DUKE REALTY CORP
Form 10-Q
November 04, 2011
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q
(Mark One)

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

For the quarterly period ended September 30, 2011
OR

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

For the transition period from to
Commission File Number: 1-9044
DUKE REALTY CORPORATION
(Exact Name of Registrant as Specified in Its Charter)

Indiana (State or Other Jurisdiction of Incorporation or Organization)	35-1740409 (I.R.S. Employer Identification Number)
600 East 96th Street, Suite 100 Indianapolis, Indiana (Address of Principal Executive Offices)	46240 (Zip Code)

Registrant's Telephone Number, Including Area Code: (317) 808-6000

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes x No ¨

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 definition of "large accelerated filer", "accelerated filer", and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer x	Accelerated filer o
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act): YES ¨ NO x

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

Class	Outstanding at November 4, 2011
Common Stock, $.01 par value per share	252,921,718

DUKE REALTY CORPORATION
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PART I - FINANCIAL INFORMATION
Item 1. Financial Statements
DUKE REALTY CORPORATION AND SUBSIDIARIES
Consolidated Balance Sheets
(in thousands, except per share amounts)

	September 30, 2011 (Unaudited)	December 31, 2010
ASSETS		
Real estate investments:		
Land and improvements	$1,307,608	$1,166,409
Buildings and tenant improvements	5,601,866	5,396,339
Construction in progress	41,490	61,205
Investments in and advances to unconsolidated companies	368,671	367,445
Undeveloped land	622,254	625,353
	7,941,889	7,616,751
Accumulated depreciation	(1,413,804)	(1,290,417)
Net real estate investments	6,528,085	6,326,334
Real estate investments and other assets held-for-sale	21,992	394,287
Cash and cash equivalents	16,182	18,384
Accounts receivable, net of allowance of $2,854 and $2,945	21,685	22,588
Straight-line rent receivable, net of allowance of $7,502 and $7,260	140,732	125,185
Receivables on construction contracts, including retentions	44,425	7,408
Deferred financing costs, net of accumulated amortization of $56,105 and $46,407	39,449	46,320
Deferred leasing and other costs, net of accumulated amortization of $329,325 and $269,000	497,594	517,934
Escrow deposits and other assets	194,517	185,836
	$7,504,661	$7,644,276
LIABILITIES AND EQUITY		
Indebtedness:		
Secured debt	$1,184,268	$1,065,628
Unsecured notes	2,783,762	2,948,405
Unsecured lines of credit	304,293	193,046
	4,272,323	4,207,079
Liabilities related to real estate investments held-for-sale	957	14,732
Construction payables and amounts due subcontractors, including retentions	66,786	44,782
Accrued real estate taxes	123,524	83,615
Accrued interest	35,725	62,407
Other accrued expenses	42,729	61,448
Other liabilities	128,123	129,860
Tenant security deposits and prepaid rents	59,551	50,450
Total liabilities	4,729,718	4,654,373
Shareholders’ equity:		
Preferred shares ($.01 par value); 5,000 shares authorized; 3,176 and 3,618 shares issued and outstanding	793,910	904,540
	2,529	2,522

Common shares ($.01 par value); 400,000 shares authorized; 252,918 and 252,195 shares issued and outstanding		
Additional paid-in capital	3,591,381	3,573,720
Accumulated other comprehensive income (loss)	493	(1,432)
Distributions in excess of net income	(1,678,484)	(1,533,740)
Total shareholders' equity	2,709,829	2,945,610
Noncontrolling interests	65,114	44,293
Total equity	2,774,943	2,989,903
	$7,504,661	$7,644,276

See accompanying Notes to Consolidated Financial Statements

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DUKE REALTY CORPORATION AND SUBSIDIARIES
Consolidated Statements of Operations
For the three and nine months ended September 30,
(in thousands, except per share amounts)
(Unaudited)

	Three Months Ended		Nine Months Ended	
	2011	2010	2011	2010
Revenues:				
Rental and related revenue	$233,555	$228,299	$698,619	$642,489
General contractor and service fee revenue	127,708	132,351	409,617	414,391
	361,263	360,650	1,108,236	1,056,880
Expenses:				
Rental expenses	49,947	47,628	153,002	143,133
Real estate taxes	33,785	32,659	101,936	88,394
General contractor and other services expenses	120,547	124,653	379,180	392,433
Depreciation and amortization	96,909	94,487	290,751	253,209
	301,188	299,427	924,869	877,169
Other operating activities:				
Equity in earnings of unconsolidated companies	3,104	580	5,890	7,525
Gain on sale of properties	(1,437)	(125)	66,910	6,917
Undeveloped land carrying costs	(2,259)	(2,359)	(7,021)	(7,152)
Impairment charges	—	(1,860)	—	(9,834)
Other operating expenses	(60)	(580)	(171)	(1,002)
General and administrative expenses	(9,493)	(8,476)	(29,231)	(31,171)
	(10,145)	(12,820)	36,377	(34,717)
Operating income	49,930	48,403	219,744	144,994
Other income (expenses):				
Interest and other income, net	172	149	543	504
Interest expense	(66,875)	(61,491)	(199,269)	(175,076)
Loss on debt transactions	—	(167)	—	(16,294)
Acquisition-related activity	(342)	57,513	(1,525)	57,513
Income (loss) from continuing operations before income taxes	(17,115)	44,407	19,493	11,641
Income tax benefit	194	1,126	194	1,126
Income (loss) from continuing operations	(16,921)	45,533	19,687	12,767
Discontinued operations:				
Income (loss) before gain on sales	(36)	375	(30)	2,293
Gain on sale of depreciable properties	2,088	11,527	16,405	24,383
Income from discontinued operations	2,052	11,902	16,375	26,676
Net income (loss)	(14,869)	57,435	36,062	39,443
Dividends on preferred shares	(14,399)	(16,726)	(46,347)	(53,452)
Adjustments for redemption/repurchase of preferred shares	(3,633)	(5,652)	(3,796)	(10,144)
Net (income) loss attributable to noncontrolling interests	825	(993)	532	562
Net income (loss) attributable to common shareholders	$(32,076)	$34,064	$(13,549)	$(23,591)
Basic net income (loss) per common share:				
Continuing operations attributable to common shareholders	$(0.14)	$0.08	$(0.13)	$(0.22)
Discontinued operations attributable to common shareholders	0.01	0.05	0.07	0.11
Total	$(0.13)	$0.13	$(0.06)	$(0.11)

Diluted net income (loss) per common share:				
Continuing operations attributable to common shareholders	$(0.14)	$0.08	$(0.13)	$(0.22)
Discontinued operations attributable to common shareholders	0.01	0.05	0.07	0.11
Total	$(0.13)	$0.13	$(0.06)	$(0.11)
Weighted average number of common shares outstanding	252,802	251,866	252,618	234,468
Weighted average number of common shares and potential dilutive securities	252,802	257,383	252,618	234,468

See accompanying Notes to Consolidated Financial Statements

DUKE REALTY CORPORATION AND SUBSIDIARIES
Consolidated Statements of Cash Flows
For the nine months ended September 30,
(in thousands)
(Unaudited)

	2011	2010
Cash flows from operating activities:		
Net income	$36,062	$39,443
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation of buildings and tenant improvements	204,134	201,352
Amortization of deferred leasing and other costs	88,295	62,734
Amortization of deferred financing costs	11,070	10,492
Straight-line rent adjustment	(19,012)	(12,252)
Impairment charges	—	9,834
Loss on debt extinguishment	—	16,294
Gain on acquisitions, net	—	(57,815)
Earnings from land and depreciated property sales	(83,315)	(31,300)
Third-party construction contracts, net	(18,417)	(16,872)
Other accrued revenues and expenses, net	14,586	13,293
Operating distributions received in excess of equity in earnings from unconsolidated companies	11,681	7,649
Net cash provided by operating activities	245,084	242,852
Cash flows from investing activities:		
Development of real estate investments	(125,676)	(82,372)
Acquisition of real estate investments and related intangible assets, net of cash acquired	(179,047)	(260,877)
Acquisition of undeveloped land	(3,825)	(13,384)
Second generation tenant improvements, leasing costs and building improvements	(71,732)	(63,361)
Other deferred leasing costs	(20,950)	(26,060)
Other assets	(4,500)	(16,847)
Proceeds from land and depreciated property sales, net	504,688	200,445
Capital distributions from unconsolidated companies	54,730	3,897
Capital contributions and advances to unconsolidated companies, net	(28,362)	(48,410)
Net cash provided by (used for) investing activities	125,326	(306,969)
Cash flows from financing activities:		
Proceeds from issuance of common shares, net	—	297,896
Payments for redemption/repurchase of preferred shares	(110,726)	(115,849)
Proceeds from unsecured debt issuance	—	250,000
Payments on and repurchases of unsecured debt	(166,346)	(392,181)
Proceeds from secured debt financings	—	3,987
Payments on secured indebtedness including principal amortization	(24,841)	(8,814)
Borrowings on lines of credit, net	111,247	82,210
Distributions to common shareholders	(128,817)	(119,116)
Distributions to preferred shareholders	(46,347)	(53,452)
Distributions to noncontrolling interests	(3,952)	(4,844)
Deferred financing costs	(2,830)	(2,193)
Net cash used for financing activities	(372,612)	(62,356)
Net decrease in cash and cash equivalents	(2,202)	(126,473)
Cash and cash equivalents at beginning of period	18,384	147,322
Cash and cash equivalents at end of period	$16,182	$20,849
Non-cash investing and financing activities:		
Assumption of indebtedness and other liabilities in real estate acquisitions	$150,042	$332,982

Contribution of properties to unconsolidated companies	$53,245	$7,002
Investment and advances related to acquisition of previously unconsolidated companies	$5,987	$134,026
Conversion of Limited Partner Units to common shares	$3,052	$(7,829)
Issuance of Limited Partner Units for acquisition	$28,357	$—

See accompanying Notes to Consolidated Financial Statements

DUKE REALTY CORPORATION AND SUBSIDIARIES
Consolidated Statement of Changes in Equity
For the nine months ended September 30, 2011
(in thousands, except per share data)
(Unaudited)

	Common Shareholders						
	Preferred Stock	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Distributions in Excess of Net Income	Non-Controlling Interests	Total
Balance at December 31, 2010	$904,540	$2,522	$3,573,720	$(1,432)	$(1,533,740)	$44,293	$2,989,903
Comprehensive income:							
Net income	—	—	—	—	36,594	(532)	36,062
Derivative instrument activity	—	—	—	1,925	—	—	1,925
Comprehensive income							37,987
Issuance of Limited Partner Units for acquisition	—	—	—	—	—	28,357	28,357
Stock based compensation plan activity	—	4	10,912	—	(2,378)	—	8,538
Conversion of Limited Partner Units	—	3	3,049	—	—	(3,052)	—
Distributions to preferred shareholders	—	—	—	—	(46,347)	—	(46,347)
Redemption/repurchase of preferred shares	(110,630)	—	3,700	—	(3,796)	—	(110,726)
Distributions to common shareholders ($0.51 per share)	—	—	—	—	(128,817)	—	(128,817)
Distributions to noncontrolling interests	—	—	—	—	—	(3,952)	(3,952)
Balance at September 30, 2011	$793,910	$2,529	$3,591,381	$493	$(1,678,484)	$65,114	$2,774,943

See accompanying Notes to Consolidated Financial Statements

DUKE REALTY CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. General Basis of Presentation

The interim consolidated financial statements included herein have been prepared by Duke Realty Corporation (the "Company"). The 2010 year-end consolidated balance sheet data included in this Quarterly Report on Form 10-Q (this "Report") was derived from the audited financial statements in our Annual Report on Form 10-K for the year ended December 31, 2010, but does not include all disclosures required by accounting principles generally accepted in the United States of America ("GAAP"). The financial statements have been prepared in accordance with GAAP for interim financial information and in accordance with Rule 10-01 of Regulation S-X of the Securities Exchange Act of 1934, as amended. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and revenue and expenses during the reporting period. Our actual results could differ from those estimates and assumptions. These financial statements should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations included herein and the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2010.

We believe that we qualify as a real estate investment trust ("REIT") under the provisions of the Internal Revenue Code of 1986, as amended (the "Code"). Substantially all of our Rental Operations (see Note 9) are conducted through Duke Realty Limited Partnership ("DRLP"). We owned approximately 97.3% of the common partnership interests of DRLP ("Units") at September 30, 2011. At the option of the holders, and subject to certain restrictions, the remaining Units are redeemable for shares of our common stock on a one-to-one basis and earn dividends at the same rate as shares of our common stock. If it is determined to be necessary in order to continue to qualify as a REIT, we may elect to purchase the Units for an equivalent amount of cash rather than issuing shares of common stock upon redemption. We conduct our Service Operations (see Note 9) through Duke Realty Services, LLC, Duke Realty Services Limited Partnership and Duke Construction Limited Partnership ("DCLP"). DCLP is owned through a taxable REIT subsidiary. The consolidated financial statements include our accounts and the accounts of our majority-owned or controlled subsidiaries. In this Report, unless the context indicates otherwise, the terms "we," "us" and "our" refer to the Company and those entities owned or controlled by the Company.

2. Reclassifications

Certain amounts in the accompanying consolidated financial statements for 2010 have been reclassified to conform to the 2011 consolidated financial statement presentation.

3. Variable Interest Entities

At September 30, 2011, there are three unconsolidated joint ventures that we have determined meet the criteria to be considered variable interest entities ("VIEs"). These three unconsolidated joint ventures were formed with the sole purpose of developing, constructing, leasing, marketing and selling or operating properties. The business activities of these unconsolidated joint ventures have been financed through a combination of equity contributions, partner/member loans, and third-party debt that is guaranteed by both us and the other partner/member of each entity. All significant decisions for these unconsolidated joint ventures, including those decisions that most significantly impact each venture's economic performance, require unanimous approval of each joint venture's partners or members. In certain cases, these decisions also require lender approval. Unanimous approval requirements for these unconsolidated joint ventures include entering into new leases, setting annual operating budgets, selling underlying properties, and incurring additional indebtedness. Because no single entity exercises control over the decisions that most significantly affect each joint venture's economic performance, we determined that the equity method of accounting is appropriate.

The following is a summary of the carrying value in our consolidated balance sheet, as well as our maximum loss exposure under guarantees for the three unconsolidated subsidiaries that we have determined to be VIEs as of September 30, 2011 (in millions):

	Carrying Value	Maximum Loss Exposure
Investment in Unconsolidated Company	$33.2	$33.2
Guarantee Obligations (1)	$(18.9)	$(58.3)

(1) We are party to guarantees of the third-party debt of these joint ventures and our maximum loss exposure is equal to the maximum monetary obligation pursuant to the guarantee agreements. In 2009, we recorded a liability for our probable future obligation under a guarantee to the lender of one of these ventures. Pursuant to an agreement with the lender, we may make partner loans to this joint venture that will reduce our maximum guarantee obligation on a dollar-for-dollar basis. The carrying value of our recorded guarantee obligations is included in other liabilities in our Consolidated Balance Sheets.

4. Acquisitions and Dispositions

Acquisition of Premier Portfolio

We purchased twelve industrial and four office buildings, as well as other real estate assets, during the nine months ended September 30, 2011. These purchases completed our acquisition of a portfolio of buildings in South Florida (the “Premier Portfolio”), which was placed under contract in 2010, and resulted in cash payments to the sellers of $27.4 million, the assumption of secured loans with a face value of $124.4 million and the issuance to the sellers of 2.1 million Units with a fair value at issuance of $28.4 million (Note 6). These units are not convertible until early 2012. On December 30, 2010, we purchased 38 industrial buildings, one office building and other real estate assets within the Premier Portfolio. The allocation of the fair value of the amounts recognized from this acquisition to buildings and other related assets was preliminary at December 31, 2010. The following table summarizes our allocation of the fair value of amounts recognized for each major class of assets and liabilities related to the 55 properties and other real estate assets from the Premier Portfolio that have been purchased through September 30, 2011 (in thousands):

	Acquired During Year ended December 31, 2010	Acquired During Nine months ended September 30, 2011	Total
Real estate assets	$249,960	$153,656	$403,616
Lease-related intangible assets	31,091	25,445	56,536
Other assets	1,801	2,571	4,372
Total acquired assets	282,852	181,672	464,524
Secured debt	158,238	125,003	283,241
Other liabilities	4,075	4,284	8,359
Total assumed liabilities	162,313	129,287	291,600
Fair value of acquired net assets	$120,539	$52,385	$172,924

The leases in the acquired properties had a weighted average remaining life at acquisition of approximately 3.5 years.

Other 2011 Acquisitions

We also acquired 14 additional properties during the nine months ended September 30, 2011. These acquisitions consisted of five bulk industrial properties in Raleigh, North Carolina, two bulk industrial properties in Chicago, Illinois, one bulk industrial property in Dallas, Texas, one bulk industrial property in Southern California, one bulk industrial property in Phoenix, Arizona, one bulk industrial property in Savannah, Georgia, one office property in Raleigh, North Carolina, one office property in Indianapolis, Indiana and one office property in Atlanta, Georgia. Our acquisition accounting is preliminary for seven of the acquired buildings, which were acquired in September 2011. The following table summarizes our allocation of the fair value of amounts recognized for each major class of assets and liabilities (in thousands) for these acquisitions:

Real estate assets	$161,825
Lease related intangible assets	22,879
Other assets	338
Total acquired assets	185,042
Secured debt	20,138
Other liabilities	1,588

Total assumed liabilities	21,726
Fair value of acquired net assets	$163,316

The leases in the acquired properties had a weighted average remaining life at acquisition of approximately 6.8 years.

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Fair Value Measurements

The fair value estimates used in allocating the aggregate purchase price of each acquisition among the individual components of real estate assets and liabilities were determined primarily through calculating the “as-if vacant” value of each building, using the income approach, and relied significantly upon internally determined assumptions. As a result, we have, thus, determined these estimates to have been primarily based upon Level 3 inputs, which are unobservable inputs based on our own assumptions. The range of most significant assumptions utilized in making the lease-up and future disposition estimates used in calculating the “as-if vacant” value of each building acquired during the nine months ended September 30, 2011 were as follows:

	Low	High
Discount rate	6.40%	10.10%
Exit capitalization rate	4.80%	9.00%
Lease-up period (months)	12	36
Net rental rate per square foot – Industrial	$2.75	$6.50
Net rental rate per square foot – Office	$8.61	$16.00

Dispositions

We disposed of income-producing real estate assets and undeveloped land and received net proceeds of $504.7 million during the nine months ended September 30, 2011. Included in the building dispositions in the nine months ended September 30, 2011 is the sale, in March 2011, of 13 suburban office buildings, totaling approximately 2.0 million square feet, to an existing 20% owned unconsolidated joint venture. These buildings were sold to the unconsolidated joint venture for $342.8 million and our share of net proceeds totaled $273.7 million.

5. Indebtedness

The following table summarizes the book value and changes in the fair value of our debt for the nine months ended September 30, 2011 (in thousands):

	Book Value at 12/31/10	Book Value at 9/30/11	Fair Value at 12/31/10	Issuances and Assumptions	Payoffs	Adjustments to Fair Value	Fair Value at 9/30/11
Fixed rate secured debt	$1,042,722	$1,162,147	$1,069,562	$143,732	$(24,056)	$75,065	$1,264,303
Variable rate secured debt	22,906	22,121	22,906	—	(785)	—	22,121
Unsecured notes	2,948,405	2,783,762	3,164,651	—	(166,345)	(63,773)	2,934,533
Unsecured lines of credit	193,046	304,293	193,224	111,248	—	4,815	309,287
Total	$4,207,079	$4,272,323	$4,450,343	$254,980	$(191,186)	$16,107	$4,530,244

Fixed Rate Secured Debt

Because our fixed rate secured debt is not actively traded in any marketplace, we utilized a discounted cash flow methodology to determine its fair value. Accordingly, we calculated fair value by applying an estimate of the current market rate to discount the debt’s remaining contractual cash flows. Our estimate of a current market rate, which is the most significant input in the discounted cash flow calculation, is intended to replicate debt of similar maturity and loan-to-value relationship. The estimated rates ranged from 2.70% to 6.20%, depending on the attributes of the specific loans. The current market rates we utilized were internally estimated; therefore, we have concluded that our determination of fair value for our fixed rate secured debt was primarily based upon Level 3 inputs.

We assumed eleven secured loans, in conjunction with our acquisition activity, in the first nine months of 2011. These acquired secured loans had a total face value of $143.7 million and fair value of $145.1 million. The assumed loans carry a weighted average stated interest rate of 5.75% and a weighted remaining term upon acquisition of 5.2 years. We used estimated market rates ranging between 4.40% and 5.81% in determining the fair value of the loans.

Unsecured Notes

In March 2011, we repaid $42.5 million of senior unsecured notes, which had an effective interest rate of 6.96%, at their scheduled maturity date. In August 2011, we repaid $122.5 million of senior unsecured notes, which had an effective interest rate of 5.69%, at their scheduled maturity date.

All but $21.0 million of our unsecured notes bear interest at fixed rates. We utilized broker estimates in estimating the fair value of our fixed rate unsecured debt. Our unsecured notes are thinly traded and, in certain cases, the broker estimates were not based upon comparable transactions. The broker estimates took into account any recent trades within the same series of our fixed rate unsecured debt, comparisons to recent trades of other series of our fixed rate unsecured debt, trades of fixed rate unsecured debt from companies with profiles similar to ours, as well as overall economic conditions. We reviewed these broker estimates for reasonableness and accuracy, considering whether the estimates were based upon market participant assumptions within the principal and most advantageous market and whether any other observable inputs would be more accurate indicators of fair value than the broker estimates. We concluded that the broker estimates were representative of fair value. We have determined that our estimation of the fair value of our fixed rate unsecured debt was primarily based upon Level 3 inputs, as defined. The estimated trading values of our fixed rate unsecured debt, depending on the maturity and coupon rates, ranged from 100.00% to 115.00% of face value.

The indentures (and related supplemental indentures) governing our outstanding series of notes also require us to comply with financial ratios and other covenants regarding our operations. We were in compliance with all such covenants as of September 30, 2011.

Unsecured Lines of Credit

Our unsecured lines of credit as of September 30, 2011 are described as follows (in thousands):

Description	Maximum Capacity	Maturity Date	Outstanding Balance at September 30, 2011
Unsecured Line of Credit - DRLP	$850,000	February 2013	$284,000
Unsecured Line of Credit - Consolidated Subsidiary	$30,000	July 2012	$20,293

The DRLP unsecured line of credit has an interest rate on borrowings of LIBOR plus 2.75% (equal to 2.98% for borrowings as of September 30, 2011), and a maturity date of February 2013. Subject to certain conditions, the terms also include an option to increase the facility by up to an additional $200.0 million, for a total of up to $1.05 billion.

This line of credit provides us with an option to obtain borrowings from financial institutions that participate in the line at rates that may be lower than the stated interest rate, subject to certain restrictions.

This line of credit contains financial covenants that require us to meet certain financial ratios and defined levels of performance, including those related to fixed charge coverage and debt-to-asset value (with asset value being defined in the DRLP unsecured line of credit agreement). As of September 30, 2011, we were in compliance with all covenants under this line of credit.

The consolidated subsidiary’s unsecured line of credit allows for borrowings up to $30.0 million at a rate of LIBOR plus 0.85% (equal to 1.09% for outstanding borrowings as of September 30, 2011). This unsecured line of credit is used to fund development activities within the consolidated subsidiary and matures in July 2012.

To the extent that there are outstanding borrowings, we utilize a discounted cash flow methodology in order to estimate the fair value of our unsecured lines of credit. The net present value of the difference between future contractual interest payments and future interest payments based on our estimate of a current market rate represents the difference between the book value and the fair value. Our estimate of a current market rate is based upon the rate, considering current market conditions and our specific credit profile, at which we estimate we could obtain similar borrowings. The current market rate of 1.74% that we utilized was internally estimated; therefore, we have concluded that our determination of fair value for our unsecured lines of credit was primarily based upon Level 3 inputs.

6. Shareholders' Equity

In the first nine months of 2011, we repurchased 80,000 shares of our 8.375% Series O Cumulative Redeemable Preferred Shares (“Series O Shares”). The Series O Shares that we repurchased had a total redemption value of $2.0 million and were repurchased for $2.1 million. An adjustment of approximately $163,000, which included a ratable portion of original issuance costs, was included as a reduction to net income attributable to common shareholders.

In conjunction with the acquisition of the Premier Portfolio (Note 4), we issued 2.1 million Units with a fair value at issuance of $28.4 million, which are included in noncontrolling interests.

In July 2011, we redeemed all of the outstanding shares of our 7.25% Series N Cumulative Redeemable Preferred Shares at a liquidation amount of $108.6 million. Offering costs of $3.6 million were charged against net income attributable to common shareholders in conjunction with the redemption of these shares.

7. Related Party Transactions

We provide property management, asset management, leasing, construction and other tenant related services to unconsolidated companies in which we have equity interests. We recorded the corresponding fees based on contractual terms that approximate market rates for these types of services and we have eliminated our ownership percentage of these fees in the consolidated financial statements. The following table summarizes the fees earned from these companies for the nine months ended September 30, 2011 and 2010, respectively (in thousands):

	Nine Months Ended September 30,	
	2011	2010
Management fees	$7,393	$5,850
Leasing fees	3,627	2,143
Construction and development fees	4,182	6,716

8. Net Income (Loss) Per Common Share

Basic net income (loss) per common share is computed by dividing net income (loss) attributable to common shareholders, less dividends on share-based awards expected to vest (referred to as "participating securities" and primarily composed of unvested restricted stock units), by the weighted average number of common shares outstanding for the period. Diluted net income (loss) per common share is computed by dividing the sum of basic net income (loss) attributable to common shareholders and the noncontrolling interest in earnings allocable to Units not owned by us (to the extent the Units are dilutive) by the sum of the weighted average number of common shares outstanding and, to the extent they are dilutive, Units outstanding, as well as any potential dilutive securities for the period.

The following table reconciles the components of basic and diluted net income (loss) per common share for the three and nine months ended September 30, 2011 and 2010, respectively (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Net income (loss) attributable to common shareholders	$(32,076)	$34,064	$(13,549)	$(23,591)
Less: Dividends on participating securities	(811)	(694)	(2,416)	(1,699)
Basic net income (loss) attributable to common shareholders	(32,887)	33,370	(15,965)	(25,290)
Noncontrolling interest in earnings of common unitholders	—	1,041	—	—
Diluted net income (loss) attributable to common shareholders	$(32,887)	$34,411	$(15,965)	$(25,290)
Weighted average number of common shares outstanding	252,802	251,866	252,618	234,468
Weighted average partnership Units outstanding	—	5,517	—	—
Other potential dilutive shares	—	—	—	—
Weighted average number of common shares and potential dilutive securities	252,802	257,383	252,618	234,468

The partnership Units are anti-dilutive for the three and nine months ended September 30, 2011 and the nine months ended September 30, 2010 as a result of the net loss for these periods. In addition, potential shares related to our stock-based compensation plans as well as our 3.75% Exchangeable Senior Notes ("Exchangeable Notes") are anti-dilutive for all periods presented. The following table summarizes the data that is excluded from the computation of net income (loss) per common share as a result of being anti-dilutive (in thousands):

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	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Noncontrolling interest in earnings of common unitholders	$(868)	$—	$(369)	$(620)
Weighted average partnership Units outstanding	7,064	—	6,887	6,172
Other potential dilutive shares:				
Anti-dilutive outstanding potential shares under fixed stock option plans	1,677	1,779	1,677	1,779
Anti-dilutive potential shares under the Exchangeable Notes	3,432	4,045	3,432	4,045
Outstanding participating securities	4,840	4,137	4,840	4,137

9. Segment Reporting

We have three reportable operating segments, the first two of which consist of the ownership and rental of (i) office and (ii) industrial real estate investments. The operations of our office and industrial properties, along with our medical office and retail properties, are collectively referred to as "Rental Operations." Our medical office and retail properties do not by themselves meet the quantitative thresholds for separate presentation as reportable segments. The third reportable segment consists of various real estate services such as property management, asset management, maintenance, leasing, development and construction management to third-party property owners and joint ventures, and is collectively referred to as "Service Operations." Our reportable segments offer different products or services and are managed separately because each segment requires different operating strategies and management expertise.

Other revenue consists of other operating revenues not identified with one of our operating segments. Interest expense and other non-property specific revenues and expenses are not allocated to individual segments in determining our performance measure.

We assess and measure our overall operating results based upon an industry performance measure referred to as Funds From Operations ("FFO"), which management believes is a useful indicator of our consolidated operating performance. FFO is used by industry analysts and investors as a supplemental operating performance measure of a REIT. The National Association of Real Estate Investment Trusts ("NAREIT") created FFO as a supplemental measure of REIT operating performance that excludes historical cost depreciation, among other items, from net income determined in accordance with GAAP. FFO is a non-GAAP financial measure. The most comparable GAAP measure is net income (loss) attributable to common shareholders. FFO attributable to common shareholders should not be considered as a substitute for net income (loss) attributable to common shareholders or any other measures derived in accordance with GAAP and may not be comparable to other similarly titled measures of other companies. FFO is calculated in accordance with the definition that was adopted by the Board of Governors of NAREIT. We do not allocate certain income and expenses ("Non-Segment Items", as shown in the table below) to our operating segments. Thus, the operational performance measure presented here on a segment-level basis represents net earnings, excluding depreciation expense and the Non-Segment Items not allocated, and is not meant to present FFO as defined by NAREIT.

Historical cost accounting for real estate assets in accordance with GAAP implicitly assumes that the value of real estate assets diminishes predictably over time. Since real estate values instead have historically risen or fallen with market conditions, many industry analysts and investors have considered presentation of operating results for real estate companies that use historical cost accounting to be insufficient by themselves. FFO, as defined by NAREIT, represents GAAP net income (loss), excluding extraordinary items as defined under GAAP and gains or losses from sales of previously depreciated real estate assets, plus certain non-cash items such as real estate asset depreciation and amortization, and after similar adjustments for unconsolidated partnerships and joint ventures.

Management believes that the use of FFO attributable to common shareholders, combined with net income (which remains the primary measure of performance), improves the understanding of operating results of REITs among the investing public and makes comparisons of REIT operating results more meaningful. Management believes that excluding gains or losses related to sales of previously depreciated real estate assets and excluding real estate asset depreciation and amortization enables investors and analysts to readily identify the operating results of the long-term assets that form the core of a REIT's activity and assist them in comparing these operating results between periods or between different companies.

The following table shows (i) the revenues for each of the reportable segments and (ii) a reconciliation of FFO attributable to common shareholders to net income (loss) attributable to common shareholders for the three and nine months ended September 30, 2011 and 2010, respectively (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Revenues				
Rental Operations:				
Office	$111,376	$124,397	$340,483	$371,206
Industrial	98,874	84,249	290,219	212,832
Non-reportable Rental Operations segments	20,334	16,495	59,698	49,453
General contractor and service fee revenue (“Service Operations”)	127,708	132,351	409,617	414,391
Total Segment Revenues	358,292	357,492	1,100,017	1,047,882
Other Revenue	2,971	3,158	8,219	8,998
Consolidated Revenue from continuing operations	361,263	360,650	1,108,236	1,056,880
Discontinued Operations	1,341	11,385	7,506	38,276
Consolidated Revenue	$362,604	$372,035	$1,115,742	$1,095,156
Reconciliation of Funds From Operations				
Net earnings excluding depreciation and Non-Segment Items				
Office	$62,768	$72,015	$191,787	$213,409
Industrial	72,006	62,716	208,925	158,395
Non-reportable Rental Operations segments	13,115	10,729	38,513	32,884
Service Operations	7,161	7,698	30,437	21,958
	155,050	153,158	469,662	426,646
Non-Segment Items:				
Interest expense	(66,875)	(61,491)	(199,269)	(175,076)
Impairment charges	—	(1,860)	—	(9,834)
Interest and other income	172	149	543	504
Other operating expenses	(60)	(580)	(171)	(1,002)
General and administrative expenses	(9,493)	(8,476)	(29,231)	(31,171)
Undeveloped land carrying costs	(2,259)	(2,359)	(7,021)	(7,152)
Loss on debt transactions	—	(167)	—	(16,294)
Acquisition-related activity	(342)	57,513	(1,525)	57,513
Income tax benefit	194	1,126	194	1,126
Other non-segment income	1,934	2,552	4,456	6,274
Net (income) loss attributable to noncontrolling interests	825	(993)	532	562
Noncontrolling interest share of FFO adjustments	(2,835)	(2,018)	(6,206)	(6,611)
Joint venture items	11,635	7,916	30,597	32,488
Dividends on preferred shares	(14,399)	(16,726)	(46,347)	(53,452)
Adjustments for redemption/repurchase of preferred shares	(3,633)	(5,652)	(3,796)	(10,144)
Discontinued operations	390	3,801	1,648	13,170
FFO attributable to common shareholders	70,304	125,893	214,066	227,547
Depreciation and amortization on continuing operations	(96,909)	(94,487)	(290,751)	(253,209)
Depreciation and amortization on discontinued operations	(426)	(3,426)	(1,678)	(10,877)
Company’s share of joint venture adjustments	(8,531)	(7,336)	(24,798)	(27,271)
Earnings from depreciated property sales on continuing operations	(1,437)	(125)	66,910	6,917
Earnings from depreciated property sales on discontinued operations	2,088	11,527	16,405	24,383
Earnings from depreciated property sales—share of joint venture	—	—	91	2,308
Noncontrolling interest share of FFO adjustments	2,835	2,018	6,206	6,611
Net income (loss) attributable to common shareholders	$(32,076)	$34,064	$(13,549)	$(23,591)

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The assets for each of the reportable segments as of September 30, 2011 and December 31, 2010 are as follows (in thousands):

	September 30, 2011	December 31, 2010
Assets		
Rental Operations:		
Office	$2,759,739	$3,122,565
Industrial	3,388,125	3,210,566
Non-reportable Rental Operations segments	640,885	627,491
Service Operations	175,839	231,662
Total Segment Assets	6,964,588	7,192,284
Non-Segment Assets	540,073	451,992
Consolidated Assets	$7,504,661	$7,644,276

10. Discontinued Operations and Assets Held for Sale

The following table illustrates the number of properties in discontinued operations:

	Held for Sale at September 30, 2011	Sold in 2011	Sold in 2010	Total
Office	3	11	11	25
Industrial	0	3	6	9
Retail	0	0	2	2
	3	14	19	36

We allocate interest expense to discontinued operations and have included such interest expense in computing income from discontinued operations. Interest expense allocable to discontinued operations includes interest on any secured debt for properties included in discontinued operations and an allocable share of our consolidated unsecured interest expense for unencumbered properties. The allocation of unsecured interest expense to discontinued operations was based upon the gross book value of the unencumbered real estate assets included in discontinued operations as it related to the total gross book value of our unencumbered real estate assets.

The following table illustrates the operations of the buildings reflected in discontinued operations for the three and nine months ended September 30, 2011 and 2010, respectively (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Revenues	$1,341	$11,385	$7,506	$38,276
Operating expenses	(640)	(4,675)	(3,751)	(15,226)
Depreciation and amortization	(426)	(3,426)	(1,678)	(10,877)
Operating income	275	3,284	2,077	12,173
Interest expense	(311)	(2,909)	(2,107)	(9,880)
Income (loss) before gain on sales	(36)	375	(30)	2,293
Gain on sale of depreciable properties	2,088	11,527	16,405	24,383
Income from discontinued operations	$2,052	$11,902	$16,375	$26,676

Dividends on preferred shares and adjustments for the redemption or repurchase of preferred shares are allocated entirely to continuing operations. The following table illustrates the allocation of the income (loss) attributable to common shareholders between continuing operations and discontinued operations, reflecting an allocation of income or loss attributable to noncontrolling interests between continuing and discontinued operations, for the three and nine months ended September 30, 2011 and 2010, respectively (in thousands):

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	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Income (loss) from continuing operations attributable to common shareholders	$(34,072)	$22,417	$(29,490)	$(49,583)
Income from discontinued operations attributable to common shareholders	1,996	11,647	15,941	25,992
Net income (loss) attributable to common shareholders	$(32,076)	$34,064	$(13,549)	$(23,591)

At September 30, 2011, we classified three in-service properties as held-for-sale, which were included in discontinued operations, due to our present intention to sell the properties in October 2011. The following table illustrates aggregate balance sheet information of the aforementioned three properties included in discontinued operations at September 30, 2011 (in thousands):

Real estate investment, net	$18,466
Other assets	3,526
Total assets held-for-sale	$21,992
Accrued expenses	$666
Other liabilities	291
Total liabilities held-for-sale	