax purposes) or a U.S. stockholder, you are a "non-U.S. stockholder."

If a partnership or other entity treated as a partnership for U.S. federal income tax purposes holds shares of our capital stock, the tax treatment of a partner generally will depend on the status of the partner and on the activities of the partnership. Partners of partnerships holding shares of our capital stock are encouraged to consult their tax advisors.



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*Taxation of Taxable U.S. Stockholders*

*Distributions Generally.* Distributions out of our current or accumulated earnings and profits will be treated as dividends and, other than with respect to capital gain dividends and certain amounts which have previously been subject to corporate level tax discussed below, will be taxable to our taxable U.S. stockholders as ordinary income when actually or constructively received. See " Tax Rates" below. As long as we qualify as a REIT, these distributions will not be eligible for the dividends-received deduction in the case of U.S. stockholders that are corporations or, except to the extent provided in " Tax Rates" below, the preferential rates on qualified dividend income applicable to non-corporate U.S. stockholders, including individuals. For purposes of determining whether distributions to holders of capital stock are out of current or accumulated earnings and profits, our earnings and profits will be allocated first to our outstanding preferred stock and then to our outstanding common stock.

To the extent that we make distributions on our capital stock in excess of our current and accumulated earnings and profits, these distributions will be treated first as a tax-free return of capital to a U.S. stockholder. This treatment will reduce the U.S. stockholder's adjusted tax basis in such shares of stock by the amount of the distribution, but not below zero. Distributions in excess of our current and accumulated earnings and profits and in excess of a U.S. stockholder's adjusted tax basis in its shares will be taxable as capital gain. Such gain will be taxable as long-term capital gain if the shares have been held for more than one year. Dividends we declare in October, November, or December of any year and which are payable to a stockholder of record on a specified date in any of these months will be treated as both paid by us and received by the stockholder on December 31 of that year, provided we actually pay the dividend on or before January 31 of the following year. U.S. stockholders may not include in their own income tax returns any of our net operating losses or capital losses.

Certain stock dividends, including dividends partially paid in our capital stock and partially paid in cash that comply with recent IRS guidance, generally will be taxable to the recipient U.S. stockholder to the same extent as if paid in cash.

*Capital Gain Dividends.* Dividends that we properly designate as capital gain dividends will be taxable to our taxable U.S. stockholders as a gain from the sale or disposition of a capital asset held for more than one year, to the extent that such gain does not exceed our actual net capital gain for the taxable year. U.S. stockholders that are corporations may, however, be required to treat up to 20% of certain capital gain dividends as ordinary income. If we properly designate any portion of a dividend as a capital gain dividend, then, except as otherwise required by law, we presently intend to allocate a portion of the total capital gain dividends paid or made available to holders of all classes of our stock for the year to the holders of our common stock and preferred stock (if and when issued) in proportion to the amount that our total dividends, as determined for U.S. federal income tax purposes, paid or made available to the holders of such stock for the year bears to the total dividends, as determined for U.S. federal income tax purposes, paid or made available to holders of all classes of our stock for the year.

*Retention of Net Capital Gains.* We may elect to retain, rather than distribute as a capital gain dividend, all or a portion of our net capital gains. If we make this election, we would pay tax on our retained net capital gains. In addition, to the extent we so elect, our earnings and profits (determined for U.S. federal income tax purposes) would be adjusted accordingly, and a U.S. stockholder generally would:

include its pro rata share of our undistributed net capital gains in computing its long-term capital gains in its return for its taxable year in which the last day of our taxable year falls, subject to certain limitations as to the amount that is includable;

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be deemed to have paid its share of the capital gains tax imposed on us on the designated amounts included in the U.S. stockholder's income as long-term capital gain;

receive a credit or refund for the amount of tax deemed paid by it;

increase the adjusted basis of its capital stock by the difference between the amount of includable gains and the tax deemed to have been paid by it; and

in the case of a U.S. stockholder that is a corporation, appropriately adjust its earnings and profits for the retained capital gains in accordance with Treasury Regulations to be promulgated by the IRS.

*Passive Activity Losses and Investment Interest Limitations.* Distributions we make and gain arising from the sale or exchange by a U.S. stockholder of our shares will not be treated as passive activity income. As a result, U.S. stockholders generally will not be able to apply any "passive losses" against this income or gain. A U.S. stockholder may elect to treat capital gain dividends, capital gains from the disposition of our stock and income designated as qualified dividend income, described in " Tax Rates" below, as investment income for purposes of computing the investment interest limitation, but in such case, the stockholder will be taxed at ordinary income rates on such amount. Other distributions made by us, to the extent they do not constitute a return of capital, generally will be treated as investment income for purposes of computing the investment interest limitation.

*Dispositions of Our Capital Stock.* If a U.S. stockholder sells or disposes of shares of capital stock, it will recognize gain or loss for U.S. federal income tax purposes in an amount equal to the difference between the amount of cash and the fair market value of any property received on the sale or other disposition and the holder's adjusted basis in the shares. This gain or loss, except as provided below, will be a long-term capital gain or loss if the holder has held such capital stock for more than one year. However, if a U.S. stockholder recognizes a loss upon the sale or other disposition of capital stock that it has held for six months or less, after applying certain holding period rules, the loss recognized will be treated as a long-term capital loss to the extent the U.S. stockholder received distributions from us which were required to be treated as long-term capital gains.

*Redemption or Repurchase by Us.* A redemption or repurchase of shares of our stock will be treated under Section 302 of the Code as a distribution taxable as a dividend to the extent of our current and accumulated earnings and profits at ordinary income rates unless the redemption or repurchase satisfies one of the tests set forth in Section 302(b) of the Code and is therefore treated as a sale or exchange of the redeemed or repurchased shares. The redemption or repurchase will be treated as a sale or exchange if it:

is "substantially disproportionate" with respect to the U.S. stockholder;

results in a "complete termination" of the U.S. stockholder's stock interest in us; or

is "not essentially equivalent to a dividend" with respect to the U.S. stockholder,

all within the meaning of Section 302(b) of the Code.

In determining whether any of these tests have been met, shares of capital stock, including common stock and other equity interests in us, considered to be owned by the U.S. stockholder by reason of certain constructive ownership rules set forth in the Code, as well as shares of our capital stock actually owned by the U.S. stockholder, must generally be taken into account. Because the determination as to whether any of the alternative tests of Section 302(b) of the Code will be satisfied with respect to the U.S. stockholder depends upon the facts and circumstances at the time that the determination must be made, U.S. stockholders are advised to consult their tax advisors to determine such tax treatment.

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If a redemption or repurchase of shares of our stock is treated as a distribution taxable as a dividend, the amount of the distribution will be measured by the amount of cash and the fair market value of any property received. See " Distributions Generally." A U.S. stockholder's adjusted basis in the redeemed or repurchased shares of the stock for tax purposes will be transferred to its remaining shares of our capital stock, if any. If a U.S. stockholder owns no other shares of our capital stock, such basis may, under certain circumstances, be transferred to a related person or it may be lost entirely.

If a redemption or repurchase of shares of our stock is not treated as a distribution taxable as a dividend, it will be treated as a taxable sale or exchange in the manner described under " Dispositions of Our Capital stock."

*Tax Rates.* The maximum tax rate for non-corporate taxpayers for capital gains, including certain "capital gain dividends," is generally 15% (although depending on the characteristics of the assets which produced these gains and on designations which we may make, certain capital gain dividends may be taxed at a 25% rate). Capital gain dividends will only be eligible for the rates described above to the extent that they are properly designated by the REIT as "capital gain dividends." The maximum tax rate for non-corporate taxpayers for income that the REIT properly designates as "qualified dividend income" is generally 15%. In general, dividends payable by a REIT are not eligible for the tax rate on qualified dividend income, except to the extent that the taxpayer satisfies certain holding requirements with respect to the REIT's stock and the REIT's dividends are attributable to dividends received from certain taxable corporations (in our case, such as Extra Space Management, Inc.) or to income that was subject to tax at the corporate/REIT level (for example, if the REIT distributed taxable income that it retained and paid tax on in the prior taxable year). After December 31, 2012, the capital gains tax rate is currently scheduled to increase to 20% and the rate applicable to dividends is currently scheduled to increase to the tax rate then applicable to ordinary income. U.S. stockholders that are corporations may be required to treat up to 20% of some capital gain dividends as ordinary income.

*Medicare Tax on Unearned Income.* Certain U.S. stockholders that are individuals, estates or trusts are required to pay an additional 3.8% tax on, among other things, dividends on, and capital gains from, the sale or other disposition of stock for taxable years beginning after December 31, 2012. U.S. stockholders should consult their tax advisors regarding the effect, if any, of this additional tax on their ownership and disposition of our capital stock.

*Foreign Accounts.* Certain future payments to "foreign financial institutions" in respect of accounts of U.S. stockholders at such financial institutions may be subject to withholding at a rate of 30%. U.S. stockholders should consult their tax advisors regarding the effect, if any, of this withholding provision on their ownership and disposition of our capital stock and the effective date of such provision. See " Taxation of Non-U.S. Stockholders Foreign Accounts."

*Information Reporting and Backup Withholding.* We are required to report to our U.S. stockholders and the IRS the amount of dividends paid during each calendar year, and the amount of any tax withheld. Under the backup withholding rules, a stockholder may be subject to backup withholding with respect to dividends paid unless the holder is a corporation or comes within certain other exempt categories and, when required, demonstrates this fact, or provides a taxpayer identification number, certifies as to no loss of exemption from backup withholding, and otherwise complies with applicable requirements of the backup withholding rules. A U.S. stockholder that does not provide us with its correct taxpayer identification number may also be subject to penalties imposed by the IRS. Backup withholding is not an additional tax. Any amount paid as backup withholding will be creditable against the stockholder's U.S. federal income tax liability, provided the required information is timely furnished to the IRS. In addition, we may be required to withhold a portion of capital gain distributions to any stockholders who fail to certify their non-foreign status. See " Taxation of Non-U.S. Stockholders."

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***Taxation of Tax-Exempt Stockholders***

Dividend income from us and gain arising upon a sale of our shares generally should not be unrelated business taxable income, or UBTI, to a tax-exempt stockholder, except as described below. This income or gain will be UBTI, however, if a tax-exempt stockholder holds its shares as "debt-financed property" within the meaning of the Code or if the shares are used in a trade or business of the tax-exempt stockholder. Generally, "debt-financed property" is property the acquisition or holding of which was financed through a borrowing by the tax-exempt stockholder.

For tax-exempt stockholders that are social clubs, voluntary employee benefit associations, supplemental unemployment benefit trusts, or qualified group legal services plans exempt from U.S. federal income taxation under Sections 501(c)(7), (c)(9), (c)(17) or (c)(20) of the Code, respectively, income from an investment in our shares will constitute UBTI unless the organization is able to properly claim a deduction for amounts set aside or placed in reserve for specific purposes so as to offset the income generated by its investment in our shares. These prospective investors should consult their tax advisors concerning these "set aside" and reserve requirements.

Notwithstanding the above, however, a portion of the dividends paid by a "pension-held REIT" may be treated as unrelated business taxable income as to certain trusts that hold more than 10%, by value, of the interests in the REIT. A REIT will not be a "pension-held REIT" if it is able to satisfy the "not closely held" requirement without relying on the "look-through" exception with respect to certain trusts or if such REIT is not "predominantly held" by "qualified trusts." As a result of restrictions on ownership and transfer of our stock contained in our charter, we do not expect to be classified as a "pension-held REIT," and as a result, the tax treatment described above should be inapplicable to our stockholders. However, because our capital stock is (and, we anticipate, will continue to be) publicly traded, we cannot guarantee that this will always be the case.

***Taxation of Non-U.S. Stockholders***

The following discussion addresses the rules governing U.S. federal income taxation of the purchase, ownership and disposition of our capital stock by non-U.S. stockholders. These rules are complex, and no attempt is made herein to provide more than a brief summary of such rules. Accordingly, the discussion does not address all aspects of U.S. federal income taxation and does not address state, local or non-U.S. tax consequences that may be relevant to a non-U.S. stockholder in light of its particular circumstances. We urge non-U.S. stockholders to consult their tax advisors to determine the impact of federal, state, local and non-U.S. income tax laws on the purchase, ownership and disposition of shares of our capital stock, including any reporting requirements.

*Distributions Generally.* Distributions (including any taxable stock dividends) that are neither attributable to gains from sales or exchanges by us of U.S. real property interests nor designated by us as capital gain dividends (except as described below) will be treated as dividends of ordinary income to the extent that they are made out of our current or accumulated earnings and profits. Such distributions ordinarily will be subject to withholding of U.S. federal income tax at a 30% rate or such lower rate as may be specified by an applicable income tax treaty, unless the distributions are treated as effectively connected with the conduct by the non-U.S. stockholder of a U.S. trade or business. Under certain treaties, however, lower withholding rates generally applicable to dividends do not apply to dividends from a REIT. Certain certification and disclosure requirements must be satisfied to be exempt from withholding under the effectively connected income exemption. Dividends that are treated as effectively connected with a U.S. trade or business will generally not be subject to withholding but will be subject to U.S. federal income tax on a net basis at graduated rates, in the same manner as dividends paid to U.S. stockholders are subject to U.S. federal income tax. Any such dividends received by a non-U.S. stockholder that is a corporation may also be subject to an additional branch profits tax

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at a 30% rate (applicable after deducting U.S. federal income taxes paid on such effectively connected income) or such lower rate as may be specified by an applicable income tax treaty.

Except as otherwise provided below, we expect to withhold U.S. federal income tax at the rate of 30% on any distributions made to a non-U.S. stockholder unless:

- (1) a lower treaty rate applies and the non-U.S. stockholder files with us an IRS Form W-8BEN evidencing eligibility for that reduced treaty rate; or
- (2) the non-U.S. stockholder files an IRS Form W-8ECI with us claiming that the distribution is income effectively connected with the non-U.S. stockholder's trade or business.

Distributions in excess of our current and accumulated earnings and profits will not be taxable to a non-U.S. stockholder to the extent that such distributions do not exceed the adjusted basis of the stockholder's capital stock, but rather will reduce the adjusted basis of such stock. To the extent that such distributions exceed the non-U.S. stockholder's adjusted basis in such capital stock, they will give rise to gain from the sale or exchange of such stock, the tax treatment of which is described below. For withholding purposes, we expect to treat all distributions as made out of our current or accumulated earnings and profits. However, amounts withheld may be refundable if it is subsequently determined that the distribution was, in fact, in excess of our current and accumulated earnings and profits, provided that certain conditions are met.

*Capital Gain Dividends and Distributions Attributable to a Sale or Exchange of U.S. Real Property Interests.* Distributions to a non-U.S. stockholder that we properly designate as capital gain dividends, other than those arising from the disposition of a U.S. real property interest, generally should not be subject to U.S. federal income taxation, unless:

- (1) the investment in our capital stock is treated as effectively connected with the non-U.S. stockholder's U.S. trade or business, in which case the non-U.S. stockholder will be subject to the same treatment as U.S. stockholders with respect to such gain, except that a non-U.S. stockholder that is a non-U.S. corporation may also be subject to a branch profits tax of up to 30%, as discussed above; or
- (2) the non-U.S. stockholder is a nonresident alien individual who is present in the United States for 183 days or more during the taxable year and certain other conditions are met, in which case the nonresident alien individual will be subject to a 30% tax on the individual's capital gains.

Pursuant to the Foreign Investment in Real Property Tax Act, or FIRPTA, distributions to a non-U.S. stockholder that are attributable to gain from sales or exchanges by us of "U.S. real property interests," or USRPI, whether or not designated as capital gain dividends, will cause the non-U.S. stockholder to be treated as recognizing such gain as income effectively connected with a U.S. trade or business. Non-U.S. stockholders would generally be taxed at the same rates applicable to U.S. stockholders, subject to any applicable alternative minimum tax. We also will be required to withhold and to remit to the IRS 35% (or 15% to the extent provided in Treasury Regulations) of any distribution to non-U.S. stockholders that is designated as a capital gain dividend or, if greater, 35% of any distribution to non-U.S. stockholders that could have been designated as a capital gain dividend. The amount withheld is creditable against the non-U.S. stockholder's U.S. federal income tax liability. However, any distribution with respect to any class of stock that is "regularly traded" on an established securities market located in the United States is not subject to FIRPTA, and therefore, not subject to the 35% U.S. withholding tax described above, if the non-U.S. stockholder did not own more than 5% of such class of stock at any time during the one-year period ending on the date of the distribution. Instead, such distributions will generally be treated as ordinary dividend distributions and subject to withholding in the manner described above with respect to ordinary dividends.

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*Retention of Net Capital Gains.* Although the law is not clear on the matter, it appears that amounts designated by us as retained net capital gains in respect of the capital stock held by stockholders generally should be treated with respect to non-U.S. stockholders in the same manner as actual distributions of capital gain dividends. Under that approach, the non-U.S. stockholders would be able to offset as a credit against their federal income tax liability their proportionate share of the tax paid by us on such retained net capital gains and to receive from the IRS a refund to the extent their proportionate share of such tax paid by us exceeds their actual federal income tax liability. If we were to designate any portion of our net capital gain as retained net capital gain, a non-U.S. stockholder should consult its tax advisor regarding the taxation of such retained net capital gain.

*Sale of Our Capital Stock.* Gain recognized by a non-U.S. stockholder upon the sale, exchange or other taxable disposition of our capital stock generally will not be subject to U.S. federal income taxation unless such stock constitutes a USRPI. In general, stock of a domestic corporation that constitutes a "U.S. real property holding corporation," or USRPHC, will constitute a USRPI. We believe that we are a USRPHC. Our capital stock will not, however, constitute a USRPI so long as we are a "domestically controlled qualified investment entity." A "domestically controlled qualified investment entity" includes a REIT in which at all times during a specified testing period less than 50% in value of its stock is held directly or indirectly by non-U.S. stockholders. We believe, but cannot guarantee, that we are a "domestically controlled qualified investment entity." Because our capital stock is (and, we anticipate, will continue to be) publicly traded, no assurance can be given that we will continue to be a "domestically controlled qualified investment entity."

Notwithstanding the foregoing, gain from the sale, exchange or other taxable disposition of our capital stock not otherwise subject to FIRPTA will be taxable to a non-U.S. stockholder if either (1) the investment in our capital stock is treated as effectively connected with the non-U.S. stockholder's U.S. trade or business or (2) the non-U.S. stockholder is a nonresident alien individual who is present in the United States for 183 days or more during the taxable year and certain other conditions are met. In addition, even if we are a domestically controlled qualified investment entity, upon disposition of our capital stock, a non-U.S. stockholder may be treated as having gain from the sale or other taxable disposition of a USRPI if the non-U.S. stockholder (a) disposes of such stock within a 30-day period preceding the ex-dividend date of a distribution, any portion of which, but for the disposition, would have been treated as gain from the sale or exchange of a USRPI and (b) acquires, or enters into a contract or option to acquire, or is deemed to acquire, other shares of that stock during the 61-day period beginning with the first day of the 30-day period described in clause (a), unless such stock is "regularly traded" and the non-U.S. stockholder did not own more than 5% of such stock at any time during the one-year period ending on the date of the distribution described in clause (a).

Even if we do not qualify as a "domestically controlled qualified investment entity" at the time a non-U.S. stockholder sells our capital stock, gain arising from the sale or other taxable disposition by a non-U.S. stockholder of such stock would not be subject to federal income taxation under FIRPTA as a sale of a USRPI if:

- (1) such class of stock is "regularly traded," as defined by applicable Treasury Regulations, on an established securities market such as the NYSE; and
- (2) such non-U.S. stockholder owned, actually and constructively, 5% or less of such class of our stock throughout the five-year period ending on the date of the sale or exchange.

If gain on the sale, exchange or other taxable disposition of our capital stock were subject to taxation under FIRPTA, the non-U.S. stockholder would be required to file a U.S. federal income tax return and would be subject to regular U.S. federal income tax with respect to such gain in the same manner as a taxable U.S. stockholder (subject to any applicable alternative minimum tax and a special alternative minimum tax in the case of nonresident alien individuals). In addition, if the sale, exchange

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or other taxable disposition of our capital stock were subject to taxation under FIRPTA, and if shares of our capital stock were not "regularly traded" on an established securities market, the purchaser of such capital stock would generally be required to withhold and remit to the IRS 10% of the purchase price.

*Information Reporting and Backup Withholding Tax.* Generally, we must report annually to the IRS the amount of dividends paid to a non-U.S. stockholder, such holder's name and address, and the amount of tax withheld, if any. A similar report is sent to the non-U.S. stockholder. Pursuant to tax treaties or other agreements, the IRS may make its reports available to tax authorities in the non-U.S. stockholder's country of residence.

Payments of dividends or of proceeds from the disposition of stock made to a non-U.S. stockholder may be subject to information reporting and backup withholding unless such holder establishes an exemption, for example, by properly certifying its non-U.S. status on an IRS Form W-8BEN or another appropriate version of IRS Form W-8. Notwithstanding the foregoing, backup withholding and information reporting may apply if either we have or our paying agent has actual knowledge, or reason to know, that a non-U.S. stockholder is a U.S. person.

Backup withholding is not an additional tax. Rather, the U.S. federal income tax liability of persons subject to backup withholding will be reduced by the amount of tax withheld. If withholding results in an overpayment of taxes, a refund or credit may be obtained, provided that the required information is timely furnished to the IRS.

*Foreign Accounts.* Withholding taxes may be imposed on certain types of payments made to "foreign financial institutions" and certain other non-U.S. entities. The legislation imposes a 30% withholding tax on dividends on, and gross proceeds from the sale or other disposition of, stock paid to a foreign financial institution or to a foreign nonfinancial entity, unless (1) the foreign financial institution undertakes certain diligence and reporting obligations or (2) the foreign non-financial entity either certifies it does not have any substantial U.S. owners or furnishes identifying information regarding each substantial U.S. owner. In addition, if the payee is a foreign financial institution, it generally must enter into an agreement with the U.S. Treasury that requires, among other things, that it undertake to identify accounts held by certain U.S. persons or U.S.-owned foreign entities, annually report certain information about such accounts, and withhold 30% on payments to certain other account holders.

Although this legislation currently applies to applicable payments made after December 31, 2012, in recent guidance, the IRS has indicated that Treasury Regulations will be issued providing that the withholding provisions described above will apply to payments of dividends on our common stock made on or after January 1, 2014 and to payments of gross proceeds from a sale or other disposition of such stock on or after January 1, 2015. Prospective investors should consult their tax advisors regarding this legislation.

### **Other Tax Consequences**

State, local and non-U.S. income tax laws may differ substantially from the corresponding U.S. federal income tax laws, and this discussion does not purport to describe any aspect of the tax laws of any state, local or non-U.S. jurisdiction, or any federal tax other than the income tax. You should consult your tax advisor regarding the effect of state, local, non-U.S., and other tax laws with respect to our tax treatment as a REIT and on an investment in our capital stock.

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**PLAN OF DISTRIBUTION**

We may sell the securities domestically or abroad to one or more underwriters for public offering and sale by them or may sell the securities to investors directly or through dealers or agents, or through a combination of methods. Any underwriter, dealer or agent involved in the offer and sale of the securities will be named in the applicable prospectus supplement.

Underwriters may offer and sell the securities at: (1) a fixed price or prices, which may be changed, (2) market prices prevailing at the time of sale, (3) prices related to the prevailing market prices at the time of sale or (4) negotiated prices. We also may, from time to time, authorize underwriters acting as their agents to offer and sell the securities upon the terms and conditions as are set forth in the applicable prospectus supplement. In connection with the sale of securities, underwriters may be deemed to have received compensation from us in the form of underwriting discounts or commissions and may also receive commissions from purchasers of securities for whom they may act as agent. Underwriters may sell securities to or through dealers, and the dealers may receive compensation in the form of discounts, concessions or commissions from the underwriters and/or commissions from the purchasers for whom they may act as agent.

Any underwriting compensation paid by us to underwriters, dealers or agents in connection with the offering of securities, and any discounts, concessions or commissions allowed by underwriters to participating dealers, will be set forth in the applicable prospectus supplement. Dealers and agents participating in the distribution of the securities may be deemed to be underwriters, and any discounts and commissions received by them and any profit realized by them on resale of the securities may be deemed to be underwriting discounts and commissions under the Securities Act. Underwriters, dealers and agents may be entitled, under agreements entered into with us and our operating partnership, to indemnification against and contribution toward civil liabilities, including liabilities under the Securities Act. We will describe any indemnification agreement in the applicable prospectus supplement.

Unless we specify otherwise in the applicable prospectus supplement, any series of securities issued hereunder will be a new issue with no established trading market (other than our common stock, which is listed on the NYSE). If we sell any shares of our common stock pursuant to a prospectus supplement, such shares will be listed on the NYSE, subject to official notice of issuance. We may elect to list any other securities issued hereunder on any exchange, but we are not obligated to do so. Any underwriters or agents to or through whom such securities are sold by us or our operating partnership for public offering and sale may make a market in such securities, but such underwriters or agents will not be obligated to do so and may discontinue any market making at any time without notice. We cannot assure you as to the liquidity of the trading market for any such securities.

If indicated in the applicable prospectus supplement, we may authorize underwriters or other persons acting as our agents to solicit offers by institutions or other suitable purchasers to purchase the securities from us at the public offering price set forth in the prospectus supplement, pursuant to delayed delivery contracts providing for payment and delivery on the date or dates stated in the prospectus supplement. These purchasers may include, among others, commercial and savings banks, insurance companies, pension funds, investment companies and educational and charitable institutions. Delayed delivery contracts will be subject to the condition that the purchase of the securities covered by the delayed delivery contracts will not at the time of delivery be prohibited under the laws of any jurisdiction in the United States to which the purchaser is subject. The underwriters and agents will not have any responsibility with respect to the validity or performance of these contracts.



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To facilitate the offering of the securities, certain persons participating in the offering may engage in transactions that stabilize, maintain, or otherwise affect the price of the securities. This may include over-allotments or short sales of the securities, which involves the sale by persons participating in the offering of more securities than we sold to them. In these circumstances, these persons would cover the over-allotments or short positions by making purchases in the open market or by exercising their over-allotment option. In addition, these persons may stabilize or maintain the price of the securities by bidding for or purchasing securities in the open market or by imposing penalty bids, whereby selling concessions allowed to dealers participating in the offering may be reclaimed if securities sold by them are repurchased in connection with stabilization transactions. The effect of these transactions may be to stabilize or maintain the market price of the securities at a level above that which might otherwise prevail in the open market. These transactions may be discontinued at any time.

The underwriters, dealers and agents and their affiliates may be customers of, engage in transactions with and perform services for us and our operating partnership in the ordinary course of business.

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**LEGAL MATTERS**

Certain legal matters will be passed upon for us by Latham & Watkins LLP, San Diego, California. Venable LLP, Baltimore, Maryland, has issued an opinion to us regarding certain matters of Maryland law.

**EXPERTS**

The consolidated financial statements of Extra Space Storage Inc. appearing in Extra Space Storage Inc.'s Annual Report (Form 10-K) for the year ended December 31, 2010 (including the schedule appearing therein), and the effectiveness of Extra Space Storage Inc.'s internal control over financial reporting as of December 31, 2010 have been audited by Ernst & Young LLP, independent registered public accounting firm, as set forth in their reports thereon, included therein, and incorporated herein by reference. Such consolidated financial statements and schedule and Extra Space Storage Inc. management's assessment of the effectiveness of internal control over financial reporting as of December 31, 2010 are incorporated herein by reference in reliance upon such reports given on the authority of such firm as experts in accounting and auditing.

Table of Contents**PART II****INFORMATION NOT REQUIRED IN PROSPECTUS****Item 14. *Other Expenses of Issuance and Distribution.***

The following table itemizes the expenses incurred by us in connection with the issuance and registration of the securities being registered hereunder. All amounts shown are estimates except the Securities and Exchange Commission registration fee.

SEC Registration Fee	\$	*
Printing and Engraving Expenses(1)	\$	10,000
Legal Fees and Expenses (other than Blue Sky)(1)	\$	50,000
Accounting Fees and Expenses(1)	\$	25,000
Miscellaneous(1)	\$	15,000
Total	\$	100,000

\*

Deferred in accordance with Rules 456(b) and 457(r).

(1)

Does not include expenses of preparing any accompanying prospectus supplements, listing fees, transfer agent fees and other expenses related to offerings of particular securities.

We will pay all of the costs identified above.

**Item 15. *Indemnification of Directors and Officers.***

Maryland law permits a Maryland corporation to include in its charter a provision limiting the liability of its directors and officers to the corporation and its stockholders for money damages except for liability resulting from (1) actual receipt of an improper benefit or profit in money, property or services or (2) active and deliberate dishonesty established by a final judgment and which is material to the cause of action. Our charter contains such a provision which eliminates such liability to the maximum extent permitted by Maryland law.

Our charter authorizes us, to the maximum extent permitted by Maryland law, to obligate ourselves, and our bylaws obligate us, to indemnify and to pay or reimburse reasonable expenses in advance of final disposition of a proceeding to (1) any present or former director or officer or (2) any individual who, while a director or officer of our company and at the request of us, serves or has served as a director, officer, partner or trustee of another corporation, REIT, partnership, joint venture, trust, employee benefit plan or other enterprise. Our bylaws require our company, to the maximum extent permitted by Maryland law, to indemnify and to pay or reimburse reasonable expenses in advance of final disposition of a proceeding to (a) any present or former director or officer who is made, or threatened to be made, a party to the proceeding by reason of his or her service in that capacity or (b) any individual who, while a director or officer of our company and at the request of us, serves or has served as a director, officer, partner or trustee of another corporation, REIT, partnership, joint venture, trust, employee benefit plan or other enterprise and who is made, or threatened to be made, a party to the proceeding by reason of his or her service in that capacity. Our charter and bylaws also permit us, with the approval of our board of directors, to indemnify and advance expenses to any person who served a predecessor of our company in any of the capacities described above and to any employee or agent of our company or a predecessor of our company.

The Maryland General Corporation Law (the "MGCL") requires a corporation (unless its charter provides otherwise, which our charter does not) to indemnify a director or officer who has been successful, on the merits or otherwise, in the defense of any proceeding to which he or she is made, or threatened to be made, a party by reason of his or her service in that capacity. The MGCL permits a corporation to indemnify its present and former directors and officers, among others, against

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judgments, penalties, fines, settlements and reasonable expenses actually incurred by them in connection with any proceeding to which they may be made, or threatened to be made, a party by reason of their service in those or other capacities unless it is established that (1) the act or omission of the director or officer was material to the matter giving rise to the proceeding and (a) was committed in bad faith or (b) was the result of active and deliberate dishonesty, (2) the director or officer actually received an improper personal benefit in money, property or services or (3) in the case of any criminal proceeding, the director or officer had reasonable cause to believe that the act or omission was unlawful. However, under the MGCL, a Maryland corporation may not indemnify for an adverse judgment in a suit by or in the right of the corporation or for a judgment of liability on the basis that personal benefit was improperly received, unless in either case, a court orders indemnification and then only for expenses. In addition, the MGCL requires us, as a condition to advancing expenses, to obtain (x) a written affirmation by the director or officer of his or her good faith belief that he or she has met the standard of conduct necessary for indemnification by us and (y) a written undertaking by him or her or on his or her behalf to repay the amount paid or reimbursed by us if it shall ultimately be determined that the standard of conduct was not met.

We have entered into indemnification agreements with each of our directors and executive officers. The indemnification agreements require, among other matters, that we indemnify our directors and executive officers to the maximum extent permitted by law and advance to the directors and executive officers all related expenses, subject to reimbursement if it is subsequently determined that indemnification is not permitted. Under these agreements, we must also indemnify and advance all expenses incurred by directors and executive officers seeking to enforce their rights under the indemnification agreements and may cover directors and executive officers under our directors' and officers' liability insurance. Although indemnification agreements offer substantially the same scope of coverage afforded the bylaws, they provide greater assurance to directors and executive officers that indemnification will be available, because, as contracts, they cannot be modified unilaterally in the future by the board of directors to eliminate the rights they provide.

Insofar as the foregoing provisions permit indemnification of directors, officers or persons controlling us for liability arising under the Securities Act of 1933, as amended (the "Securities Act"), we have been informed that, in the opinion of the Securities and Exchange Commission, this indemnification is against public policy as expressed in the Securities Act and is therefore unenforceable.

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**Item 16. Exhibits.**

The following exhibits are filed as part of, or incorporated by reference into, this registration statement on Form S-3:

Exhibit	1.1 Form of Underwriting Agreement - BOTTOM:									
	2005		2004							
Balance Sheet Data:	(In thousands)									
Cash and cash equivalents	\$	22,909	\$	8,070	\$	4,549	\$	5,096	\$	3,905
Working capital	\$	56,176	\$	41,368	\$	24,859	\$	17,078	\$	9,234
Property and equipment, net	\$	2,345	\$	3,226	\$	1,806	\$	960	\$	806
Goodwill and intangible assets, net	\$	115,634	\$	121,339	\$	81,056	\$	52,031	\$	37,340
Total assets	\$	194,247	\$	189,992	\$	131,000	\$	84,935	\$	62,582
Current portion of long term debt and line of credit	\$	--	\$	--	\$	1,201	\$	1,581	\$	1,379
Long-term debt and line of credit, less current portion	\$	--	\$	--	\$	137	\$	5,338	\$	2,902
Total stockholders' equity	\$	174,818	\$	165,562	\$	107,352	\$	65,911	\$	44,622

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

7.

You should read the following summary together with the more detailed business information and consolidated financial statements and related notes that appear elsewhere in this annual report and in the documents that we incorporate by reference into this annual report. This annual report may contain certain “forward-looking” information within the meaning of the Private Securities Litigation Reform Act of 1995. This information involves risks and uncertainties. Our actual results may differ materially from the results discussed in the forward-looking statements. Factors that might cause such a difference include, but are not limited to, those discussed in “Risk Factors.”

#### Overview

We are an information technology consulting firm serving Forbes Global 2000 (“Global 2000”) and other large enterprise companies with a primary focus on the United States. We help our clients gain competitive advantage by using Internet-based technologies to make their businesses more responsive to market opportunities and threats, strengthen relationships with their customers, suppliers and partners, improve productivity and reduce information technology costs. We design, build and deliver business-driven technology solutions using third party software products developed by our partners. Our solutions include custom applications, portals and collaboration, eCommerce, customer relationship management, enterprise content management, business intelligence, business integration, mobile technology, technology platform implementations and service oriented architectures. Our solutions enable clients to meet the changing demands of an increasingly global, Internet-driven and competitive marketplace.

#### Services Revenues

Services revenues are derived from professional services performed developing, implementing, integrating, automating and extending business processes, technology infrastructure, and software applications. Most of our projects are performed on a time and materials basis, and a smaller amount of revenues is derived from projects performed on a fixed fee basis. Fixed fee engagements represented approximately 13% of our services revenues for the twelve months ended December 31, 2008. For time and material projects, revenues are recognized and billed by multiplying the number of hours our professionals expend in the performance of the project by the established billing rates. For fixed fee projects, revenues are generally recognized using the proportionate performance method. Revenues on uncompleted projects are recognized on a contract-by-contract basis in the period in which the portion of the fixed fee is complete. Amounts invoiced to clients in excess of revenues recognized are classified as deferred revenues. On most projects, we are also reimbursed for out-of-pocket expenses such as airfare, lodging and meals. These reimbursements are included as a component of revenues. The aggregate amount of reimbursed expenses will fluctuate depending on the location of our customers, the total number of our projects that require travel, and whether our arrangements with our clients provide for the reimbursement of travel and other project related expenses.

#### Software and Hardware Revenues

Software and hardware revenues are derived from sales of third-party software and hardware. Revenues from sales of third-party software and hardware are generally recorded on a gross basis provided we act as a principal in the transaction. In the event we do not meet the requirements to be considered a principal in the transaction and act as an agent, the revenues are recorded on a net basis. Software and hardware revenues are expected to fluctuate from quarter-to-quarter depending on our customers’ demand for these products.

If we enter into contracts for the sale of services and software or hardware, Company management evaluates whether the services are essential to the functionality of the software or hardware and whether the Company has

objective fair value evidence for each deliverable in the transaction. If management concludes the services to be provided are not essential to the functionality of the software or hardware and can determine objective fair value evidence for each deliverable of the transaction, then we account for each deliverable in the transaction separately, based on the relevant revenue recognition policies. Generally, all deliverables of our multiple element arrangements meet these separation criteria.

#### Cost of revenues

Cost of revenues consists primarily of cash and non-cash compensation and benefits, including bonuses and non-cash compensation related to equity awards, associated with our technology professionals. Cost of revenues also includes the costs associated with subcontractors. Third-party software and hardware costs, reimbursable expenses and other unreimbursed project related expenses are also included in cost of revenues. Project related expenses will fluctuate generally depending on outside factors including the cost and frequency of travel and the location of our customers. Cost of revenues does not include depreciation of assets used in the production of revenues which are primarily personal computers, servers and other information technology related equipment.

## Gross Margins

Our gross margins for services are affected by the utilization rates of our professionals, defined as the percentage of our professionals' time billed to customers divided by the total available hours in the respective period, the salaries we pay our consulting professionals and the average billing rate we receive from our customers. If a project ends earlier than scheduled or we retain professionals in advance of receiving project assignments, or if demand for our services declines, our utilization rate will decline and adversely affect our gross margins. Gross margin percentages of third party software and hardware sales are typically lower than gross margin percentages for services, and the mix of services and software and hardware for a particular period can significantly impact our total combined gross margin percentage for such period. In addition, gross margin for software and hardware sales can fluctuate due to pricing and other competitive pressures.

## Selling, General and Administrative Expenses

Selling, general and administrative expenses ("SG&A") consist of salaries, benefits, bonuses, non-cash compensation, office costs, recruiting, professional fees, sales and marketing activities, training, and other miscellaneous expenses. Non-cash compensation includes stock compensation expenses related to restricted stock, option grants to employees and non-employee directors, and retirement savings plan contributions. We work to minimize selling costs by focusing on repeat business with existing customers and by accessing sales leads generated by our software vendors, most notably IBM, whose products we use to design and implement solutions for our clients. These relationships enable us to reduce our selling costs and sales cycle times and increase win rates through leveraging our partners' marketing efforts and endorsements.

## Plans for Growth and Acquisitions

Our goal is to continue to build one of the leading independent information technology consulting firms in North America by expanding our relationships with existing and new clients, leveraging our operations to expand and continuing to make disciplined acquisitions. As demand for our services grows, we anticipate increasing the number of professionals in our 19 North American offices and adding new offices throughout the United States, both organically and through acquisitions. We also intend to continue to leverage our existing offshore capabilities to support our growth and provide our clients flexible options for project delivery. In addition, we believe our track record for identifying acquisitions and our ability to integrate acquired businesses help us complete acquisitions efficiently and productively, while continuing to offer quality services to our clients, including new clients resulting from the acquisitions.

Consistent with our strategy of growth through disciplined acquisitions, we consummated nine acquisitions since January 1, 2005, including four in 2007. Given the current economic conditions, the Company has temporarily suspended making additional acquisitions pending improved visibility into the health of the economy.

## Results of Operations

The following table summarizes our results of operations as a percentage of total revenues:

Revenues:	2008	2007	2006
Services revenues	89.6%	87.8%	85.6%
Software and hardware revenues	4.6	6.5	9.0
Reimbursable expenses	5.8	5.7	5.4
Total revenues	100.0	100.0	100.0



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Cost of revenues (exclusive of depreciation and amortization, shown separately below):			
Project personnel costs	56.6	52.6	52.3
Software and hardware costs	3.7	5.5	7.5
Reimbursable expenses	5.7	5.7	5.4
Other project related expenses	2.2	1.5	1.3
Total cost of revenues	68.2	65.3	66.5
Services gross margin	34.4	38.4	37.4
Software and hardware gross margin	19.4	15.9	16.1
Total gross margin	31.8	34.7	33.5
Selling, general and administrative	20.4	19.2	20.1
Depreciation and intangibles amortization	3.0	2.9	2.7
Impairment of intangibles	0.7	0.0	0.0
Income from operations	7.7	12.6	10.6
Interest income (expense), net	0.2	0.1	(0.3)
Other income (expense), net	(0.4)	0.0	0.1
Income before income taxes	7.5	12.7	10.5
Provision for income taxes	3.2	5.2	4.5
Net income	4.3%	7.5%	6.0%

## Year Ended December 31, 2008 Compared to Year Ended December 31, 2007

Revenues. Total revenues increased 6% to \$231.5 million for the year ended December 31, 2008 from \$218.1 million for the year ended December 31, 2007.

	Financial Results (in thousands)			Explanation for Increases/(Decreases) Over Prior Year Period (in thousands)	
	For the Year Ended December 31, 2008	For the Year Ended December 31, 2007	Total Increase/ (Decrease) Over Prior Year Period	Increase Attributable to Acquired Companies*	Increase/ (Decrease) Attributable to Base Business**
Services Revenues	\$ 207,480	\$ 191,395	\$ 16,085	\$ 29,611	\$ (13,526)
Software and Hardware Revenues	10,713	14,243	(3,530)	1,871	(5,401)
Reimbursable Expenses	13,295	12,510	785	1,372	(587)
Total Revenues	\$ 231,488	\$ 218,148	\$ 13,340	\$ 32,854	\$ (19,514)

\*Defined as companies acquired during 2007; no companies were acquired in 2008.

\*\*Defined as businesses owned as of January 1, 2007.

Services revenues increased 8% to \$207.5 million for the year ended December 31, 2008 from \$191.4 million for the year ended December 31, 2007. Services revenues attributable to our base business decreased \$13.5 million while services revenues attributable to the companies acquired in 2007 increased \$29.6 million, resulting in a net increase of \$16.1 million. We experienced a slowdown in demand during the year related to the deterioration of the U.S. economy.

Software and hardware revenues decreased 25% to \$10.7 million in 2008 from \$14.2 million in 2007. Software and hardware revenues attributable to our base business decreased \$5.4 million while software and hardware revenues attributable to acquired companies increased \$1.9 million, resulting in a net decrease of \$3.5 million. Reimbursable expenses increased 6% to \$13.3 million in 2008 from \$12.5 million in 2007 due to acquisitions and an increased number of projects requiring consultant travel. We do not realize any profit on reimbursable expenses.

Cost of revenues. Cost of revenues increased 11% to \$158.0 million for the year ended December 31, 2008 from \$142.5 million for the year ended December 31, 2007. Cost of revenues attributable to our base business decreased \$7.9 million while cost of revenues attributable to the companies acquired in 2007 increased \$23.4 million, resulting in a net increase of \$15.5 million. The average number of professionals performing services, including subcontractors, increased to 1,165 for the year ended December 31, 2008 from 984 for the year ended December 31, 2007 primarily related to acquisitions and partially offset with head count reductions related to lower demand for services.

Costs associated with software and hardware sales decreased 28% to \$8.6 million for year ended December 31, 2008 from \$12.0 million for the year ended December 31, 2007 which directly relates to the decline in software and hardware revenues discussed above. Costs associated with software and hardware sales attributable to our base business decreased \$4.9 million, while costs associated with software and hardware sales attributable to acquired companies increased \$1.5 million, resulting in a net decrease of \$3.4 million.

**Gross Margin.** Gross margin decreased 3% to \$73.5 million for the year ended December 31, 2008 from \$75.7 million for the year ended December 31, 2007. Gross margin as a percentage of revenues decreased to 31.8% for the year ended December 31, 2008 from 34.7% for the year ended December 31, 2007 due primarily to a decrease in services gross margin offset by an increase in margin from software and hardware. Services gross margin, excluding reimbursable expenses, decreased to 34.4% in 2008 from 38.4% in 2007 primarily as a result of higher labor costs associated with a soft revenue cycle and delays in the start dates of projects. The average utilization rate of our professionals, excluding subcontractors, decreased to 79% for the year ended December 31, 2008 from 81% for the year ended December 31, 2007. Average hourly billing rates decreased to \$109 for 2008 from \$118 for 2007, primarily due to lower rates associated with the acquisition of the China offshore business and the ePairs business in the second half of 2007. The average hourly bill rate for 2008 excluding China, ePairs, and subcontractors was \$116 compared to \$119 for 2007. Software and hardware gross margin increased to 19.4% in 2008 from 15.9% in 2007 primarily as a result of increased sales of our higher margin internally developed software.

Selling, General and Administrative. Selling, general and administrative expenses increased 13% to \$47.2 million for the year ended December 31, 2008 from \$42.0 million for the year ended December 31, 2007 due primarily to fluctuations in expenses as detailed in the following table:

	Increase / (Decrease) (in millions)
Selling, General, and Administrative Expense	
Stock compensation expense	\$ 1.7
Office and technology-related costs	1.5
Salary expense	1.4
Sales related costs	1.0
Bad debt expense	0.8
Customer dispute settlement	0.8
Other	0.6
Bonus expense	(2.6)
Net increase	\$ 5.2

Selling, general and administrative expenses as a percentage of revenues increased slightly to 20% for the year ended December 31, 2008 from 19% for the year ended December 31, 2007, primarily driven by an increase in stock compensation expense, office and technology-related costs, and salary expense. Stock compensation expense increased primarily due to additional restricted stock awards granted in 2007 and 2008. Investments in our technology infrastructure and offshore resources, as well as increases in our facility costs, caused our office and technology-related costs to rise in 2008. The increase in salary expense was associated with development of our healthcare and communications industry verticals. These increases were offset by a decrease in bonus costs. Bonus costs decreased as a result of the Company not achieving the projected performance goals.

Depreciation. Depreciation expense increased 38% to \$2.1 million during 2008 from \$1.6 million during 2007. The increase in depreciation expense is due to both organic and acquisition-related additions of software programs, servers, and other computer equipment to enhance our technology infrastructure. Depreciation expense as a percentage of services revenue, excluding reimbursable expenses, was 1.0% and 0.8% for the years ended December 31, 2008 and 2007, respectively.

Amortization. Amortization increased 2% to \$4.8 million for the year ended December 31, 2008 from \$4.7 million for the year ended December 31, 2007. The increase in amortization expense reflects the acquisition of intangibles in 2007, as well as the amortization of capitalized costs associated with internal use software. The valuations and estimated useful lives of acquired identifiable intangible assets are outlined in Note 6, Goodwill and Intangible Assets, of our consolidated financial statements.

Impairment of Intangible Assets. During the fourth quarter of 2008, we determined that the continuous trading of our common stock below book value and a loss of a key customer were possible indicators of impairment to goodwill or long-lived assets as defined under Statement of Financial Accounting Standards (“SFAS”) No. 142, Goodwill and Other Intangible Assets (“SFAS 142”), and SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets (“SFAS 144”), triggering the necessity of impairment tests as of December 31, 2008. As a result of the tests performed, we recorded a \$1.6 million impairment primarily related to customer relationships we acquired from e tech solutions, Inc. (“E Tech”). The value of these relationships was affected primarily by the loss of a key customer acquired by E Tech, which caused cash flows from the asset group to be lower than originally projected.

Net Interest Income or Expense. We had interest income, net of interest expense, of \$0.5 million for the year ended December 31, 2008 compared to interest income, net of interest expense, of \$0.2 million during the year ended

December 31, 2007. The increase in interest income in 2008 resulted from higher cash balances throughout 2008 compared to prior year and the receipt of interest payments in connection with a promissory note entered into with a customer in June 2008.

**Other Expense.** We expensed \$0.9 million of previously capitalized deferred offering costs during the third quarter of 2008. We no longer intend to use the current shelf registration statement associated with these costs for an equity offering. As required, we wrote off the deferred offering costs.

**Provision for Income Taxes.** We provide for federal, state and foreign income taxes at the applicable statutory rates adjusted for non-deductible expenses. Our effective tax rate increased to 42.2% for the year ended December 31, 2008 from 41.3% for the year ended December 31, 2007. The effective income tax rate increased primarily as a result of the decreased tax benefit of certain dispositions of incentive stock options by holders.

## Year Ended December 31, 2007 Compared to Year Ended December 31, 2006

Revenues. Total revenues increased 36% to \$218.1 million for the year ended December 31, 2007 from \$160.9 million for the year ended December 31, 2006.

	Financial Results (in thousands)			Explanation for Increases/(Decreases) Over Prior Year Period (in thousands)	
	For the Year Ended December 31, 2007	For the Year Ended December 31, 2006	Total Increase/ (Decrease) Over Prior Year Period	Increase Attributable to Acquired Companies*	Increase/ (Decrease) Attributable to Base Business**
Services Revenues	\$ 191,395	\$ 137,722	\$ 53,673	\$ 43,437	\$ 10,236
Software and Hardware Revenues	14,243	14,435	(192)	1,570	(1,762)
Reimbursable Expenses	12,510	8,769	3,741	2,578	1,163
Total Revenues	\$ 218,148	\$ 160,926	\$ 57,222	\$ 47,585	\$ 9,637

\*Defined as companies acquired during 2006 and 2007.

\*\*Defined as businesses owned as of January 1, 2006.

Services revenues increased 39% to \$191.4 million for the year ended December 31, 2007 from \$137.7 million for the year ended December 31, 2006. Base business accounted for 19% of the increase in services revenues for the year ended December 31, 2007 compared to the year ended December 31, 2006. The remaining 81% of the increase is attributable to revenues generated from the companies acquired during 2006 and 2007.

Software revenues decreased 1% to \$14.2 million in 2007 from \$14.4 million in 2006. Software revenues attributable to our base business decreased \$1.8 million while software revenues attributable to acquired companies increased \$1.6 million, resulting in a net decrease of \$192,000. Reimbursable expenses increased 43% to \$12.5 million in 2007 from \$8.8 million in 2006 due to acquisitions and an increased number of projects requiring consultant travel. We do not realize any profit on reimbursable expenses.

Cost of revenues. Cost of revenues increased 33% to \$142.5 million for the year ended December 31, 2007 from \$107.2 million for the year ended December 31, 2006. Base business accounted for 14% of the \$35.3 million increase in cost of revenues for the year ended December 31, 2007 compared to the year ended December 31, 2006. The remaining increase in cost of revenues is attributable to the acquired companies. The average number of professionals performing services, including subcontractors, increased to 1,026 for the year ended December 31, 2007 from 686 for the year ended December 31, 2006.

Costs associated with software sales decreased 1% to \$12.0 million for year ended December 31, 2007 from \$12.1 million for the year ended December 31, 2006 due to an increase in sales of our higher margin internally developed software. Costs associated with software sales attributable to our base business decreased \$1.4 million, while costs associated with software sales attributable to acquired companies increased \$1.3 million, resulting in a net decrease of \$0.1 million.

Gross Margin. Gross margin increased 41% to \$75.7 million for the year ended December 31, 2007 from \$53.8 million for the year ended December 31, 2006. Gross margin as a percentage of revenues increased to 34.7% for the

year ended December 31, 2007 from 33.4% for the year ended December 31, 2006 due primarily to an increase in services gross margin offset by a slight decrease in margin from software. Services gross margin, excluding reimbursable expenses, increased to 38.4% in 2007 from 37.4% in 2006 primarily due to lower bonus as a percent of revenues and lower direct labor cost as a percent of revenues driven by improved billing rates. The average utilization rate of our professionals, excluding subcontractors, decreased slightly to 81% for the year ended December 31, 2007 from 83% for the year ended December 31, 2006. Average hourly billing rates were \$118 for 2007 and \$115 for 2006. Software gross margin decreased to 15.9% in 2007 from 16.1% in 2006 primarily as a result of fluctuations in vendor and competitive pricing based on market conditions at the time of the sales.

Selling, General and Administrative. Selling, general and administrative expenses increased 30% to \$42.0 million for the year ended December 31, 2007 from \$32.3 million for the year ended December 31, 2006 due primarily to fluctuations in expenses as detailed in the following table:

	Increase / (Decrease) (in millions)
Selling, General, and Administrative Expense	
Sales related costs	\$ 3.4
Stock compensation expense	2.5
Salary expense	1.9
Bad debt expense	0.8
Office and technology-related costs	1.6
Recruiting and training-related costs	0.8
Other	0.5
Bonus expense	(1.8)
Net increase	\$ 9.7

Selling, general and administrative expenses as a percentage of revenues decreased to 19% for the year ended December 31, 2007 from 20% for the year ended December 31, 2006, primarily driven by lower bonus costs as a percent of revenue and the Company leveraging its infrastructure. Bonus costs, as a percentage of service revenues, excluding reimbursable expenses, decreased to 1.6% for the year ended December 31, 2007 compared to 3.5% for the year ended December 31, 2006 due to increasingly challenging growth and profitability targets in 2007. Stock compensation expense, as a percentage of services revenues, excluding reimbursed expenses, increased to 2.4% for the year ended December 31, 2007 compared to 1.6% for the year ended December 31, 2006.

Depreciation. Depreciation expense increased 64% to \$1.6 million during 2007 from approximately \$0.9 million during 2006. The increase in depreciation expense is due to the addition of software programs, servers, and other computer equipment to enhance our technology infrastructure and support our growth, both organic and acquisition-related. Depreciation expense as a percentage of services revenue, excluding reimbursable expenses, was 0.8% and 0.7% for the years ended December 31, 2007 and 2006, respectively.

Amortization. Amortization increased 36% to \$4.7 million for the year ended December 31, 2007 from approximately \$3.5 million for the year ended December 31, 2006. The increase in amortization expense reflects the acquisition of intangibles acquired in 2006 and 2007, as well as the amortization of capitalized costs associated with internal use software. The valuations and estimated useful lives of acquired identifiable intangible assets are outlined in Note 6, Goodwill and Intangible Assets, of our consolidated financial statements.

Net Interest Income or Expense. We had interest income, net of interest expense, of \$172,000 for the year ended December 31, 2007 compared to interest expense, net of interest income, of \$407,000 during the year ended December 31, 2006. We repaid all outstanding debt in May 2007 and incurred no debt or interest expense during the rest of the fiscal year.

Provision for Income Taxes. We provided for federal, state and foreign income taxes at the applicable statutory rates adjusted for non-deductible expenses. Our effective tax rate decreased to 41.3% for the year ended December 31, 2007 from 43.2% for the year ended December 31, 2006. The effective income tax rate decreased as a result of the increased tax benefit of certain dispositions of incentive stock options by holders and a decrease in the state income taxes, net of the federal benefit.



Liquidity and Capital Resources

Selected measures of liquidity and capital resources are as follows (in millions):

	As of December 31,	
	2008	2007
Cash and cash equivalents	\$ 22.9	\$ 8.1
Working capital (including cash and cash equivalents)	\$ 56.2	\$ 41.5
Amounts available under credit facilities	\$ 49.9	\$ 49.8

#### Net Cash Provided By Operating Activities

Net cash provided by operations for the year ended December 31, 2008 was \$26.8 million compared to \$23.1 million for the year ended December 31, 2007. For the year ended December 31, 2008, net cash provided by operations consisted of net income of \$10.0 million plus non-cash charges such as stock compensation, amortization, depreciation, and impairment of intangible assets, of \$15.8 million plus net working capital reductions of \$1.0 million. The primary components of operating cash flows for the year ended December 31, 2007 are net income of \$16.2 million plus non-cash charges of \$12.0 million which were offset by investments in working capital of \$5.1 million. The Company's days sales outstanding as of December 31, 2008 decreased to 71 days from 73 days at December 31, 2007.

#### Net Cash Used in Investing Activities

For the year ended December 31, 2008, we used approximately \$0.8 million in cash to pay certain acquisition-related costs and \$1.5 million in cash to purchase equipment and develop certain software. For the year ended December 31, 2007, we used approximately \$26.8 million in cash, net of cash acquired, to acquire E Tech, Tier1, BoldTech, and ePairs. In addition, we used approximately \$2.2 million during 2007 to purchase equipment and develop certain software.

#### Net Cash Provided By Financing Activities

During the year ended December 31, 2008, we made no borrowings under our line of credit; however, we made payments of \$0.4 million in fees related to our new credit facility and we incurred \$0.9 million in income tax expense due to the decline in the Company's share price of underlying stock awards that were exercised or vested. We used \$9.2 million to repurchase shares of the Company's common stock through the stock repurchase program which was partially offset by \$0.9 million from exercises of stock options and sales of stock through our Employee Stock Purchase Plan. During the year ended December 31, 2007, we made payments of \$1.3 million on our long-term debt. Also, we received \$3.9 million from proceeds from exercises of stock options and sales under our Employee Stock Purchase Plan and we realized tax benefits related to stock option exercises and restricted stock vesting of \$6.9 million.

#### Availability of Funds from Bank Line of Credit Facilities

On May 30, 2008, the Company entered into a Credit Agreement (the "Credit Agreement") with Silicon Valley Bank ("SVB") and KeyBank National Association ("KeyBank"). The Agreement replaces the Company's Amended and Restated Loan and Security Agreement dated as of September 3, 2005 and further amended on September 29, 2006. The Credit Agreement provides for revolving credit borrowings up to a maximum principal amount of \$50 million, subject to a commitment increase of \$25 million. The Credit Agreement also allows for the issuance of letters of credit in the aggregate amount of up to \$500,000 at any one time; outstanding letters of credit reduce the credit available for revolving credit borrowings. The credit facility will be used for ongoing, general corporate purposes.

All outstanding amounts owed under the Credit Agreement become due and payable no later than the final maturity date of May 30, 2012. Borrowings under the credit facility bear interest at the Company's option at SVB's prime rate (4.00% on December 31, 2008) plus a margin ranging from 0.00% to 0.50% or one-month LIBOR (0.44% on December 31, 2008) plus a margin ranging from 2.50% to 3.00%. The additional margin amount is dependent on the amount of outstanding borrowings. As of December 31, 2008, the Company had \$49.9 million of available borrowing capacity. The Company will incur an annual commitment fee of 0.30% on the unused portion of the line of credit.

As of December 31, 2008, we were in compliance with all covenants under our credit facility and we expect to be in compliance during the next twelve months. Substantially all of our assets are pledged to secure the credit facility.

#### Stock Repurchase Program

In 2008, the Company's Board of Directors authorized the repurchase of up to \$20.0 million of the Company's common stock. As of December 31, 2008, \$9.2 million of Company common stock has been repurchased under this program and \$10.8 million of Company common stock may yet be purchased under such authorization.

The Company has established a written trading plan in accordance with Rule 10b5-1 of the Securities Exchange Act of 1934 (the "Exchange Act"), under which it will make a portion of its Company stock repurchases. Additional repurchases will be at times and in amounts as the Company deems appropriate and will be made through open market transactions in compliance with Rule 10b-18 of the Exchange Act, subject to market conditions, applicable legal requirements and other factors. The program expires on June 30, 2010.

## Lease Obligations

There were no material changes outside the ordinary course of our business in lease obligations or other contractual obligations in 2008.

## Shelf Registration Statement

In July 2008, we filed a shelf registration statement with the SEC to allow for offers and sales of our common stock from time to time. Approximately four million shares of common stock may be sold under this registration statement if we choose to do so. We determined that we currently have no intent to use the shelf registration to complete an offering.

## Contractual Obligations

We currently have one letter of credit for \$100,000 outstanding that serves as collateral to secure a facility lease. The letter of credit reduces the borrowings available under our line of credit.

We have incurred commitments to make future payments under contracts such as leases. Maturities under these contracts are set forth in the following table as of December 31, 2008 (in thousands):

Contractual Obligations	Total	Payments Due by Period			
		Less Than 1 Year	1-3 Years	3-5 Years	More Than 5 Years
Operating lease obligations	\$ 7,673	\$ 2,258	\$ 3,884	\$ 1,216	\$ 315
Total	\$ 7,673	\$ 2,258	\$ 3,884	\$ 1,216	\$ 315

See Note 9, Income Taxes, in Notes to Consolidated Financial Statements for information related to the Company's obligations for taxes.

## Conclusion

If our capital is insufficient to fund our activities in either the short or long term, we may need to raise additional funds. In the ordinary course of business, we may engage in discussions with various persons in connection with additional financing. If we raise additional funds through the issuance of equity securities, our existing stockholders' percentage ownership will be diluted. These equity securities may also have rights superior to our common stock. Additional debt or equity financing may not be available when needed or on satisfactory terms. If adequate funds are not available on acceptable terms, we may be unable to expand our services, respond to competition, pursue acquisition opportunities or continue our operations.

We believe that the current available funds, access to capital from our credit facility, and cash flows generated from operations will be sufficient to meet our working capital requirements and other capital needs for the next twelve months.

## Critical Accounting Policies

The Company's accounting policies are described in Note 2, Summary of Significant Accounting Policies, in Notes to Consolidated Financial Statements. The Company believes its most critical accounting policies include revenue recognition, accounting for goodwill and intangible assets, purchase accounting, accounting for stock-based

compensation, and income taxes.

#### Revenue Recognition and Allowance for Doubtful Accounts

Revenues are primarily derived from professional services provided on a time and materials basis. For time and material contracts, revenues are recognized and billed by multiplying the number of hours expended in the performance of the contract by the established billing rates. For fixed fee projects, revenues are generally recognized using the input method based on the ratio of hours expended to total estimated hours. Amounts invoiced to clients in excess of revenues recognized are classified as deferred revenues. On many projects the Company is also reimbursed for out-of-pocket expenses such as airfare, lodging and meals. These reimbursements are included as a component of revenues. Revenues from software and hardware sales are generally recorded on a gross basis based on the Company's role as principal in the transaction. On rare occasions, the Company enters into a transaction where it is not the principal. In these cases, revenue is recorded on a net basis.

Revenues are recognized when the following criteria are met: (1) persuasive evidence of the customer arrangement exists, (2) fees are fixed and determinable, (3) delivery and acceptance have occurred, and (4) collectibility is deemed probable. The Company's policy for revenue recognition in instances where multiple deliverables are sold contemporaneously to the same counterparty is in accordance with American Institute of Certified Public Accountants ("AICPA") Statement of Position 97-2, Software Revenue Recognition, Emerging Issues Task Force ("EITF") Issue No. 00-21, Revenue Arrangements with Multiple Deliverables, and SEC Staff Accounting Bulletin No. 104, Revenue Recognition. Specifically, if the Company enters into contracts for the sale of services and software or hardware, then the Company evaluates whether the services are essential to the functionality of the software or hardware and whether it has objective fair value evidence for each deliverable in the transaction. If the Company has concluded that the services to be provided are not essential to the functionality of the software or hardware and it can determine objective fair value evidence for each deliverable of the transaction, then it accounts for each deliverable in the transaction separately, based on the relevant revenue recognition policies. Generally, all deliverables of the Company's multiple element arrangements meet these criteria. The Company may provide multiple services under the terms of an arrangement and are required to assess whether one or more units of accounting are present. Fees are typically accounted for as one unit of accounting as fair value evidence for individual tasks or milestones is not available. The Company follows the guidelines discussed above in determining revenues; however, certain judgments and estimates are made and used to determine revenues recognized in any accounting period. If estimates are revised, material differences may result in the amount and timing of revenues recognized for a given period.

Revenues are presented net of taxes assessed by governmental authorities. Sales taxes are generally collected and subsequently remitted on all software and hardware sales and certain services transactions as appropriate.

Our allowance for doubtful accounts is based upon specific identification of likely and probable losses. Each accounting period, we evaluate accounts receivable for risk associated with a client's inability to make contractual payments, historical experience and other currently available information. Billed and unbilled receivables that are specifically identified as being at risk are provided for with a charge to revenue or bad debts as appropriate in the period the risk is identified. We use considerable judgment in assessing the ultimate realization of these receivables, including reviewing the financial stability of the client, evaluating the successful mitigation of service delivery disputes, and gauging current market conditions. If our evaluation of service delivery issues or a client's ability to pay is incorrect, we may incur future reductions to revenue or bad debt expense.

#### Goodwill, Other Intangible Assets and Impairment of Long-Lived Assets

Goodwill represents the excess purchase price over the fair value of net assets acquired, or net liabilities assumed, in a business combination. In accordance with SFAS 142, the Company performs an annual impairment test of goodwill. The Company evaluates goodwill as of October 1 each year and more frequently if events or changes in circumstances indicate that goodwill might be impaired. As required by SFAS 142, the impairment test is accomplished using a two-step approach. The first step screens for impairment and, when impairment is indicated, a second step is employed to measure the impairment. The Company also reviews other factors to determine the likelihood of impairment.

The Company's fair value was determined by weighting the results of two valuation methods: 1) market capitalization based on the average price of the Company's common stock, including a control premium, for a reasonable period of time prior to the evaluation date (generally 15 to 30 days) and 2) a discounted cash flow model. The fair value calculated using the Company's average common stock price (including a control premium) was weighted 40% while the value calculated by the discounted cash flow model was weighted 60% in the Company's determination of its overall fair value. Management believes that while the use of its average common stock price, plus a control premium, may be considered the best evidence of fair value in SFAS 142, the declines in the Company's

stock price, and in the market overall, are not consistently aligned with the Company's financial results or outlook. The discounted cash flow approach allows the Company to calculate its fair value based on operating performance and meaningful financial metrics.

A key assumption used in the calculation of the Company's fair value using its average common stock price was the consideration of a control premium. The Company reviewed industry premium data and determined an appropriate control premium for its analysis based on the low end of any premium received in transactions over the past several years.

Significant estimates used in the discounted cash flow model included projections of revenue growth, net income margins, discount rate, and terminal business value. The forecasts of revenue growth and net income margins are based upon management's long-term view of the business and are used by senior management and the Board of Directors to evaluate operating performance. The discount rate utilized was estimated using the weighted average cost of capital for the Company's industry. The terminal business value was determined by applying a growth factor to the latest year for which a forecast exists.

Other intangible assets include customer relationships, non-compete arrangements and internally developed software, which are being amortized over the assets' estimated useful lives using the straight-line method. Estimated useful lives range from three to eight years. Amortization of customer relationships, non-compete arrangements and internally developed software are considered operating expenses and are included in "Amortization" in the accompanying Consolidated Statements of Operations. The Company periodically reviews the estimated useful lives of its identifiable intangible assets, taking into consideration any events or circumstances that might result in a lack of recoverability or revised useful life.

The Company's annual goodwill impairment test was performed as of October 1, 2008. The Company's fair value as of the annual testing date exceeded its book value and consequently, no impairment was indicated.

During the fourth quarter of 2008, the Company determined that the continuous trading of its common stock below book value was a possible indicator of impairment to goodwill or long-lived assets as defined under SFAS 142 and SFAS 144, triggering the necessity of impairment tests as of December 31, 2008. In accordance with SFAS 142, the Company tested its long-lived assets for impairment prior to performing an interim test of goodwill impairment. Assets were grouped together to test recoverability based on the lowest level of identifiable cash flows directly attributable to those assets. Fair values of the identified asset groups were calculated using a discounted cash flow model. Key assumptions used in the discounted cash flow model for calculating the fair value of the asset groups were similar in nature to those described above. Based on the valuations performed, the Company determined that the cash flows of one of the identified asset groups would not be sufficient to recover the group's carrying amount. Consequently, we recorded an impairment of \$1.6 million primarily related to customer relationship intangible assets acquired from E Tech. The value of these relationships was affected primarily by the loss of a key customer acquired by E Tech, which caused cash flows from the acquired relationships to be lower than originally projected.

After recording the impairment of the E Tech customer relationships intangible asset, the Company performed the first step of the goodwill impairment test and based on the weighted average of market capitalization, including a control premium, and discounted cash flow analysis, goodwill was not impaired as of December 31, 2008. Changes in management intentions, market conditions, our stock value, operating performance, and other similar circumstances could affect the assumptions used in the future for the impairment tests described above. Changes in the assumptions could result in future impairment charges that could be material to our financial results in any given period.

Subsequent to December 31, 2008 our stock price has declined. Accordingly, the Company will continue to evaluate the carrying value of the remaining goodwill and intangible assets to determine whether the decline in stock price is an indication that there is a triggering event that may require the Company to perform an interim impairment test and record impairment charges to earnings, which could adversely affect the Company's financial results.

#### Purchase Accounting

We allocate the purchase price of our acquisitions to the assets and liabilities acquired, including identifiable intangible assets, based on their respective fair values at the date of acquisition. Such fair market value assessments require significant judgments and estimates that can change materially as additional information becomes available. The purchase price is allocated to intangibles based on management's estimate and an independent valuation. Management finalizes the purchase price allocation within twelve months of the acquisition date as certain initial accounting estimates are resolved.

#### Accounting for Stock-Based Compensation



The Company estimates the fair value of stock option awards on the date of grant utilizing a modified Black-Scholes option pricing model. The Black-Scholes option valuation model was developed for use in estimating the fair value of short-term traded options that have no vesting restrictions and are fully transferable. However, certain assumptions used in the Black-Scholes model, such as expected term, can be adjusted to incorporate the unique characteristics of the Company's stock option awards. Option valuation models require the input of somewhat subjective assumptions including expected stock price volatility and expected term. The Company believes it is unlikely that materially different estimates for the assumptions used in estimating the fair value of stock options granted would be made based on the conditions suggested by actual historical experience and other data available at the time estimates were made. Restricted stock awards are valued at the price of our common stock on the date of the grant.

#### Income Taxes

To record income tax expense, we are required to estimate our income taxes in each of the jurisdictions in which we operate. In addition, income tax expense at interim reporting dates requires us to estimate our expected effective tax rate for the entire year. This involves estimating our actual current tax liability together with assessing temporary differences that result in deferred tax assets and liabilities and expected future tax rates.

## Recent Accounting Pronouncements

Effective January 1, 2008, the Company adopted SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, Including an amendment of SFAS No. 115 (“SFAS 159”). SFAS 159 permits companies to choose to measure many financial instruments and certain other items at fair value. SFAS 159 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The adoption of SFAS 159 did not have a material impact on the Company’s consolidated financial statements.

Effective January 1, 2008, the Company adopted SFAS No. 157, Fair Value Measurements (“SFAS 157”). In February 2008, the FASB issued Staff Position No. 157-2, Effective Date of FASB Statement No. 157 (“FSP 157-2”), which delayed the effective date of SFAS 157 for certain nonfinancial assets and liabilities, including fair value measurements under SFAS No. 141, Business Combinations (“SFAS 141”) and SFAS 142, to fiscal years beginning after November 15, 2008. Therefore, the Company has adopted the provisions of SFAS 157 with respect to its financial assets and liabilities only. SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. Fair value is defined under SFAS 157 as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value under SFAS 157 must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy based on the following three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value:

- Level 1 – Quoted prices in active markets for identical assets or liabilities.
- Level 2 – Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

As of December 31, 2008, the Company did not hold any assets or liabilities that are required to be measured at fair value on a recurring basis, and therefore the adoption of the respective provisions of SFAS 157 did not have an impact on the Company’s consolidated financial statements. On January 1, 2009, the Company will implement the previously deferred provisions of SFAS 157 for nonfinancial assets and liabilities recorded at fair value, as required. Management does not believe that the remaining provisions will have a material effect on the Company’s consolidated financial statements when they become effective.

In May 2008, the FASB issued SFAS No. 162, The Hierarchy of Generally Accepted Accounting Principles (“SFAS 162”). The statement is intended to improve financial reporting by identifying a consistent hierarchy for selecting accounting principles to be used in preparing financial statements that are prepared in accordance with generally accepted accounting principles. Unlike Statement on Auditing Standards (“SAS”) No. 69, The Meaning of Present Fairly in Conformity With GAAP, SFAS 162 is directed to the entity rather than the auditor. The statement was effective November 15, 2008, after approval by the SEC which occurred in September 2008. The application of this statement did not have a material impact on the Company’s consolidated financial statements.

In April 2008, the FASB issued FASB Staff Position No. 142-3, Determination of the Useful Life of Intangible Assets (“FSP 142-3”). FSP 142-3 requires companies estimating the useful life of a recognized intangible asset to consider their historical experience in renewing or extending similar arrangements or, in the absence of historical experience, to consider assumptions that market participants would use about renewal or extension as adjusted for

SFAS 142's entity-specific factors. FSP 142-3 is effective for financial statements issued for fiscal years beginning after December 15, 2008. Adoption of this statement is not expected to have a material impact on the Company's consolidated financial statements when it becomes effective.

In December 2007, FASB issued SFAS No. 141 (revised 2007), Business Combinations ("SFAS 141R"), which is a revision of SFAS 141. SFAS 141R establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed and any noncontrolling interest in the acquiree, recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase, and determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. The revised statement will require, among other things, that transaction costs be expensed instead of recognized as purchase price. SFAS 141R applies prospectively to business combinations for which the acquisition date is on or after January 1, 2009.

#### Off-Balance Sheet Arrangements

The Company currently has no off-balance sheet arrangements, except operating lease commitments as disclosed in Note 10, Commitments and Contingencies.

Item Quantitative and Qualitative Disclosures About Market Risk.  
7A.

We are exposed to market risks related to changes in foreign currency exchange rates and interest rates. We believe our exposure to market risks is immaterial.

Exchange Rate Sensitivity

During the year ended December 31, 2008, \$2.5 million and \$2.7 million of our total revenues were attributable to our Canadian operations and revenues generated in Europe, respectively. Our exposure to changes in foreign currency rates primarily arises from short-term intercompany transactions with our Canadian, Chinese, and Indian subsidiaries and from client receivables denominated in other than our functional currency. Our foreign subsidiaries incur a significant portion of their expenses in their applicable currency as well, which helps minimize our risk of exchange rate fluctuations. Based on the amount of revenues attributed to clients in Canada and Europe during the year ended December 31, 2008, this exchange rate risk will not have a material impact on our financial position or results of operations.

Interest Rate Sensitivity

We had unrestricted cash and cash equivalents totaling \$22.9 million and \$8.1 million at December 31, 2008 and December 31, 2007, respectively. These amounts were invested primarily in money market funds. The unrestricted cash and cash equivalents are held for working capital purposes. We do not enter into investments for trading or speculative purposes. Due to the short-term nature of these investments, we believe that we do not have any material exposure to changes in the fair value of our investment portfolio as a result of changes in interest rates. Declines in interest rates, however, will reduce future investment income.

## Item Financial Statements and Supplementary Data.

8.

PERFICIENT, INC.  
CONSOLIDATED BALANCE SHEETS  
AS OF DECEMBER 31, 2008 AND 2007

	December 31,	
	2008	2007
	(In thousands, except share information)	
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 22,909	\$ 8,070
Accounts and note receivable, net of allowance for doubtful accounts of \$1,497 in 2008 and \$1,475 in 2007	47,584	50,855
Prepaid expenses	1,374	1,182
Other current assets	3,157	4,142
Total current assets	75,024	64,249
Property and equipment, net	2,345	3,226
Goodwill	104,178	103,686
Intangible assets, net	11,456	17,653
Other non-current assets	1,244	1,178
Total assets	\$ 194,247	\$ 189,992
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 4,509	\$ 4,160
Other current liabilities	14,339	18,550
Total current liabilities	18,848	22,710
Deferred income taxes	--	1,549
Other non-current liabilities	581	171
Total liabilities	\$ 19,429	\$ 24,430
Commitments and contingencies (see Notes 4 and 10)		
Stockholders' equity:		
Common stock (\$0.001 par value per share; 50,000,000 shares authorized and 30,350,700 shares issued and 28,502,400 shares outstanding as of December 31, 2008; 29,423,296 shares issued and outstanding as of December 31, 2007)	\$ 30	\$ 29
Additional paid-in capital	197,653	188,998
Accumulated other comprehensive loss	(338)	(117)
Treasury stock, at cost (1,848,300 shares as of December 31, 2008)	(9,179)	--
Accumulated deficit	(13,348)	(23,348)
Total stockholders' equity	174,818	165,562
Total liabilities and stockholders' equity	\$ 194,247	\$ 189,992

See accompanying notes to consolidated financial statements.



PERFICIENT, INC.  
CONSOLIDATED STATEMENTS OF OPERATIONS  
FOR THE YEARS ENDED DECEMBER 31, 2008, 2007 AND 2006

	Year Ended December 31,		
	2008	2007	2006
	(In thousands, except per share information)		
Revenues:			
Services	\$ 207,480	\$ 191,395	\$ 137,722
Software and hardware	10,713	14,243	14,435
Reimbursable expenses	13,295	12,510	8,769
Total revenues	231,488	218,148	160,926
Cost of revenues (exclusive of depreciation and amortization, shown separately below):			
Project personnel costs	131,019	114,692	84,161
Software and hardware costs	8,639	11,982	12,118
Reimbursable expenses	13,295	12,510	8,769
Other project related expenses	5,033	3,274	2,122
Total cost of revenues	157,986	142,458	107,170
Gross margin	73,502	75,690	53,756
Selling, general and administrative	47,242	41,963	32,268
Depreciation	2,139	1,553	948
Amortization	4,810	4,712	3,458
Impairment of intangible assets	1,633	--	--
Income from operations	17,678	27,462	17,082
Interest income	555	239	102
Interest expense	(27)	(67)	(509)
Other income (expense)	(915)	20	174
Income before income taxes	17,291	27,654	16,849
Provision for income taxes	7,291	11,424	7,282
Net income	\$ 10,000	\$ 16,230	\$ 9,567
Basic net income per share	\$ 0.34	\$ 0.58	\$ 0.38
Diluted net income per share	\$ 0.33	\$ 0.54	\$ 0.35
Shares used in computing basic net income per share	29,412,329	27,998,093	25,033,337
Shares used in computing diluted net income per share	30,350,616	30,121,962	27,587,449

See accompanying notes to consolidated financial statements.





PERFICIENT, INC.  
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY  
FOR THE YEARS ENDED DECEMBER 31, 2008, 2007 AND 2006  
(In thousands)

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Accumulated Other Comprehensive Loss	Treasury Stock	Accumulated Deficit	Total Stockholders' Equity
Balance at December 31, 2005	23,295	\$ 23	\$ 115,120	\$ (87)	\$ --	\$ (49,145)	\$ 65,911
Bay Street, Insolexen, and EGG acquisition purchase accounting adjustments	1,499	2	17,989	--	--	--	17,991
Warrants exercised	145	--	146	--	--	--	146
Stock options exercised	1,672	2	4,001	--	--	--	4,003
Purchases of stock under the Employee Stock Purchase Plan	6	--	86	--	--	--	86
Tax benefit of stock option exercises and restricted stock vesting	--	--	6,554	--	--	--	6,554
Stock compensation	83	--	3,132	--	--	--	3,132
Foreign currency translation adjustment	--	--	--	(38)	--	--	(38)
Net income	--	--	--	--	--	9,567	9,567
Total comprehensive income	--	--	--	--	--	--	9,529
Balance at December 31, 2006	26,700	\$ 27	\$ 147,028	\$ (125)	\$ --	\$ (39,578)	\$ 107,352
E Tech, Tier1, BoldTech, and ePairs acquisition purchase accounting adjustments	1,250	1	24,975	--	--	--	24,976
Stock options exercised	1,160	1	3,696	--	--	--	3,697
Purchases of stock under the Employee Stock Purchase Plan	11	--	206	--	--	--	206
Tax benefit of stock option exercises and restricted stock vesting	--	--	6,889	--	--	--	6,889

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Stock compensation	302	--	6,204	--	--	--	6,204
Foreign currency translation adjustment	--	--	--	8	--	--	8
Net income	--	--	--	--	--	16,230	16,230
Total comprehensive income	--	--	--	--	--	--	16,238
Balance at December 31, 2007	29,423	\$ 29	\$ 188,998	\$ (117)	\$ --	\$ (23,348)	\$ 165,562
E Tech and ePairs acquisition purchase accounting adjustments	(19)	--	(290)	--	--	--	(290)
Stock options exercised	338	1	726	--	--	--	727
Purchases of stock under the Employee Stock Purchase Plan	29	--	196	--	--	--	196
Tax expense of stock option exercises and restricted stock vesting	--	--	(922)	--	--	--	(922)
Stock compensation and retirement savings plan contributions	579	--	8,945	--	--	--	8,945
Purchases of treasury stock	(1,848)	--	--	--	(9,179)	--	(9,179)
Foreign currency translation adjustment	--	--	--	(221)	--	--	(221)
Net income	--	--	--	--	--	10,000	10,000
Total comprehensive income	--	--	--	--	--	--	9,779
Balance at December 31, 2008	28,502	\$ 30	\$ 197,653	\$ (338)	\$ (9,179)	\$ (13,348)	\$ 174,818

See accompanying notes to consolidated financial statements.

PERFICIENT, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED DECEMBER 31, 2008, 2007 AND 2006

	Year Ended December 31,		
	2008	2007	2006
	(In thousands)		
<b>OPERATING ACTIVITIES</b>			
Net income	\$ 10,000	\$ 16,230	\$ 9,567
Adjustments to reconcile net income to net cash provided by operations:			
Depreciation	2,139	1,553	948
Amortization	4,810	4,712	3,458
Impairment of intangible assets	1,633		
Deferred income taxes	(1,769)	(495)	1,393
Non-cash stock compensation and retirement savings plan contributions	8,945	6,204	3,132
Non-cash interest expense	--	--	6
Changes in operating assets and liabilities, net of acquisitions:			
Accounts and note receivable	3,081	(1,589)	(5,771)
Other assets	354	3,256	(294)
Accounts payable	399	(1,694)	1,251
Other liabilities	(2,824)	(5,126)	(543)
Net cash provided by operating activities	26,768	23,051	13,147
<b>INVESTING ACTIVITIES</b>			
Purchase of property and equipment	(1,320)	(2,035)	(1,518)
Capitalization of software developed for internal use	(185)	(181)	(136)
Cash paid for acquisitions and related costs	(836)	(26,774)	(17,210)
Payments on Javelin notes	--	--	(250)
Net cash used in investing activities	(2,341)	(28,990)	(19,114)
<b>FINANCING ACTIVITIES</b>			
Proceeds from short-term borrowings	--	11,900	34,900
Payments on short-term borrowings	--	(11,900)	(38,900)
Payments on long-term debt	--	(1,338)	(1,338)
Payments for credit facility financing fees	(420)	--	--
Tax benefit (expense) of stock option exercises and restricted stock vesting	(922)	6,889	6,554
Proceeds from the exercise of stock options and Employee Stock Purchase Plan	923	3,903	4,089
Proceeds from the exercise of warrants	--	--	146
Purchases of treasury stock	(9,179)	--	--
Net cash provided by financing activities	(9,598)	9,454	5,451
Effect of exchange rate on cash and cash equivalents	10	6	(31)
Change in cash and cash equivalents	14,839	3,521	(547)
Cash and cash equivalents at beginning of period	8,070	4,549	5,096
Cash and cash equivalents at end of period	\$ 22,909	\$ 8,070	\$ 4,549

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Supplemental disclosures:

Cash paid for interest	\$	15	\$	40	\$	540
Cash paid for income taxes	\$	10,206	\$	3,680	\$	3,156
Non-cash activities:						
Stock issued for purchase of businesses (stock reacquired for escrow claim)	\$	(290)	\$	24,976	\$	17,991
Change in goodwill	\$	492	\$	(1,957)	\$	318
Write-off of deferred offering costs	\$	(943)	\$	--	\$	--

See accompanying notes to consolidated financial statements.

PERFICIENT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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1. Description of Business and Principles of Consolidation

Perficient, Inc. (the "Company") is an information technology consulting firm. The Company helps its clients use Internet-based technologies to make their businesses more responsive to market opportunities and threats, strengthen relationships with customers, suppliers and partners, improve productivity and reduce information technology costs. The Company designs, builds and delivers solutions using a core set of middleware software products developed by third party vendors. The Company's solutions enable its clients to meet the changing demands of an increasingly global, Internet-driven and competitive marketplace.

The Company is incorporated in Delaware. The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All material intercompany accounts and transactions have been eliminated in consolidation.

2. Summary of Significant Accounting Policies

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 reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates, and such differences could be material to the financial statements.

Reclassification

The Company has reclassified the presentation of certain prior period information to conform to the current year presentation.

Revenue Recognition

Revenues are primarily derived from professional services provided on a time and materials basis. For time and material contracts, revenues are recognized and billed by multiplying the number of hours expended in the performance of the contract by the established billing rates. For fixed fee projects, revenues are generally recognized using the input method based on the ratio of hours expended to total estimated hours. Amounts invoiced to clients in excess of revenues recognized are classified as deferred revenues. On many projects the Company is also reimbursed for out-of-pocket expenses such as airfare, lodging and meals. These reimbursements are included as a component of revenues. Revenues from software and hardware sales are generally recorded on a gross basis based on the Company's role as principal in the transaction. On rare occasions, the Company enters into a transaction where it is not the principal. In these cases, revenue is recorded on a net basis.

Revenues are recognized when the following criteria are met: (1) persuasive evidence of the customer arrangement exists, (2) fees are fixed and determinable, (3) delivery and acceptance have occurred, and (4) collectibility is deemed probable. The Company's policy for revenue recognition in instances where multiple deliverables are sold contemporaneously to the same counterparty is in accordance with American Institute of Certified Public Accountants

(“AICPA”) Statement of Position 97-2, Software Revenue Recognition, Emerging Issues Task Force (“EITF”) Issue No. 00-21, Revenue Arrangements with Multiple Deliverables, and SEC Staff Accounting Bulletin No. 104, Revenue Recognition. Specifically, if the Company enters into contracts for the sale of services and software or hardware, then the Company evaluates whether the services are essential to the functionality of the software or hardware and whether it has objective fair value evidence for each deliverable in the transaction. If the Company has concluded that the services to be provided are not essential to the functionality of the software or hardware and it can determine objective fair value evidence for each deliverable of the transaction, then it accounts for each deliverable in the transaction separately, based on the relevant revenue recognition policies. Generally, all deliverables of the Company’s multiple element arrangements meet these criteria. The Company may provide multiple services under the terms of an arrangement and are required to assess whether one or more units of accounting are present. Fees are typically accounted for as one unit of accounting as fair value evidence for individual tasks or milestones is not available. The Company follows the guidelines discussed above in determining revenues; however, certain judgments and estimates are made and used to determine revenues recognized in any accounting period. If estimates are revised, material differences may result in the amount and timing of revenues recognized for a given period.

Revenues are presented net of taxes assessed by governmental authorities. Sales taxes are generally collected and subsequently remitted on all software and hardware sales and certain services transactions as appropriate.

PERFICIENT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)  
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#### Cash and Cash Equivalents

Cash equivalents consist primarily of cash deposits and investments with original maturities of 90 days or less when purchased.

#### Property and Equipment

Property and equipment are recorded at cost. Depreciation of property and equipment is computed using the straight-line method over the useful lives of the assets (generally one to five years). Leasehold improvements are amortized over the shorter of the life of the lease or the estimated useful life of the assets.

#### Goodwill, Other Intangible Assets and Impairment of Long-Lived Assets

Goodwill represents the excess purchase price over the fair value of net assets acquired, or net liabilities assumed, in a business combination. In accordance with Statement of Financial Accounting Standards (“SFAS”) No. 142, Goodwill and Other Intangible Assets (“SFAS 142”), the Company performs an annual impairment test of goodwill. The Company evaluates goodwill as of October 1 each year and more frequently if events or changes in circumstances indicate that goodwill might be impaired. As required by SFAS 142, the impairment test is accomplished using a two-step approach. The first step of the goodwill impairment test compares the fair value of a reporting unit with its carrying amount, including goodwill. If, based on the second step, it is determined that the implied fair value of the goodwill of the reporting unit is less than the carrying value, goodwill is considered impaired.

Other intangible assets include customer relationships, non-compete arrangements and internally developed software, which are being amortized over the assets’ estimated useful lives using the straight-line method. Estimated useful lives range from three to eight years. Amortization of customer relationships, non-compete arrangements and internally developed software are considered operating expenses and are included in “Amortization” in the accompanying Consolidated Statements of Operations. The Company periodically reviews the estimated useful lives of its identifiable intangible assets, taking into consideration any events or circumstances that might result in a lack of recoverability or revised useful life.

During the fourth quarter of 2008, the Company determined that the continuous trading of its common stock below book value was a possible indicator of impairment to goodwill or long-lived assets as defined under SFAS 142 and SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets (“SFAS 144”), triggering the necessity of impairment tests as of December 31, 2008. As a result of the tests performed, the Company recorded a \$1.6 million impairment primarily related to the customer relationships we acquired from e tech solutions, Inc. (“E Tech”). The value of these relationships was affected primarily by the loss of a key customer acquired by E Tech, which caused cash flows from the acquired relationships to be lower than originally projected.

#### Income Taxes

The Company accounts for income taxes in accordance with SFAS No. 109, Accounting for Income Taxes (“SFAS 109”), and Financial Accounting Standards Interpretation No. 48, Accounting for Uncertainty in Income Taxes – an interpretation of SFAS 109 (“FIN 48”). SFAS 109 prescribes the use of the liability method whereby deferred tax asset and liability account balances are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences

are expected to reverse. Deferred tax assets are subject to tests of recoverability. A valuation allowance is provided for such deferred tax assets to the extent realization is not judged to be more likely than not. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, treatment of interest and penalties, and disclosure of such positions. The Company adopted the provisions of FIN 48 on January 1, 2007 as required and such adoption did not have a material impact to the consolidated financial statements.



PERFICIENT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)  
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#### Earnings Per Share

Basic earnings per share is computed by dividing net income available to common stockholders by the weighted-average number of common shares outstanding during the period. Diluted earnings per share includes the weighted average number of common shares outstanding and the number of equivalent shares which would be issued related to the stock options, unvested restricted stock, and warrants using the treasury method, unless such additional equivalent shares are anti-dilutive.

#### Stock-Based Compensation

Effective January 1, 2006, the Company adopted the provisions of SFAS No. 123R (As Amended), Share Based Payment ("SFAS 123R"), using the modified prospective application transition method. Under this method, compensation cost for the portion of awards for which the requisite service has not yet been rendered that are outstanding as of the adoption date is recognized over the remaining service period. The compensation cost for that portion of awards is based on the grant-date fair value of those awards as calculated for pro-forma disclosures under SFAS No. 123. All new awards and awards that are modified, repurchased, or cancelled after the adoption date are accounted for under the provisions of SFAS 123R. Prior periods are not restated under this transition method. The Company recognizes share-based compensation ratably using the straight-line attribution method over the requisite service period. In addition, pursuant to SFAS 123R, the Company is required to estimate the amount of expected forfeitures when calculating share-based compensation, instead of accounting for forfeitures as they occur, which was the Company's practice prior to the adoption of SFAS 123R.

#### Deferred Rent

Certain of the Company's operating leases contain predetermined fixed escalations of minimum rentals during the original lease terms. For these leases, the Company recognizes the related rental expense on a straight-line basis over the life of the lease and records the difference between the amounts charged to operations and amounts paid as accrued rent expense.

#### Fair Value of Financial Instruments

Cash equivalents, accounts receivable, accounts payable, other accrued liabilities, and debt are stated at amounts which approximate fair value due to the near term maturities of these instruments.

#### Treasury Stock

The Company uses the cost method to account for repurchases of its own stock.

#### Segment Information

The Company operates as one reportable operating segment according to SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, which establishes standards for the way that business enterprises report information about operating segments. The chief operating decision maker formulates decisions about how to allocate resources and assess performance based on consolidated financial results. The Company also has one

reporting unit for purposes of the SFAS 142 impairment analysis discussed above.

#### Recently Issued Accounting Standards

Effective January 1, 2008, the Company adopted SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, Including an amendment of SFAS No. 115 (“SFAS 159”). SFAS 159 permits companies to choose to measure many financial instruments and certain other items at fair value. SFAS 159 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The adoption of SFAS 159 did not have a material impact on the Company’s consolidated financial statements.

PERFICIENT, INC.  
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Effective January 1, 2008, the Company adopted SFAS No. 157, Fair Value Measurements (“SFAS 157”). In February 2008, the FASB issued Staff Position No. 157-2, Effective Date of FASB Statement No. 157 (“FSP 157-2”), which delayed the effective date of SFAS 157 for certain nonfinancial assets and liabilities, including fair value measurements under SFAS No. 141, Business Combinations (“SFAS 141”) and SFAS 142, to fiscal years beginning after November 15, 2008. Therefore, the Company has adopted the provisions of SFAS 157 with respect to its financial assets and liabilities only. SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. Fair value is defined under SFAS 157 as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value under SFAS 157 must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy based on the following three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value:

- Level 1 – Quoted prices in active markets for identical assets or liabilities.
- Level 2 – Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

As of December 31, 2008, the Company did not hold any assets or liabilities that are required to be measured at fair value on a recurring basis, and therefore the adoption of the respective provisions of SFAS 157 did not have an impact on the Company’s consolidated financial statements. On January 1, 2009, the Company will implement the previously deferred provisions of SFAS 157 for nonfinancial assets and liabilities recorded at fair value, as required. Management does not believe that the remaining provisions will have a material effect on the Company’s consolidated financial statements when they become effective.

In May 2008, the FASB issued SFAS No. 162, The Hierarchy of Generally Accepted Accounting Principles (“SFAS 162”). The statement is intended to improve financial reporting by identifying a consistent hierarchy for selecting accounting principles to be used in preparing financial statements that are prepared in accordance with generally accepted accounting principles. Unlike Statement on Auditing Standards (“SAS”) No. 69, The Meaning of Present Fairly in Conformity With GAAP, SFAS 162 is directed to the entity rather than the auditor. The statement was effective November 15, 2008, after approval by the SEC which occurred in September 2008. The application of this statement did not have a material impact on the Company’s consolidated financial statements.

In April 2008, the FASB issued FASB Staff Position No. 142-3, Determination of the Useful Life of Intangible Assets (“FSP 142-3”). FSP 142-3 requires companies estimating the useful life of a recognized intangible asset to consider their historical experience in renewing or extending similar arrangements or, in the absence of historical experience, to consider assumptions that market participants would use about renewal or extension as adjusted for SFAS 142’s entity-specific factors. FSP 142-3 is effective for financial statements issued for fiscal years beginning after December 15, 2008. Adoption of this statement is not expected to have a material impact on the Company’s consolidated financial statements when it becomes effective.

In December 2007, FASB issued SFAS No. 141 (revised 2007), Business Combinations (“SFAS 141R”), which is a revision of SFAS 141. SFAS 141R establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed and any noncontrolling interest in the acquiree, recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase, and determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. The revised statement will require, among other things, that transaction costs be expensed instead of recognized as purchase price. SFAS 141R applies prospectively to business combinations for which the acquisition date is on or after January 1, 2009.

PERFICIENT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)  
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### 3. Net Income Per Share

The following table presents the calculation of basic and diluted net income per share (in thousands, except per share information):

	Year Ended December 31,		
	2008	2007	2006
Net income	\$ 10,000	\$ 16,230	\$ 9,567
Basic:			
Weighted-average shares of common stock outstanding	29,338	27,442	23,783
Weighted-average shares of common stock subject to contingency (i.e., restricted stock)	74	556	1,250
Shares used in computing basic net income per share	29,412	27,998	25,033
Effect of dilutive securities:			
Stock options	835	1,707	2,281
Warrants	6	8	74
Restricted stock subject to vesting	98	409	199
Shares used in computing diluted net income per share (1)	30,351	30,122	27,587
Basic net income per share	\$ 0.34	\$ 0.58	\$ 0.38
Diluted net income per share	\$ 0.33	\$ 0.54	\$ 0.35

(1) As of December 31, 2008 approximately 0.4 million options for shares and 1.9 million shares of restricted stock were excluded. These shares were excluded from shares used in computing diluted net income per share because they would have had an anti-dilutive effect.

### 4. Concentration of Credit Risk and Significant Customers

Cash and accounts receivable potentially expose the Company to concentrations of credit risk. Cash is placed with highly rated financial institutions. The Company provides credit, in the normal course of business, to its customers. The Company generally does not require collateral or up-front payments. The Company performs periodic credit evaluations of its customers and maintains allowances for potential credit losses. Customers can be denied access to services in the event of non-payment. A substantial portion of the services the Company provides are built on IBM WebSphere® platforms and a significant number of its clients are identified through joint selling opportunities conducted with IBM and through sales leads obtained from the relationship with IBM. Revenues from IBM accounted for approximately 6% of total revenues for 2008 and 8% of total revenues for 2007 and 2006. Accounts receivable from IBM accounted for approximately 6%, 4%, and 9% of total accounts receivable as of December 31, 2008, 2007, and 2006, respectively. While the dollar amount of revenues from IBM has remained relatively constant over the past three years, the percentage of total revenues from IBM has decreased as a result of the Company's growth and corresponding customer diversification. Due to the Company's significant fixed operating expenses, the loss of sales to IBM or any significant customer could result in the Company's inability to generate net income or positive cash flow from operations for some time in the future.

### 5. Employee Benefit Plan

The Company has a qualified 401(k) profit sharing plan available to full-time employees who meet the plan's eligibility requirements. This defined contribution plan permits employees to make contributions up to maximum limits allowed by the Internal Revenue Code. The Company, at its discretion, matches a portion of the employee's contribution under a predetermined formula based on the level of contribution and years of vesting services. In 2008, the Company made matching contributions of 50% (25% in cash and 25% in Company stock) of the first 6% of eligible compensation deferred by the participant, totaling \$1.0 million. The Company made matching contributions equal to 25% of the first 6% of employee contributions totaling approximately \$0.8 million and \$0.5 million during 2007 and 2006, respectively. All matching contributions vest over a three year period of service.

In 2007, the Company initiated a deferred compensation plan for officers, directors, and certain sales personnel. The plan is designed to allow eligible participants to accumulate additional income through a nonqualified deferred compensation plan that enables them to make elective deferrals of compensation to which they will become entitled in the future. As of December 31, 2008, the deferred compensation liability balance was \$0.6 million compared to \$0.2 million as of December 31, 2007.

PERFICIENT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)  
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## 6. Goodwill and Intangible Assets

The Company performed its annual impairment test of goodwill as of October 1, 2008. As required by SFAS 142, the impairment test is accomplished using a two-step approach. The first step screens for impairment and, when impairment is indicated, a second step is employed to measure the impairment. The Company also reviews other factors to determine the likelihood of impairment. Based on the test performed, the Company's fair value as of the annual testing date exceeded its book value and consequently, no impairment was indicated.

The Company's fair value was determined by weighting the results of two valuation methods: 1) market capitalization based on the average price of the Company's common stock, including a control premium, for a reasonable period of time prior to the evaluation date (generally 15 to 30 days) and 2) a discounted cash flow model. The fair value calculated using the Company's average common stock price (including a control premium) was weighted 40% while the value calculated by the discounted cash flow model was weighted 60% in the Company's determination of its overall fair value.

During the fourth quarter of 2008, the Company determined that the continuous trading of its common stock below book value was a possible indicator of impairment to goodwill or long-lived assets as defined under SFAS 142 and SFAS 144, triggering the necessity of impairment tests as of December 31, 2008. Fair values for long-lived asset testing were calculated using a discounted cash flow model for the asset group. Significant estimates used in the discounted cash flow model included projections of revenue growth, earnings margins, and discount rate. The discount rate utilized was estimated using the weighted average cost of capital for the Company's industry.

The discounted cash flow model yielded a fair value lower than the asset group's carrying amount and consequently, the Company recorded a \$1.6 million impairment of the customer relationships we acquired from etech solutions, Inc. ("E Tech"). The value of these relationships was affected primarily by the loss of a key customer acquired by E Tech, which caused cash flows from the asset group to be lower than originally projected. After recording the impairment of the E Tech customer relationships intangible asset, the Company performed the first step of the goodwill impairment test and based on the weighted average of market capitalization, including a control premium, and discounted cash flow analysis, goodwill was not impaired as of December 31, 2008.

Subsequent to December 31, 2008 our stock price has declined. Accordingly, the Company will continue to evaluate the carrying value of the remaining goodwill and intangible assets to determine whether the decline in stock price is an indication that there is a triggering event that may require the Company to perform an interim impairment test and record impairment charges to earnings, which could adversely affect the Company's financial results.

### Goodwill

Activity related to goodwill consisted of the following (in thousands):

	2008	2007
Balance, beginning of year	\$ 103,686	\$ 69,170
Purchase price allocated to goodwill upon acquisition (Note 13)	--	35,301
Adjustments to preliminary purchase price allocations for acquisitions	1,088	1,172
Adjustment to E Tech purchase price allocation for escrow claim	(378)	--
Utilization of net operating loss carryforwards associated with acquisitions	(218)	(1,957)

Balance, end of year	\$ 104,178	\$ 103,686
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PERFICIENT, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)  
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## Intangible Assets with Definite Lives

Following is a summary of the Company's intangible assets that are subject to amortization (in thousands):

	Year ended December 31,					
	2008			2007		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Customer relationships	\$ 18,013	\$ (7,693)	\$ 10,320	\$ 21,130	\$ (5,285)	\$ 15,845
Non-compete agreements	2,633	(2,098)	535	2,633	(1,550)	1,083
Internally developed software	1,358	(757)	601	1,173	(448)	725
Total	\$ 22,004	\$ (10,548)	\$ 11,456	\$ 24,936	\$ (7,283)	\$ 17,653

The estimated useful lives of acquired identifiable intangible assets are as follows:

Customer relationships	3 - 8 years
Non-compete agreements	3 - 5 years
Internally developed software	3 - 5 years

The weighted average amortization periods for customer relationships and non-compete agreements are 6 years and 5 years, respectively. Total amortization expense for the years ended December 31, 2008, 2007, and 2006 was approximately \$4.8 million, \$4.7 million, and \$3.5 million respectively. In addition, the Company recorded an impairment charge of \$1.6 million related to the loss of a customer relationship in 2008.

Estimated annual amortization expense for the next five years ended December 31 is as follows (in thousands):

2009	\$ 4,107
2010	\$ 3,336
2011	\$ 2,710
2012	\$ 971
2013	\$ 83
Thereafter	\$ 249

## 7. Stock-Based Compensation

## Stock Option Plans

In May 1999, the Company's Board of Directors and stockholders approved the 1999 Stock Option/Stock Issuance Plan (the "1999 Plan"). The 1999 Plan contains programs for (i) the discretionary granting of stock options to employees, non-employee board members and consultants for the purchase of shares of the Company's common stock, (ii) the discretionary issuance of common stock directly to eligible individuals, and (iii) the automatic issuance of stock options to non-employee board members. The Compensation Committee of the Board of Directors administers the 1999 Plan, and determines the exercise price and vesting period for each grant. Options granted under the 1999 Plan have a maximum term of 10 years. In the event that the Company is acquired, whether by merger or asset sale or

board-approved sale by the stockholders of more than 50% of the Company's voting stock, each outstanding option under the discretionary option grant program which is not to be assumed by the successor corporation or otherwise continued will automatically accelerate in full, and all unvested shares under the discretionary option grant and stock issuance programs will immediately vest, except to the extent the Company's repurchase rights with respect to those shares are to be assigned to the successor corporation or otherwise continued in effect. The Compensation Committee may grant options under the discretionary option grant program that will accelerate in the event of an acquisition even if the options are assumed or that will accelerate if the optionee's service is subsequently terminated.

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The Compensation Committee may grant options and issue shares that accelerate in connection with a hostile change in control effected through a successful tender offer for more than 50% of the Company's outstanding voting stock or by proxy contest for the election of board members, or the options and shares may accelerate upon a subsequent termination of the individual's service.

A summary of changes in common stock options during 2008, 2007 and 2006 is as follows (in thousands, except exercise price information):

	Shares	Range of Exercise Prices	Weighted-Average Exercise Price	Aggregate Intrinsic Value
Options outstanding at January 1, 2006	5,268	\$ 0.02 - 16.94	\$ 3.53	
Options granted	--	--	--	
Options exercised	(1,672)	\$ 0.02 - 12.13	\$ 2.4	\$ 18,637
Options canceled	(44)	\$ 1.01 - 13.25	\$ 5.41	
Options outstanding at December 31, 2006	3,552	\$ 0.02 - 16.94	\$ 4.03	
Options granted	9	\$ 3.00 - 3.00	\$ 3	
Options exercised	(1,160)	\$ 0.02 - 16.94	\$ 3.18	\$ 21,055
Options canceled	(22)	\$ 2.28 -7.48	\$ 3.36	
Options outstanding at December 31, 2007	2,379	\$ 0.02 - 16.94	\$ 4.44	
Options granted	--	--	\$ --	
Options exercised	(338)	\$ 0.02 - 10.00	\$ 2.15	\$ 2,726
Options canceled	(11)	\$ 0.50 - 13.25	\$ 7.57	
Options outstanding at December 31, 2008	2,030	\$ 0.03 - 16.94	\$ 4.81	\$ 2,560
Options vested, December 31, 2006	2,347	\$ 0.02 - 16.94	\$ 3.62	
Options vested, December 31, 2007	1,887	\$ 0.02 - 16.94	\$ 4.03	
Options vested, December 31, 2008	1,773	\$ 0.03 - 16.94	\$ 4.59	\$ 2,560

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Restricted stock activity for the year ended December 31, 2008 was as follows (in thousands, except fair value information):

	Shares	Weighted-Average Grant Date Fair Value
Restricted stock awards outstanding at January 1, 2008	2,053	\$ 14.33
Awards granted	2,024	\$ 6.12
Awards vested	(452)	\$ 14.07
Awards canceled or forfeited	(115)	\$ 13.82
Restricted stock awards outstanding at December 31, 2008	3,510	\$ 9.65

The total fair value of restricted shares vesting during the years ended December 31, 2008, 2007, and 2006 was \$2.3 million, \$5.2 million, and \$1.4 million, respectively.

PERFICIENT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)  
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The following is additional information related to stock options outstanding at December 31, 2008:

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Options	Weighted Average Exercise Price
\$ 0.03 – 2.28	632,782	\$ 1.71	3.86	632,782	\$ 1.71
\$ 2.77 – 3.75	481,335	\$ 3.52	3.02	481,335	\$ 3.52
\$ 4.40 – 6.24	76,689	\$ 5.02	4.19	76,689	\$ 5.02
\$ 6.31 – 6.31	555,000	\$ 6.31	5.96	297,857	\$ 6.31
7.48 –					
\$ 16.94	284,039	\$ 10.91	3.62	284,039	\$ 10.91
0.03 –					
\$ 16.94	2,029,845	\$ 4.81	4.21	1,772,702	\$ 4.59

At December 31, 2008, 2007 and 2006, the weighted-average remaining contractual life of outstanding options was 4.21, 5.20, and 6.27 years, respectively.

The Company recognized \$9.0 million of share-based compensation expense during 2008, which included \$1.0 million of expense for retirement savings plan contributions. For 2007 and 2006, total share-based compensation was \$6.1 million and \$3.1 million, respectively. The associated current and future income tax benefit recognized during 2008, 2007, and 2006 was \$2.9 million, \$2.1 million and \$0.8 million, respectively. As of December 31, 2008, there was \$33.4 million of total unrecognized compensation cost related to non-vested share-based awards. This cost is expected to be recognized over a weighted-average period of 4 years. The Company's estimated forfeiture rate for the year ended December 31, 2008 of approximately 5% for share based awards was calculated using our historical forfeiture experience to anticipate actual forfeitures in the future.

At December 31, 2008, 2.0 million shares were reserved for future issuance upon exercise of outstanding options and 8,075 shares were reserved for future issuance upon exercise of outstanding warrants. The majority of the outstanding warrants expire in December 2011. At December 31, 2008, there were 3.5 million shares of restricted stock outstanding under the 1999 Plan and classified as equity.

#### Employee Stock Purchase Plan

In 2005, the Compensation Committee approved the Employee Stock Purchase Plan (the "ESPP") to be available to employees starting January 1, 2006. The ESPP is a broadly-based stock purchase plan in which any eligible employee may elect to participate by authorizing the Company to make payroll deductions in a specific amount or designated percentage to pay the exercise price of an option. In no event will an employee be granted an ability under the ESPP that would permit the purchase of Common Stock with a fair market value in excess of \$25,000 in any calendar year and the Compensation Committee of the Company has set the current annual participation limit at \$12,500. During the year ended December 31, 2008, approximately 29,000 shares were purchased under the ESPP.

There are four three-month offering periods in each calendar year beginning on January 1, April 1, July 1, and October 1, respectively. The purchase price of shares offered under the ESPP is an amount equal to 95% of the fair market value of the Common Stock on the date of purchase (occurring on, respectively, March 31, June 30, September 30, and December 31). The ESPP is designed to comply with Section 423 of the Code and thus is eligible for the favorable tax treatment afforded by Section 423.

8. Line of Credit and Long Term Debt

On May 30, 2008, the Company entered into a Credit Agreement (the "Credit Agreement") with Silicon Valley Bank ("SVB") and KeyBank National Association ("KeyBank"). The Agreement replaces the Company's Amended and Restated Loan and Security Agreement dated as of June 3, 2005 and further amended on June 29, 2006. The Credit Agreement provides for revolving credit borrowings up to a maximum principal amount of \$50 million, subject to a commitment increase of \$25 million. The Credit Agreement also allows for the issuance of letters of credit in the aggregate amount of up to \$500,000 at any one time; outstanding letters of credit reduce the credit available for revolving credit borrowings.

PERFICIENT, INC.  
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All outstanding amounts owed under the Credit Agreement become due and payable no later than the final maturity date of May 30, 2012. Borrowings under the credit facility bear interest at the Company's option of SVB's prime rate (4.00% on December 31, 2008) plus a margin ranging from 0.00% to 0.50% or one-month LIBOR (0.44% on December 31, 2008) plus a margin ranging from 2.50% to 3.00%. The additional margin amount is dependent on the amount of outstanding borrowings. As of December 31, 2008, the Company had \$49.9 million of available borrowing capacity. The Company will incur an annual commitment fee of 0.30% on the unused portion of the line of credit.

The Company is required to comply with various financial covenants under the Credit Agreement. Specifically, the Company is required to maintain a ratio of earnings before interest, taxes, depreciation, and amortization ("EBITDA") plus stock compensation and minus income taxes paid and capital expenditures to interest expense and scheduled payments due for borrowings on a trailing three months basis annualized of less than 2.00 to 1.00 and a ratio of current maturities of long-term debt to EBITDA plus stock compensation and minus income taxes paid and capital expenditures of at least 2.75 to 1.00. As of December 31, 2008, the Company was in compliance with all covenants under the credit facility and the Company expects to be in compliance during the next 12 months. Substantially all of the Company's assets are pledged to secure the credit facility.

#### 9. Income Taxes

The Company files income tax returns in the U.S. federal jurisdiction, and various states and foreign jurisdictions. The Internal Revenue Service ("IRS") has completed examinations of the Company's U.S. income tax returns for 2002, 2003 and 2004. As of December 31, 2008, the IRS has proposed no significant adjustments to any of the Company's tax positions.

The Company adopted the provisions of FIN 48 on January 1, 2007. As a result of the implementation of FIN 48, the Company recognized no increases or decreases in the total amount of previously unrecognized tax benefits. The Company had no unrecognized tax benefits as of December 31, 2008 or 2007.

As of December 31, 2008, the Company had U.S. Federal tax net operating loss carry forwards of approximately \$6.0 million that will begin to expire in 2020 if not utilized. Utilization of net operating losses may be subject to an annual limitation due to the "change in ownership" provisions of the Internal Revenue Code of 1986. The annual limitation may result in the expiration of net operating losses before utilization.

Significant components of the provision for income taxes are as follows (in thousands):

	Year Ended December 31,		
	2008	2007	2006
<b>Current:</b>			
Federal	\$ 7,639	\$ 4,110	\$ 1,138
State	1,536	752	260
Foreign	(9)	26	102
<b>Total current</b>	<b>9,166</b>	<b>4,888</b>	<b>1,500</b>
<b>Tax benefit on acquired net operating loss carryforward</b>	<b>488</b>	<b>385</b>	<b>246</b>
	(922)	6,889	6,554

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Tax benefit (expense) from stock option exercises and restricted stock vesting

Deferred:

Federal	(1,304)	(668)	(902)
State	(137)	(70)	(116)
Total deferred	(1,441)	(738)	(1,018)
Total provision for income taxes	\$ 7,291	\$ 11,424	\$ 7,282

The components of pretax income for the years ended December 31, 2008, 2007 and 2006 are as follows (in thousands):

	Year Ended December 31,		
	2008	2007	2006
Domestic	\$ 16,879	\$ 27,640	\$ 16,565
Foreign	412	14	284
Total	\$ 17,291	\$ 27,654	\$ 16,849



PERFICIENT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)  
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In 2006, foreign operations only included Canada. For the year ended December 31, 2008 and 2007, foreign operations included Canada, China, and India.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's deferred taxes as of December 31, 2008 and 2007 are as follows:

	December 31,	
	2008	2007
	(In thousands)	
Deferred tax assets:		
Current deferred tax assets:		
Accrued liabilities	\$ 435	\$ 384
Net operating losses	475	273
Bad debt reserve	878	511
	1,788	1,168
Valuation allowance	(31)	(24)
Net current deferred tax assets	\$ 1,757	\$ 1,144
Non-current deferred tax assets:		
Net operating losses and capital loss	\$ 1,985	\$ 2,380
Fixed assets	329	169
Deferred compensation	1,654	1,031
	3,968	3,580
Valuation allowance	(109)	(106)
Net non-current deferred tax assets	\$ 3,859	\$ 3,474

	December 31,	
	2008	2007
	(In thousands)	
Deferred tax liabilities:		
Current deferred tax liabilities:		
Deferred income	\$ 302	\$ 307
Prepaid expenses	419	--
Net current deferred tax liabilities	\$ 721	\$ 307
Non-current deferred tax liabilities:		
Deferred income	\$ 84	\$ 402
Deferred compensation	244	214
Intangibles	3,510	4,407
Total non-current deferred tax liabilities	\$ 3,838	\$ 5,023
Net current deferred tax asset	\$ 1,036	\$ 837
Net non-current deferred tax asset (liability)	\$ 21	\$ (1,549)

The Company established a valuation allowance in 2005 to offset a portion of the Company's deferred tax assets due to uncertainties regarding the realization of deferred tax assets based on the Company's earnings history and limitations on the utilization of acquired net operating losses. In 2006, the valuation allowance decreased by approximately \$0.3 million primarily due to the benefit of acquired net operating loss carryforwards. During 2007,

the Company released approximately \$1.9 million of its valuation allowance after determining that the acquired net operating losses would be realized. As of December 31, 2008, the remaining valuation allowance relates mainly to a capital loss carryforward from an acquired entity. Management regularly assesses the likelihood that deferred tax assets will be recovered from future taxable income. To the extent management believes that it is more likely than not that a deferred tax asset will not be realized, a valuation allowance is established. Management believes it is more likely than not that the Company will generate sufficient taxable income in future years to realize the benefits of its deferred tax assets, except for those deferred tax assets for which an allowance has been provided.

PERFICIENT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)  
DECEMBER 31, 2008

Changes to the valuation allowance are summarized as follows for the years presented (in thousands):

	Year ended December 31,		
	2008	2007	2006
Balance, beginning of year	\$ 130	\$ 2,056	\$ 2,345
Additions	9	31	--
Additions/(Reductions) from purchase accounting	2	(1,957)	(289)
Balance, end of year	\$ 141	\$ 130	\$ 2,056

The federal corporate statutory rate is reconciled to the Company's effective income tax rate as follows:

	Year Ended December 31,		
	2008	2007	2006
Federal corporate statutory rate	35.0%	34.3%	34.3%
State taxes, net of federal benefit	4.5	4.2	4.6
Effect of foreign operations	--	0.1	--
Stock compensation	0.9	1.9	3.6
Other	1.7	0.8	0.7
Effective income tax rate	42.1%	41.3%	43.2%

The effective income tax rate increased to 42.1% for the year ended December 31, 2008 from 41.3% for the year ended December 31, 2007 as a result of the decreased tax benefit of certain dispositions of incentive stock options by holders.

#### 10. Commitments and Contingencies

The Company leases its office facilities and certain equipment under various operating lease agreements. The Company has the option to extend the term of certain of its office facility leases. Future minimum commitments under these lease agreements as of December 31, 2008 are as follows (in thousands):

	Operating Leases
2009	\$ 2,258
2010	2,125
2011	1,759
2012	745
2013	471
Thereafter	315
Total minimum lease payments	\$ 7,673

Rent expense for the years ended December 31, 2008, 2007 and 2006 was approximately \$2.9 million, \$2.3 million and \$1.7 million respectively.

As of December 31, 2008, the Company had one letter of credit outstanding for \$100,000 to serve as collateral to secure an office lease. This letter of credit expires in October 2009 and reduces the borrowings available under the

Company's account receivable line of credit.

#### 11. Balance Sheet Components

	December 31,	
	2008	2007
	(In thousands)	
Accounts receivable:		
Accounts receivable	\$ 30,565	\$ 36,894
Unbilled revenues	16,374	15,436
Note receivable (1)	2,142	--
Allowance for doubtful accounts	(1,497)	(1,475)
Total	\$ 47,584	\$ 50,855

(1) In June 2008, the Company entered into a note arrangement with a customer. The note provides that the customer will pay for a portion of services performed by the Company up to \$2.5 million over a one-year term. The customer's outstanding balance bears an annual interest rate of 10%.

PERFICIENT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)  
DECEMBER 31, 2008

	December 31, 2008          2007 (In thousands)	
<b>Other current assets:</b>		
Income tax receivable	\$ 1,558	\$ 1,174
Deferred tax asset	1,036	837
Other current assets	563	2,131
<b>Total</b>	<b>\$ 3,157</b>	<b>\$ 4,142</b>
<b>Other current liabilities:</b>		
Accrued bonus	\$ 5,644	\$ 9,378
Accrued subcontractor fees	1,625	2,399
Deferred revenues	1,575	1,439
Payroll related costs	1,495	1,862
Accrued settlement (2)	800	--
Accrued reimbursable expenses	671	788
Accrued medical claims expense	654	850
Other accrued expenses	1,875	2,005
<b>Total</b>	<b>\$ 14,339</b>	<b>\$ 18,721</b>

(2) The Company negotiated the termination of an ongoing fixed fee contract. Management believed the negotiation would result in a probable loss that was reasonably estimatable, and accrued its best estimate of the settlement amount as of December 31, 2008. The Company settled with the customer in February 2009 for an amount approximating the accrual.

<b>Property and Equipment:</b>		
Computer hardware (useful life of 2 years)	\$ 6,206	\$ 5,805
Furniture and fixtures (useful life of 5 years)	1,406	1,248
Leasehold improvements (useful life of 5 years)	969	884
Software (useful life of 1 year)	1,216	920
Less: Accumulated depreciation	(7,452)	(5,631)
<b>Total</b>	<b>\$ 2,345</b>	<b>\$ 3,226</b>

## 12. Allowance for Doubtful Accounts

Activity in the allowance for doubtful accounts is summarized as follows for the years presented (in thousands):

	Year ended December 31,		
	2008	2007	2006
Balance, beginning of year	\$ 1,475	\$ 707	\$ 367
Charged to expense	1,822	1,060	264
Additions (reductions) resulting from purchase accounting	(203)	153	371
Uncollected balances written off, net of recoveries	(1,597)	(445)	(295)
<b>Balance, end of year</b>	<b>\$ 1,497</b>	<b>\$ 1,475</b>	<b>\$ 707</b>

### 13. Business Combinations

The Company did not enter into any agreements to acquire another business during the twelve months ended December 31, 2008.

#### 2007 Acquisitions:

On February 20, 2007, the Company acquired E Tech, a solutions-oriented IT consulting firm, for approximately \$12.3 million. The purchase price consisted of approximately \$5.9 million in cash, transaction costs of approximately \$663,000, and 306,247 shares of the Company's common stock valued at approximately \$20.34 per share (approximately \$6.2 million worth of the Company's common stock) less the value of those shares subject to a lapse acceleration right of approximately \$474,000, as determined by a third party valuation firm. The results of E Tech's operations have been included in the Company's consolidated financial statements since February 20, 2007.

PERFICIENT, INC.  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)  
 DECEMBER 31, 2008

During the third quarter 2008, the Company and the shareholder representative for E Tech reached a settlement agreement related to an escrow claim. As a result of the settlement, the Company reacquired approximately 19,000 shares of its common stock issued as consideration. The settlement was recorded as a reduction to goodwill and additional paid-in capital in the third quarter 2008.

On June 25, 2007, the Company acquired Tier1 Innovation, LLC (“Tier1”), a national customer relationship management consulting firm, for approximately \$15.1 million. The purchase price consisted of approximately \$7.1 million in cash, transaction costs of approximately \$762,500, and 355,633 shares of the Company’s common stock valued at approximately \$20.69 per share (approximately \$7.4 million worth of the Company’s common stock) less the value of those shares subject to a lapse acceleration right of approximately \$144,000 as determined by a third party valuation firm. The results of Tier1’s operations have been included in the Company’s consolidated financial statements since June 25, 2007.

On September 20, 2007, the Company acquired BoldTech Systems, Inc. (“BoldTech”), an information technology consulting firm, for approximately \$20.9 million. The purchase price consisted of approximately \$10.0 million in cash, transaction costs of \$1.0 million, and 449,680 shares of the Company’s common stock valued at approximately \$23.69 per share (approximately \$10.6 million worth of the Company’s common stock) less the value of those shares subject to a lapse acceleration right of approximately \$723,000 as determined by a third party valuation firm. The results of BoldTech’s operations have been included in the Company’s consolidated financial statements since September 20, 2007.

On November 21, 2007, the Company acquired ePairs, Inc. (“ePairs”), a California-based consulting firm focused on Oracle-Siebel with a recruiting center in Chennai, India, for approximately \$5.1 million. The purchase price consisted of approximately \$2.5 million in cash, transaction costs of \$500,000, and 138,604 shares of the Company’s common stock valued at approximately \$16.25 per share (approximately \$2.2 million worth of the Company’s common stock) less the value of those shares subject to a lapse acceleration right of approximately \$86,000 as determined by a third party valuation firm. The results of ePairs’ operations have been included in the Company’s consolidated financial statements since November 21, 2007.

14. Quarterly Financial Results (Unaudited)

The following tables set forth certain unaudited supplemental quarterly financial information for the years ended December 31, 2008 and 2007. The quarterly operating results are not necessarily indicative of future results of operations. The financial data presented is not directly comparable between periods as a result of the four acquisitions in 2007 (in thousands, except per share data):

	March 31, 2008	June 30, 2008	Three Months Ended, September 30, 2008	December 31, 2008
	(Unaudited)			
Revenues:				
Services	\$ 52,100	\$ 53,632	\$ 52,510	\$ 49,238
Software and hardware	1,684	2,098	2,290	4,641

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Reimbursable expenses		3,539		3,370		3,506		2,880
Total revenues	\$	57,323	\$	59,100	\$	58,306	\$	56,759
Gross margin	\$	17,562	\$	20,139	\$	19,176		16,625
Income from operations	\$	5,047	\$	6,802	\$	4,402	\$	1,427
Income before income taxes	\$	5,203	\$	6,793	\$	3,677	\$	1,618
Net income	\$	3,076	\$	3,989	\$	2,176	\$	759
Basic net income per share	\$	0.10	\$	0.13	\$	0.07	\$	0.03
Diluted net income per share	\$	0.10	\$	0.13	\$	0.07	\$	0.03



PERFICIENT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)  
DECEMBER 31, 2008

	March 31, 2007	June 30, 2007	Three Months Ended, September 30, 2007 (Unaudited)	December 31, 2007
<b>Revenues:</b>				
Services	\$ 43,297	\$ 45,961	\$ 48,387	\$ 53,750
Software	4,192	3,696	1,582	4,773
Reimbursable expenses	2,560	2,938	3,115	3,897
<b>Total revenues</b>	<b>\$ 50,049</b>	<b>\$ 52,595</b>	<b>\$ 53,084</b>	<b>\$ 62,420</b>
Gross margin	\$ 17,052	\$ 18,185	\$ 19,046	\$ 21,407
Income from operations	\$ 5,570	\$ 6,907	\$ 7,569	\$ 7,416
Income before income taxes	\$ 5,575	\$ 6,958	\$ 7,649	\$ 7,472
Net income	\$ 3,160	\$ 4,014	\$ 4,541	\$ 4,515
Basic net income per share	\$ 0.12	\$ 0.15	\$ 0.16	\$ 0.15
Diluted net income per share	\$ 0.11	\$ 0.13	\$ 0.15	\$ 0.15

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders  
Perficient, Inc.:

We have audited the accompanying consolidated balance sheets of Perficient, Inc. (the Company) as of December 31, 2008 and 2007, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the years in the two-year period ended December 31, 2008. We also have audited the Company's internal control over financial reporting as of December 31, 2008, based on criteria established in Internal Control – Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on these consolidated financial statements and an opinion on the Company's internal control over financial reporting based on our audits. The accompanying consolidated financial statements of the Company as of December 31, 2006, and for the year then ended, were audited by other auditors whose report thereon dated March 1, 2007, except note 2 to the 2006 financial statements as to which date is August 13, 2007, expressed an unqualified opinion on those statements.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the consolidated financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

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

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

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In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2008 and 2007, and the results of their operations and their cash flows for each of the years in the two-year period ended December 31, 2008, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2008, based on criteria established in Internal Control – Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission.

As discussed in note 2 to the consolidated financial statements, effective January 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 123 (Revised 2004), Shared-Based Payment.

/s/ KPMG LLP

St. Louis, Missouri  
March 5, 2009

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders  
Perficient, Inc.  
Austin, Texas

We have audited the accompanying consolidated statements of operations, stockholders' equity and comprehensive income, and cash flows of Perficient, Inc. for the year ended December 31, 2006. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan 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, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the results of operations and cash flows of Perficient, Inc. for the year ended December 31, 2006, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the consolidated financial statements, effective January 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 123(R), Share-Based Payment.

/s/ BDO Seidman, LLP  
Houston, Texas  
March 1, 2007, except Note 2 to the 2006 financial  
statements as to which date is August 13, 2007

Item Changes In and Disagreements With Accountants on Accounting and Financial Disclosure.  
9.

None.

Item Controls and Procedures.

9A.

#### Evaluation of Disclosure Controls and Procedures

We have established disclosure controls and procedures to ensure that material information relating to the Company, including its consolidated subsidiaries, is made known to the officers who certify the Company's financial reports and to other members of senior management and the Board of Directors.

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's reports under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to management, including the principal executive officer and principal financial officer of the Company, as appropriate, to allow timely decisions regarding required disclosure. The Company's management, with the participation of the Company's principal executive officer and principal financial officer, has evaluated the effectiveness of the Company's disclosure controls and procedures as of the end of the fiscal year covered by this Annual Report on Form 10-K. Based on that evaluation, the Company's principal executive and principal financial officers have determined that the Company's disclosure controls and procedures were effective.

#### Management's Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f). In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control procedures. The objectives of internal control include providing management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America. Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our assessment under those criteria, management concluded that the Company's internal control over financial reporting was effective as of December 31, 2008.

KPMG LLP, our independent registered public accounting firm, has audited our financial statements for the year ended December 31, 2008 included in this Form 10-K, and has issued its report on the effectiveness of internal control over financial reporting as of December 31, 2008, which is included herein.

#### Changes in Internal Control Over Financial Reporting

There have not been any changes in the Company's internal control over financial reporting as defined in Exchange Act Rule 13a-15(f) during the quarter ended December 31, 2008, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Item Other Information.

9B.

The Company's annual stockholders meeting will be held on April 17, 2009. The deadline for submitting shareholder proposals and the date on which such submittals will be deemed untimely remain as set in the Company's Proxy Statement for its 2008 annual stockholders meeting, which was filed with the SEC on April 30, 2008.

The Company entered into an employment agreement with John T. McDonald, our Chairman of the Board and Chief Executive Officer, on March 3, 2009. The agreement is effective as of January 1, 2009 and will expire on December 31, 2011. Mr. McDonald's employment agreement provides for the following compensation:

- an annual salary of \$285,000 that may be increased by the Board of Directors from time to time;
- an annual performance bonus of up to 200% of Mr. McDonald's annual salary in the event the Company achieves certain performance targets approved by the Board of Directors ("Mr. McDonald's Target Bonus"), which may be increased up to 300% of Mr. McDonald's annual salary pursuant to the 2009 Executive Bonus Plan;

- entitlement to participate in such insurance, disability, health, and medical benefits and retirement plans or programs as are from time to time generally made available to executive employees of the Company, pursuant to the policies of the Company and subject to the conditions and terms applicable to such benefits, plans or programs; and
- death, disability, severance, and change of control benefits upon Mr. McDonald's termination of employment or change of control of the Company.

Under his agreement, Mr. McDonald can choose to reduce his role as Chief Executive Officer and Chairman of the Board to Chairman of the Board only. If this were to occur, Mr. McDonald would incur a reduction in salary and bonus by 50% and would only be eligible for equity grants awarded to non-employee directors. Also, Mr. McDonald would be required to make himself available to the Company for up to 20 hours per week and his responsibilities would include presiding over the Board of Directors and committees of the Board of Directors, providing oversight of corporate strategy, financing, acquisitions, and investor relations, including presenting on the Company's quarterly earnings conference calls and presenting at such investor conferences and handling such other investor relations functions as reasonably requested by the Company.

Mr. McDonald has agreed to refrain from competing with the Company for a period of five years following the termination of his employment. Mr. McDonald's compensation is subject to review and adjustment on an annual basis in accordance with the Company's compensation policies as in effect from time to time.

The Company entered into an employment agreement with Jeffrey S. Davis, our President and Chief Operating Officer, on March 3, 2009. The agreement is effective as of January 1, 2009 and will expire on December 31, 2011. Mr. Davis' previous employment agreement with the Company was effective July 1, 2006 and was set to expire on June 30, 2009. Mr. Davis's current employment agreement provides for the following compensation:

- an annual salary of \$285,000 that may be increased by the CEO from time to time;
- an annual performance bonus of up to 200% of Mr. Davis's annual salary in the event the Company achieves certain performance targets ("Mr. Davis's Target Bonus"), which may be increased up to 300% of Mr. Davis's annual salary pursuant to the 2009 Executive Bonus Plan;
- entitlement to participate in such insurance, disability, health, and medical benefits and retirement plans or programs as are from time to time generally made available to executive employees of the Company, pursuant to the policies of the Company and subject to the conditions and terms applicable to such benefits, plans or programs; and
- death, disability, severance, and change of control benefits upon Mr. Davis's termination of employment or change of control of the Company

Mr. Davis has agreed to refrain from competing with the Company for a period of five years following the termination of his employment. Mr. Davis's compensation is subject to review and adjustment on an annual basis in accordance with the Company's compensation policies as in effect from time to time.

## PART III

Item Directors, Executive Officers and Corporate Governance.  
10.

## Executive Officers and Directors

Our executive officers and directors, including their ages as of the date of this filing are as follows:

Name	Age	Position
John T. McDonald	45	Chairman of the Board and Chief Executive Officer
Jeffrey S. Davis	44	President and Chief Operating Officer
Paul E. Martin	48	Chief Financial Officer, Treasurer and Secretary
Timothy J. Thompson	48	Vice President of Client Development Controller and Vice President of Finance and
Richard T. Kalbfleish	53	Administration
Ralph C. Derrickson	50	Director
Max D. Hopper	74	Director
Kenneth R. Johnsen	55	Director
David S. Lundeen	47	Director

John T. McDonald joined the Company in April 1999 as Chief Executive Officer and was elected Chairman of the Board in March 2001. From April 1996 to October 1998, Mr. McDonald was president of VideoSite, Inc., a multimedia software company that was acquired by GTECH Corporation in October 1997, 18 months after Mr. McDonald became VideoSite's president. From May 1995 to April 1996, Mr. McDonald was a Principal with Zilkha & Co., a New York-based merchant banking firm. From June 1993 to April 1996, Mr. McDonald served in various positions at Blockbuster Entertainment Group, including Director of Corporate Development and Vice President, Strategic Planning and Corporate Development of NewLeaf Entertainment Corporation, a joint venture between Blockbuster and IBM. From 1987 to 1993, Mr. McDonald was an attorney with Skadden, Arps, Slate, Meagher & Flom in New York, focusing on mergers and acquisitions and corporate finance. Mr. McDonald currently serves as a member of the board of directors of a number of privately held companies and non-profit organizations. Mr. McDonald received a B.A. in Economics from Fordham University and a J.D. from Fordham Law School.

Jeffrey S. Davis became the Chief Operating Officer of the Company upon the closing of the acquisition of Vertecon in April 2002 and was named the Company's President in 2004. He previously served the same role of Chief Operating Officer at Vertecon from October 1999 to its acquisition by Perficient. Prior to Vertecon, Mr. Davis was a Senior Manager and member of the leadership team in Arthur Andersen's Business Consulting Practice starting in January 1999 where he was responsible for defining and managing internal processes, while managing business development and delivery of products, services and solutions to a number of large accounts. Prior to Arthur Andersen, Mr. Davis worked at Ernst & Young LLP for two years, Mallinckrodt, Inc. for two years, and spent five years at McDonnell Douglas in many different technical and managerial positions. Mr. Davis has a M.B.A. from Washington University and a B.S. degree in Electrical Engineering from the University of Missouri.

Paul E. Martin joined the Company in August 2006 as Chief Financial Officer, Treasurer and Secretary. From August 2004 until February 2006, Mr. Martin was the Interim co-Chief Financial Officer and Interim Chief Financial Officer of Charter Communications, Inc. ("Charter"), a publicly traded multi-billion dollar in revenue domestic cable television multi-system operator. From April 2002 through April 2006, Mr. Martin was the Senior Vice President, Principal Accounting Officer and Corporate Controller of Charter and was Charter's Vice President and Corporate



Controller from March 2000 to April 2002. Prior to Charter, Mr. Martin was Vice President and Controller for Operations and Logistics for Fort James Corporation, a manufacturer of paper products with multi-billion dollar revenues. From 1995 to February 1999, Mr. Martin was Chief Financial Officer of Rawlings Sporting Goods Company, Inc., a publicly traded multi-million dollar revenue sporting goods manufacturer and distributor. Mr. Martin received a B.S. degree with honors in accounting from the University of Missouri – St. Louis. Mr. Martin is also a member of the University of Missouri – St. Louis School of Business Leadership Council.

Richard T. Kalbfleish joined the Company as Controller in November 2004 and became Vice President of Finance and Administration and Assistant Treasurer in May 2005. In August 2006, Mr. Kalbfleish became the Principal Accounting Officer of the Company. Prior to joining the Company, Mr. Kalbfleish served as Vice President of Finance and Administration with IntelliMark/Technisource, a national IT staffing company, for 11 years. Mr. Kalbfleish has over 23 years of experience at the Controller level and above in a number of service industries with an emphasis on acquisition integration and accounting, human resources and administrative support. Mr. Kalbfleish has a B.S.B.A. in Accountancy from the University of Missouri - Columbia.

Ralph C. Derrickson became a member of the Board of Directors in July 2004. Mr. Derrickson has more than 27 years of technology management experience in a wide range of settings including start-up, interim management and restructuring situations. Currently Mr. Derrickson is President and CEO of Carena, Inc. Prior to joining Carena, Inc., Mr. Derrickson was managing director of venture investments at Vulcan Inc., an investment management firm with headquarters in Seattle, Washington from October 2001 to July 2004. Mr. Derrickson is a founding partner of Watershed Capital, an early-stage venture capital firm, and is the managing member of RCollins Group, LLC, a management advisory firm. He served as a board member of Metricom, Inc., a publicly traded company, from April 1997 to November 2001 and as Interim CEO of Metricom from February 2001 to August 2001. He served as vice president of product development at Starwave Corporation, one of the pioneers of the Internet. Earlier, Mr. Derrickson held senior management positions at NeXT Computer, Inc. and Sun Microsystems, Inc. He has served on the boards of numerous start-up technology companies. Mr. Derrickson is on the faculty of the Michael G. Foster School of Business at the University of Washington, and serves on the Executive Advisory Board of the Center for Entrepreneurship and Innovation at the University of Washington, as well as a member of the President's Circle of the National Academy of Sciences, The National Academy of Engineering and the Institute of Medicine. Mr. Derrickson holds a bachelor's degree in systems software from the Rochester Institute of Technology.

Max D. Hopper became a member of the Board of Directors in September 2002. Mr. Hopper began his information systems career in 1960 at Shell Oil and served with EDS, United Airlines and Bank of America prior to joining American Airlines. During Mr. Hopper's twenty-year tenure at American Airlines he served as CIO, and as CEO of several business units. Most recently, he founded Max D. Hopper Associates, Inc., a consulting firm that specializes in the strategic use of information technology and business-driven technology. Mr. Hopper currently serves on the board of directors for several companies such as Gartner Group as well as other private corporations.

Kenneth R. Johnsen became a member of the Board of Directors in July 2004. Mr. Johnsen is currently the CEO and Chairman of the Board of HG Food, LLC. Prior to joining HG Food, LLC, Mr. Johnsen was a partner with Aspen Advisors, LP. From January 1999 to October 2006, Mr. Johnsen served as President, CEO and Chairman of the Board of Parago Inc., a marketing services transaction processor. Before joining Parago Inc. in 1999, he served as President, Chief Operating Officer and Board Member of Metamor Worldwide Inc., an \$850 million public technology services company specializing in information technology consulting and implementation. Metamor was later acquired by PSINet for \$1.7 billion. At Metamor, Mr. Johnsen grew the IT Solutions Group revenues from \$20 million to over \$300 million within two years. His experience also includes 22 years at IBM where he held general management positions, including Vice President of Business Services for IBM Global Services and General Manager of IBM China/Hong Kong Operations. He achieved record revenues, profit and customer satisfaction levels in both business units.

David S. Lundeen became a member of the Board of Directors in April 1998. From March 1999 through 2002, Mr. Lundeen was a partner with Watershed Capital, a private equity firm based in Mountain View, California. From June 1997 to February 1999, Mr. Lundeen was self-employed, managed his personal investments and acted as a consultant and advisor to various businesses. From June 1995 to June 1997, he served as the Chief Financial Officer and Chief Operating Officer of BSG Corporation. From January 1990 until June 1995, Mr. Lundeen served as President of Blockbuster Technology and as Vice President of Finance of Blockbuster Entertainment Corporation. Prior to that time, Mr. Lundeen was an investment banker with Drexel Burnham Lambert in New York City. Mr. Lundeen currently serves as a member of the board of directors of Parago, Inc., and as Chairman of the Board of Interstate Connections, Inc. Mr. Lundeen received a B.S. in Engineering from the University of Michigan in 1984 and an M.B.A. from the University of Chicago in 1988. The Board of Directors has determined that Mr. Lundeen is an audit committee financial expert, as such term is defined in the rules and regulations promulgated by the Securities and Exchange Commission ("SEC").

Codes of Conduct and Ethics

The Company has adopted a Corporate Code of Business Conduct and Ethics that applies to all employees and directors of the Company while acting on the Company's behalf and has adopted a Financial Code of Ethics applicable to the chief executive officer, the chief financial officer, and other senior financial officials. Both of these codes are available for viewing on Perficient's website at [www.Perficient.com](http://www.Perficient.com). Any amendments to, or waivers from, the Financial Code of Ethics will also be posted on Perficient's website.

Audit Committee of the Board of Directors

The board of directors has created an audit committee. Each committee member is independent as defined by Nasdaq Global Select Market listing standards.

The audit committee has the sole authority to appoint, retain and terminate our independent accountants and is directly responsible for the compensation, oversight and evaluation of the work of the independent accountants. The independent accountants report directly to the audit committee. The audit committee also has the sole authority to approve all audit engagement fees and terms and all non-audit engagements with our independent accountants and must pre-approve all auditing and permitted non-audit services to be performed for us by the independent accountants, subject to certain exceptions provided by the Securities Exchange Act of 1934. The members of the audit committee are Max D. Hopper, David S. Lundeen and Ralph C. Derrickson. Mr. Lundeen serves as chairman of the audit committee. The board of directors has determined that Mr. Lundeen is qualified as our audit committee financial expert within the meaning of Securities and Exchange Commission regulations and that he has accounting and related financial management expertise within the meaning of the listing standards of the Nasdaq Global Select Market. The board of directors has affirmatively determined that Mr. Lundeen qualified as an independent director as defined by the Nasdaq Global Select Market listing standards.

Additional information with respect to Directors and Executive Officers of the Company is incorporated by reference to the Proxy Statement under the captions "Directors and Executive Officers", "Composition and Meetings of the Board of Directors and Committees", and "Section 16(a) Beneficial Ownership Reporting Compliance." The Proxy Statement will be filed pursuant to Regulation 14A within 120 days of the end of the Company's fiscal year.

Item Executive Compensation.

11.

Information on this subject is found in the Proxy Statement under the captions "Compensation of Directors and Executive Officers" and "Directors and Executive Officers" and is incorporated herein by reference. The Proxy Statement will be filed pursuant to Regulation 14A within 120 days of the end of the Company's fiscal year.

Item Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

12.

Information on this subject is found in the Proxy Statement under the captions "Security Ownership of Certain Beneficial Owners and Management", "Directors and Executive Officers", and "Equity Compensation Plan Information" and is incorporated herein by reference. The Proxy Statement will be filed pursuant to Regulations 14A within 120 days of the end of the Company's fiscal year.

Item Certain Relationships and Related Transactions, and Director Independence.

13.

Information on this subject is found in the Proxy Statement under the caption "Certain Relationships and Related Transactions" and incorporated herein by reference. The Proxy Statement will be filed pursuant to Regulation 14A within 120 days of the end of the Company's fiscal year.

Item Principal Accounting Fees and Services.

14.

Information on this subject is found in the Proxy Statement under the caption "Principal Accounting Firm Fees and Services" and incorporated herein by reference. The Proxy Statement will be filed pursuant to Regulation 14A within 120 days of the end of the Company's fiscal year.

PART IV

Item Exhibits, Financial Statement Schedules.  
15.

(a) 1. Financial Statements

The following consolidated statements are included within Item 8 under the following captions:

Index	Page(s)
Consolidated Balance Sheets	33
Consolidated Statements of Income	34
Consolidated Statements of Changes in Stockholders' Equity	35
Consolidated Statements of Cash Flows	36
Notes to Consolidated Financial Statements	37
Reports of Independent Registered Public Accounting Firms	52-53

2. Financial Statement Schedules

No financial statement schedules are required to be filed by Items 8 and 15(d) because they are not required or are not applicable, or the required information is set forth in the applicable financial statements or notes thereto.

3. Exhibits

See Index to Exhibits starting on page 61.

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.

PERFICIENT, INC.

Date: March 5, 2009

By: /s/ John T. McDonald  
John T. McDonald  
Chief Executive Officer (Principal Executive Officer)

Date: March 5, 2009

By: /s/ Paul E. Martin  
Paul E. Martin  
Chief Financial Officer (Principal Financial Officer)

Date: March 5, 2009

By: /s/ Richard T. Kalbfleish  
Richard T. Kalbfleish  
Vice President of Finance and Administration (Principal Accounting Officer)

KNOW ALL MEN BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints John T. McDonald and Paul E. Martin, and each of them (with full power to each of them to act alone), his or her true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution, for him or her and in his or her name, place and stead, in any and all capacities, to sign on his or her behalf individually and in each capacity stated below any and all amendments (including post-effective amendments) to this annual report, and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in and about the premises, as fully to all intents and purposes as he or she might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents and either of them, or their substitutes, may lawfully do or cause to be done by virtue hereof.

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/ John T. McDonald John T. McDonald	Chief Executive Officer and Chairman of the Board (Principal Executive Officer)	March 5, 2009
/s/ Ralph C. Derrickson Ralph C. Derrickson	Director	March 5, 2009

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/s/ Max D. Hopper  
Max D. Hopper

Director

March 5, 2009

/s/ Kenneth R. Johnsen  
Kenneth R. Johnsen

Director

March 5, 2009

/s/ David S. Lundeen  
David S. Lundeen

Director

March 5, 2009



INDEX TO EXHIBITS

Exhibit Number	Description
2.1	Agreement and Plan of Merger, dated as of April 6, 2006, by and among Perficient, Inc., PFT MergeCo, Inc., Bay Street Solutions, Inc. and the other signatories thereto, previously filed with the Securities and Exchange Commission as an Exhibit to our Current Report on Form 8-K filed on April 12, 2006 and incorporated herein by reference
2.2	Agreement and Plan of Merger, dated as of May 31, 2006, by and among Perficient, Inc., PFT MergeCo II, Inc., Insolexen, Corp., HSU Investors, LLC, Hari Madamalla, Steve Haglund and Uday Yallapragada, previously filed with the Securities and Exchange Commission as an Exhibit to our Current Report on Form 8-K filed on June 5, 2006 and incorporated herein by reference
2.3	Asset Purchase Agreement, dated as of July 20, 2006, by and among Perficient, Inc., Perficient DCSS, Inc. and Digital Consulting & Software Services, Inc., previously filed with the Securities and Exchange Commission as an Exhibit to our Current Report on Form 8-K filed on July 26, 2006 and incorporated herein by reference
2.4	Agreement and Plan of Merger, dated as of February 20, 2007, by and among Perficient, Inc., PFT MergeCo III, Inc., e tech solutions, Inc., each of the Principals of e tech solutions, Inc., and Gary Rawding, as Representative, previously filed with the Securities and Exchange Commission as an Exhibit to our Current Report on Form 8-K filed on February 23, 2007 and incorporated herein by reference
2.5	Asset Purchase Agreement, dated as of June 25, 2007, by and among Perficient, Inc., Tier1 Innovation, LLC, and Mark Johnston and Jay Johnson, previously filed with the Securities and Exchange Commission as an Exhibit to our Current Report on Form 8-K filed on June 28, 2007 and incorporated herein by reference
2.6	Agreement and Plan of Merger, dated as of September 20, 2007, by and among Perficient, Inc., PFT MergeCo IV, Inc., BoldTech Systems, Inc., a Colorado corporation, BoldTech Systems, Inc., a Delaware corporation, each of the Principals (as defined therein) and the Representative (as defined therein), previously filed with the Securities and Exchange Commission as an Exhibit to our Current Report on Form 8-K filed September 21, 2007 and incorporated herein by reference
2.7	Asset Purchase Agreement, dated as of November 21, 2007, by and among Perficient, Inc., ePairs, Inc., the Principal (as defined therein) and the Seller Shareholders (as defined therein), previously filed with the Securities and Exchange Commission as an Exhibit to our Current Report on Form 8-K filed November 27, 2007 and incorporated herein by reference
3.1	Certificate of Incorporation of Perficient, Inc., previously filed with the Securities and Exchange Commission as an Exhibit to our Registration Statement on Form SB-2 (File No. 333-78337) declared effective on July 28, 1999 by the Securities and Exchange Commission and incorporated herein by reference
3.2	

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Certificate of Amendment to Certificate of Incorporation of Perficient, Inc., previously filed with the Securities and Exchange Commission as an Exhibit to our Form 8-A filed with the Securities and Exchange Commission pursuant to Section 12(g) of the Securities Exchange Act of 1934 on February 15, 2005 and incorporated herein by reference

- 3.3 Certificate of Amendment to Certificate of Incorporation of Perficient, Inc., previously filed with the Securities and Exchange Commission as an Exhibit to our Registration Statement on Form S-8 (File No. 333-130624) filed on December 22, 2005 and incorporated herein by reference
- 3.4 Bylaws of Perficient, Inc., previously filed with the Securities and Exchange Commission as an Exhibit to our Current Report on Form 8-K filed November 9, 2007 and incorporated herein by reference
- 4.1 Specimen Certificate for shares of common stock, previously filed with the Securities and Exchange Commission as an Exhibit to our Registration Statement on Form SB-2 (File No. 333-78337) declared effective on July 28, 1999 by the Securities and Exchange Commission and incorporated herein by reference
- 4.2 Warrant granted to Gilford Securities Incorporated, previously filed with the Securities and Exchange Commission as an Exhibit to our Registration Statement on Form SB-2 (File No. 333-78337) declared effective on July 28, 1999 by the Securities and Exchange Commission and incorporated herein by reference

Exhibit Number	Description
4.3	Form of Common Stock Purchase Warrant, previously filed with the Securities and Exchange Commission as an Exhibit to our Current Report on Form 8-K (File No.001-15169) filed on January 17, 2002 and incorporated herein by reference
4.4	Form of Warrant, previously filed with the Securities and Exchange Commission as an Exhibit to our Registration Statement on Form S-3 (File No. 333-117216) and incorporated by reference herein
10.1†	Perficient, Inc. Amended and Restated 1999 Stock Option/Stock Issuance Plan, previously filed with the Securities and Exchange Commission as an Exhibit to our annual report on Form 10-K for the year ended December 31, 2005 and incorporated by reference herein
10.2†	Form of Stock Option Agreement, previously filed with the Securities and Exchange Commission as an Exhibit to our Annual Report on Form 10-KSB for the fiscal year ended December 31, 2004 and incorporated herein by reference
10.3†	Perficient, Inc. Employee Stock Purchase Plan, previously filed with the Securities and Exchange Commission as Appendix A to the Registrant's Schedule 14A (File No. 001-15169) on October 13, 2005 and incorporated herein by reference
10.4†	Form of Restricted Stock Agreement, previously filed with the Securities and Exchange Commission as an Exhibit to our annual report on Form 10-K for the year ended December 31, 2005 and incorporated by reference herein
10.5†	Form of Indemnity Agreement between Perficient, Inc. and each of our directors and officers, previously filed with the Securities and Exchange Commission as an Exhibit to our Registration Statement on Form SB-2 (File No. 333-78337) declared effective on July 28, 1999 by the Securities and Exchange Commission and incorporated herein by reference
10.6†	Offer Letter, dated July 20, 2006, by and between Perficient, Inc. and Mr. Paul E. Martin, previously filed with the Securities and Exchange Commission as an Exhibit to our Current Report on Form 8-K filed on July 26, 2006 and incorporated herein by reference
10.7†	Offer Letter Amendment, dated August 31, 2006, by and between Perficient, Inc. and Mr. Paul E. Martin, previously filed with the Securities and Exchange Commission as an Exhibit to our Current Report on Form 8-K filed on September 1, 2006 and incorporated herein by reference
10.8†*	Employment Agreement between Perficient, Inc. and John T. McDonald dated March 3, 2009, and effective as of January 1, 2009
10.9†*	Employment Agreement between Perficient, Inc. and Jeffrey S. Davis dated March 3, 2009, and effective as of January 1, 2009
10.10	Amended and Restated Loan and Security Agreement by and among Silicon Valley Bank, KeyBank National Association, Perficient, Inc., Perficient Canada Corp., Perficient Genisys, Inc., Perficient Meritage, Inc. and Perficient Zettaworks, Inc. dated effective as of June 3, 2005, previously filed with the

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Securities and Exchange Commission as an Exhibit to our annual report on Form 10-K for the year ended December 31, 2005 and incorporated herein by reference

- 10.11 Amendment to Amended and Restated Loan and Security Agreement, dated as of June 29, 2006, by and among Silicon Valley Bank, KeyBank National Association, Perficient, Inc., Perficient Genisys, Inc., Perficient Canada Corp., Perficient Meritage, Inc., Perficient Zettaworks, Inc., Perficient iPath, Inc., Perficient Vivare, Inc., Perficient Bay Street, LLC and Perficient Insolexen, LLC, previously filed with the Securities and Exchange Commission as an Exhibit to our Current Report on Form 8-K filed on July 5, 2006 and incorporated herein by reference

Exhibit

Number Description

- 10.12 Lease by and between Cornerstone Opportunity Ventures, LLC and Perficient, Inc., previously filed with the Securities and Exchange Commission as an Exhibit to our annual report on Form 10-K for the year ended December 31, 2005 and incorporated by reference herein
- 10.13 First Amended and Restated Investor Rights Agreements dated as of June 26, 2002 by and between Perficient, Inc. and the Investors listed on Exhibits A and B thereto, previously filed with the Securities and Exchange Commission as an Exhibit to our Current Report on Form 8-K (File No. 001-15169) filed on July 18, 2002 and incorporated by reference herein
- 10.14 Securities Purchase Agreement, dated as of June 16, 2004, by and among Perficient, Inc., Tate Capital Partners Fund, LLC, Pandora Select Partners, LP, and Sigma Opportunity Fund, LLC, previously filed with the Securities and Exchange Commission as an Exhibit to our Current Report on Form 8-K filed on June 23, 2004 and incorporated by reference herein
- 21.1\* Subsidiaries
- 23.1\* Consent of BDO Seidman, LLP
- 23.2\* Consent of KPMG LLP
- 24.1 Power of Attorney (included on the signature page hereto)
- 31.1\* Certification by the Chief Executive Officer of Perficient, Inc. as required by Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2\* Certification by the Chief Financial Officer of Perficient, Inc. as required by Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1\* Certification by the Chief Executive Officer and Chief Financial Officer of Perficient, Inc. pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

† Identifies an Exhibit that consists of or includes a management contract or compensatory plan or arrangement.

\* Filed herewith.

