KILROY REALTY CORP
Form 10-K
February 12, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K
(MARK ONE)
S ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2012
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 1-12675 (Kilroy Realty Corporation)
Commission file number 000-54005 (Kilroy Realty, L.P.)
KILROY REALTY CORPORATION
KILROY REALTY, L.P.
(Exact name of registrant as specified in its charter)

Kilroy Realty Corporation	Maryland (State or other jurisdiction of incorporation or organization)	95-4598246 (I.R.S. Employer Identification No.)
Kilroy Realty, L.P.	Delaware (State or other jurisdiction of incorporation or organization)	95-4612685 (I.R.S. Employer Identification No.)

12200 W. Olympic Boulevard, Suite 200, Los Angeles, California 90064
(Address of principal executive offices) (Zip Code)
Registrant’s telephone number, including area code: (310) 481-8400
Securities registered pursuant to Section 12(b) of the Act:

Registrant	Title of each class	Name of each exchange on which registered
Kilroy Realty Corporation	Common Stock, $.01 par value	New York Stock Exchange
Kilroy Realty Corporation	6.875% Series G Cumulative Redeemable Preferred Stock, $.01 par value	New York Stock Exchange
Kilroy Realty Corporation	6.375% Series H Cumulative Redeemable Preferred Stock, $.01 par value	New York Stock Exchange

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

Registrant	Title of each class
Kilroy Realty, L.P.	Common Units Representing Limited Partnership Interests

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Kilroy Realty Corporation Yes x No £
Kilroy Realty, L. P. Yes x No £
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act.
Kilroy Realty Corporation Yes £ No x
Kilroy Realty, L. P. Yes £ No x
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.
Kilroy Realty Corporation Yes x No £
Kilroy Realty, L. P. 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Kilroy Realty Corporation Yes x No £
Kilroy Realty, L. P. Yes x No £

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x
Indicate by check mark whether the registrant is 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.

Kilroy Realty Corporation

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

Kilroy Realty, L.P.

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).
Kilroy Realty Corporation Yes £ No x
Kilroy Realty, L. P. Yes £ No x
The aggregate market value of the voting and non-voting shares of common stock held by non-affiliates of Kilroy Realty Corporation was approximately $2,382,187,648 based on the quoted closing price on the New York Stock Exchange for such shares on June 30, 2012.
The aggregate market value of the voting and non-voting common units of limited partnership interest held by non-affiliates of Kilroy Realty, L.P. was approximately $12,415,519 based on the quoted closing price on the New York Stock Exchange for Kilroy Realty Corporation shares on June 30, 2012.
As of February 11, 2013, 74,895,990 shares of Kilroy Realty Corporation's common stock, par value $.01 per share, were outstanding.
DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Kilroy Realty Corporation's Proxy Statement with respect to its 2013 Annual Meeting of Stockholders to be filed not later than 120 days after the end of the registrant’s fiscal year are incorporated by reference into Part III of this Form 10-K.

EXPLANATORY NOTE

This report combines the annual reports on Form 10-K for the year ended December 31, 2012 of Kilroy Realty Corporation and Kilroy Realty, L.P. Unless stated otherwise or the context otherwise requires, references to "Kilroy Realty Corporation" or the "Company," "we," "our," and "us" mean Kilroy Realty Corporation, a Maryland corporation, and it controlled and consolidated subsidiaries, and references to "Kilroy Realty, L.P." or the "Operating Partnership" mean Kilroy Realty, L.P., a Delaware limited partnership, and its controlled and consolidated subsidiaries.

The Company is a real estate investment trust, or REIT, and the general partner of the Operating Partnership. As of December 31, 2012, the Company owned an approximate 97.6% common general partnership interest in the Operating Partnership. The remaining approximate 2.4% common limited partnership interests are owned by non-affiliated investors and certain directors and officers of the Company. As the sole general partner of the Operating Partnership, the Company exercises exclusive and complete discretion over the Operating Partnership's day-to-day management and control and can cause it to enter into certain major transactions including acquisitions, dispositions, and refinancings and cause changes in its line of business, capital structure, and distribution policies.

There are a few differences between the Company and the Operating Partnership that are reflected in the disclosures in this Form 10-K. We believe it is important to understand the differences between the Company and the Operating Partnership in the context of how the Company and the Operating Partnership operate as an interrelated, consolidated company. The Company is a REIT, the only material asset of which is the partnership interests it holds in the Operating Partnership. As a result, the Company does not conduct business itself, other than acting as the sole general partner of the Operating Partnership, issuing equity from time to time and guaranteeing certain debt of the Operating Partnership. The Company itself is not directly obligated under any indebtedness, but guarantees some of the debt of the Operating Partnership. The Operating Partnership owns substantially all of the assets of the Company either directly or through its subsidiaries, conducts the operations of the Company's business and is structured as a limited partnership with no publicly-traded equity. Except for net proceeds from equity issuances by the Company, which the Company is required to contribute to the Operating Partnership in exchange for units of partnership interest, the Operating Partnership generates the capital required by the Company's business through the Operating Partnership's operations, by the Operating Partnership's incurrence of indebtedness or through the issuance of units of partnership interest.

Noncontrolling interests and stockholders' equity and partners' capital are the main areas of difference between the consolidated financial statements of the Company and those of the Operating Partnership. The common limited partnership interests in the Operating Partnership are accounted for as partners' capital in the Operating Partnership's financial statements and, to the extent not held by the Company, as noncontrolling interests in the Company's financial statements. The Operating Partnership's financial statements reflect the noncontrolling interest in Kilroy Realty Finance Partnership, L.P. a Delaware limited partnership (the "Finance Partnership"). This noncontrolling interest represents the Company's 1% indirect general partnership interest in the Finance Partnership, which is directly held by Kilroy Realty Finance, Inc., a wholly-owned subsidiary of the Company. The differences between stockholders' equity, partners' capital and noncontrolling interests result from the differences in the equity issued by the Company and the Operating Partnership, and in the Company's noncontrolling interest in the Finance Partnership.

We believe combining the annual reports on Form 10-K of the Company and the Operating Partnership into this single report results in the following benefits:

- Combined reports better reflect how management and the analyst community view the business as a single operating unit;
- Combined reports enhance investors' understanding of the Company and the Operating Partnership by enabling them to view the business as a whole and in the same manner as management;
- Combined reports are more efficient for the Company and the Operating Partnership and result in savings in time, effort and expense; and
- Combined reports are more efficient for investors by reducing duplicative disclosure and providing a single document for their review.

To help investors understand the significant differences between the Company and the Operating Partnership, this report presents the following separate sections for each of the Company and the Operating Partnership:

- consolidated financial statements;
- the following notes to the consolidated financial statements:

Note 6, Secured and Unsecured Debt of the Company;
Note 7, Secured and Unsecured Debt of the Operating Partnership;
Note 9, Noncontrolling Interests on the Company's Consolidated Financial Statements;

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Note 10, Stockholders' Equity of the Company;
Note 11, Preferred and Common Units of the Operating Partnership;
Note 19, Net Income Available to Common Stockholders Per Share of the Company;
Note 20, Net Income Available to Common Unitholders Per Unit of the Operating Partnership;
Note 22, Quarterly Financial Information of the Company (Unaudited);
Note 23, Quarterly Financial Information of the Operating Partnership (Unaudited);
Note 25, Pro Forma Results of the Company (Unaudited); and
Note 26, Pro Forma Results of the Operating Partnership (Unaudited);

- “Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources of the Company”; and

- “Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources of the Operating Partnership”.

This report also includes separate sections under Item 9A. Controls and Procedures and separate Exhibit 31 and Exhibit 32 certifications for each of the Company and the Operating Partnership to establish that the Chief Executive Officer and the Chief Financial Officer of each entity have made the requisite certifications and that the Company and Operating Partnership are compliant with Rule 13a-15 or Rule 15d-15 of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and 18 U.S.C. §1350.

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PART I

This document contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Exchange Act, including information concerning projected future occupancy and rental rates, lease expirations, debt maturity, potential investments, strategies such as capital recycling, development and redevelopment activity, projected construction costs, dispositions, future executive incentive compensation and other forward-looking financial data, as well as the discussion in “Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations-Factors That May Influence Future Results of Operations.” Forward-looking statements are based on our current expectations, beliefs and assumptions, and are not guarantees of future performance. Forward-looking statements are inherently subject to uncertainties, risks, changes in circumstances, trends and factors that are difficult to predict, many of which are outside of our control. Accordingly, actual performance, results and events may vary materially from those indicated in the forward-looking statements, and you should not rely on the forward-looking statements as predictions of future performance, results or outcomes. All forward-looking statements are based on currently available information and speak only as of the date on this report was filed with the Securities and Exchange Commission (the “SEC”).

ITEM 1. BUSINESS

The Company

We are a self-administered REIT active in office submarkets along the West Coast. We own, develop, acquire and manage real estate assets, consisting primarily of Class A properties in the coastal regions of Los Angeles, Orange County, San Diego County, the San Francisco Bay Area and greater Seattle, which we believe have strategic advantages and strong barriers to entry. Class A properties encompass attractive and efficient buildings of high quality that are attractive to tenants, are well-designed and constructed with above-average material, workmanship and finishes and are well-maintained and managed. We qualify as a REIT under the Internal Revenue Code of 1986, as amended (the "Code").

Our portfolio of operating properties was comprised of the following office buildings at December 31, 2012.

	Number of Buildings	Rentable Square Feet	Number of Tenants	Percentage Occupied	
Office Properties	114	13,249,780	530	92.8	%

During the fourth quarter of 2012 we disposed of our entire portfolio of 39 industrial properties and, as a result, no longer owned any industrial properties at December 31, 2012.

Our stabilized portfolio includes all of our properties with the exception of undeveloped land, development and redevelopment properties currently under construction or committed for construction, “lease-up” properties and properties held-for-sale. We define “lease-up” properties as properties we recently developed or redeveloped that have not yet reached 95% occupancy and are within one year following cessation of major construction activities. We define redevelopment properties as those projects for which we expect to spend significant development and construction costs on existing or acquired buildings pursuant to a formal plan, the intended result of which is a higher economic return on the property. Our stabilized portfolio also excludes our future development pipeline, which is comprised of nine potential development sites, including one office property moved from the stabilized portfolio to the development pipeline in the fourth quarter of 2012, representing 118.5 gross acres of undeveloped land.

As of December 31, 2012, the following properties were excluded from our stabilized portfolio:

	Number of Properties	Estimated Rentable Square Feet (1)
Development properties under construction	4	1,416,000
Redevelopment properties under construction	1	410,000
Lease-up properties	1	98,000

(1) Estimated rentable square feet upon completion.

As of December 31, 2012, all of our properties and development and redevelopment projects are owned and all of our business is currently conducted in the state of California with the exception of ten office properties located in the state of Washington. We had no properties held-for-sale as of December 31, 2012.

We own our interests in all of our office properties through the Operating Partnership and the Finance Partnership. We conduct substantially all of our operations through the Operating Partnership of which we owned a 97.6% general partnership interest as of December 31, 2012. The remaining 2.4% common limited partnership interest was owned by certain of our directors and executive officers and non-affiliated investors. Kilroy Realty Finance, Inc., a wholly-owned subsidiary of the Company, is the sole general partner of the Finance Partnership and owns a 1.0% general partnership interest. The Operating Partnership owns the remaining 99.0% limited partnership interest. We conduct substantially all of our development activities through Kilroy Services, LLC ("KSLLC"), which is a wholly-owned subsidiary of the Operating Partnership. With the exception of the Operating Partnership, all of the Company's subsidiaries are wholly-owned.

The following diagram illustrates our organizational structure as of December 31, 2012:

Available Information; Website Disclosure; Corporate Governance Documents

Kilroy Realty Corporation was incorporated in the state of Maryland on September 13, 1996 and Kilroy Realty, L.P. was organized in the state of Delaware on October 2, 1996. Our principal executive offices are located at 12200 W. Olympic Boulevard, Suite 200 Los Angeles, California 90064. Our telephone number at that location is (310) 481-8400. Our website is located at www.kilroyrealty.com. The information found on, or otherwise accessible through, our website is not incorporated into, and does not form a part of, this annual report on Form 10-K or any other report or document we file with or furnish to the SEC. All reports we will file with the SEC will be available free of charge via EDGAR through the SEC website at www.sec.gov. In addition, the public may read and copy materials we file with the SEC at the SEC's public reference room located at 100 F Street, N.E., Washington, D.C. 20549. All reports that we will file with the SEC will also be available free of charge on our website at www.kilroyrealty.com as soon as reasonably practicable after we file those materials with, or furnish them to, the SEC.

The following documents relating to corporate governance are also available free of charge on our website under "Investor Relations—Corporate Governance" and available in print to any security holder upon request:

- Corporate Governance Guidelines;
- Code of Business Conduct and Ethics;
- Audit Committee Charter;
- Executive Compensation Committee Charter; and
- Nominating / Corporate Governance Committee Charter.

You may request copies of any of these documents by writing to:

Attention: Investor Relations
Kilroy Realty Corporation
12200 West Olympic Boulevard, Suite 200
Los Angeles, California 90064

Business and Growth Strategies

Growth Strategies. We believe that a number of factors and strategies will enable us to continue to achieve our objectives of long-term sustainable growth in Net Operating Income (defined below) and FFO (defined below) as well as maximization of long-term stockholder value. These factors and strategies include:

- the quality and location of our properties;
- our ability to efficiently manage our assets as a low cost provider of commercial real estate through our seasoned management team possessing core capabilities in all aspects of real estate ownership, including property management, leasing, marketing, financing, accounting, legal, construction and development management;
- our ability to capitalize on inflection points in a real estate cycle to add quality assets to our portfolio at substantial discounts to long-term value, through either acquisition, development or redevelopment;
- our strong financial position that has and will continue to allow us to pursue attractive acquisition and development and redevelopment opportunities;
- our access to development, redevelopment, acquisition, and leasing opportunities as a result of our extensive experience and significant working relationships with major West Coast property owners, corporate tenants, municipalities, and landowners given our over 65-year presence in the West Coast markets;
- our capital recycling program (see "Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations —Liquidity Sources" for additional information pertaining to the Company's capital recycling program and related 2012 property dispositions); and
- our future development pipeline of undeveloped land sites.

"Net Operating Income" is defined as operating revenues (rental income, tenant reimbursements, and other property income) less property and related expenses (property expenses, real estate taxes, provision for bad debts, and ground leases) before depreciation. "FFO" is funds from operations as defined by the National Association of Real Estate

Investment Trusts ("NAREIT"). See "Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations —Results of Operations" and "—Non-GAAP Supplemental Financial Measures: Funds From Operations" for a reconciliation of these measures to generally accepted accounting principles ("GAAP") net income available to common stockholders.

Operating Strategies. We focus on enhancing long-term growth in Net Operating Income and FFO from our properties by:

- maximizing cash flow from our properties through active leasing, early renewals, and effective property management;
- structuring leases to maximize returns and internal growth;
- managing portfolio credit risk through effective underwriting, including the use of credit enhancements and interests in collateral to mitigate portfolio credit risk;
- managing operating expenses through the efficient use of internal management, leasing, marketing, financing, accounting, legal, and construction management functions;
- maintaining and developing long-term relationships with a diverse tenant base;
- managing our properties to offer the maximum degree of utility and operational efficiency to tenants;
- building substantially all of our recent development projects to Leadership in Energy and Environmental Design (LEED) specifications, achieving gold or silver certification levels for several of our buildings, including the first LEED Platinum ground-up commercial development in San Francisco at 350 Mission Street;
- actively pursuing LEED certification for over 3.2 million square feet of office space within our existing portfolio;
- aggressively pursuing high-performance environmental building initiatives that create economic value for our tenants, shareholders and employees;
- continuing to effectively manage capital improvements to enhance our properties' competitive advantages in their respective markets and improve the efficiency of building systems;
- enhancing our management team with individuals who have extensive regional experience and are highly knowledgeable in their respective markets; and
- attracting and retaining motivated employees by providing financial and other incentives to meet our operating and financial goals.

Acquisition Strategies. We believe we are well positioned to acquire properties and development and redevelopment opportunities as the result of our extensive experience, strong financial position, and ability to access capital. We continue to actively monitor our target markets and focus on acquiring additional high quality office properties and development and redevelopment opportunities that:

- provide attractive yields and significant potential for growth in cash flow from property operations;
- present growth opportunities in our existing or other strategic markets; and
- demonstrate the potential for improved performance through intensive management, repositioning and leasing that should result in increased occupancy and rental revenues.

Development and Redevelopment Strategies. We and our predecessors have developed office and industrial properties primarily located in California since 1947. As of December 31, 2012, our future development pipeline was comprised of nine potential development sites, representing 118.5 gross acres of undeveloped land on which we believe we have the potential to develop over two million rentable square feet of office space, depending upon economic conditions. Our strategy with respect to development is to:

- maintain a disciplined approach by emphasizing pre-leasing, commencing development in stages, or phasing, and cost control;
- continue to execute our build-to-suit philosophy in which we develop properties to be leased by specific committed tenants providing for lower-risk development;
- be the premier provider of modern and collaborative office buildings on the West Coast;
- reinvest capital from dispositions of nonstrategic assets into new state-of-the-market development and acquisition assets with higher cash flow and rates of return;
- evaluate redevelopment opportunities in supply-constrained markets because such efforts generally achieve similar returns to new development with reduced entitlement risk and shorter construction periods; and
- execute on our development projects under construction and our future development pipeline.

Redevelopment opportunities are those projects in which we spend significant development and construction costs on existing buildings pursuant to a formal plan, the intended result of which is a higher economic return on the property. We may engage in

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the additional development or redevelopment of office properties when market conditions support a favorable risk–adjusted return on such development or redevelopment. We expect that our significant working relationships with tenants, municipalities, and landowners on the West Coast will give us further access to development and redevelopment opportunities. We cannot assure you that we will be able to successfully develop or redevelop any of our properties or that we will have access to additional development or redevelopment opportunities.

Financing Strategies. Our financing policies and objectives are determined by our board of directors. Our goal is to limit our dependence on leverage and maintain a conservative ratio of debt-to-total market capitalization. As of December 31, 2012, our total debt as a percentage of total market capitalization was 34.7%, and our total debt and liquidation value of our preferred equity as a percentage of total market capitalization was 38.1%, both of which were calculated based on the quoted closing price per share of the Company's common stock of $47.37 on December 31, 2012 (see "Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources of the Company - Capitalization" for additional information). Our financing strategies include:

- maintaining financial flexibility, including a low secured to unsecured debt ratio, to maximize our ability to access a variety of both public and private capital sources;
- maintaining a staggered debt maturity schedule in which the maturity dates of our debt are spread over several years to limit risk exposure at any particular point in the capital and credit market cycles;
- completing financing in advance of the need for capital; and
- managing interest rate exposure by generally maintaining a greater amount of fixed-rate debt as compared to variable-rate debt.

We utilize multiple sources of capital, including borrowings under our unsecured line of credit, proceeds from the issuance of public or private debt or equity securities and other bank and/or institutional borrowings, and dispositions of nonstrategic assets. There can be no assurance that we will be able to obtain capital as needed on terms favorable to us or at all. See the discussion under the caption "Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations —Factors That May Influence Future Results of Operations" and "Item 1A: Risk Factors".

Significant Tenants

As of December 31, 2012, our 15 largest tenants in terms of annualized base rental revenues represented approximately 34.1% of our total annualized base rental revenues, defined as annualized monthly contractual rents from existing tenants as of December 31, 2012. Annualized base rental revenue includes the impact of straight-lining rent escalations and the amortization of free rent periods and excludes the impact of the following: amortization of deferred revenue related tenant-funded tenant improvements, amortization of above/below market rents, amortization for lease incentives due under existing leases, and expense reimbursement revenue.

For further information on our 15 largest tenants and the composition of our tenant base, see "Item 2: Properties —Significant Tenants."

Competition

We compete with several developers, owners, operators and acquirers of office and other commercial real estate, many of which own properties similar to ours in the same submarkets in which our properties are located. For further discussion of the potential impact of competitive conditions on our business, see "Item 1A: Risk Factors".

Segment and Geographic Financial Information

For the year ended December 31, 2012, we only had one segment, our office properties segment. During the fourth quarter of 2012, we sold our entire portfolio of industrial properties and, as a result, no longer owned any industrial properties at December 31, 2012. For information about our office property revenues and long-lived assets and other financial information, see Note 18 to our consolidated financial statements included in this report and "Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations -Results of Operations."

All of our properties are located and all of our business is currently conducted in the state of California with the exception of the ownership and operation of ten office properties located in the state of Washington.

Employees

As of December 31, 2012, we employed 201 people through the Operating Partnership, KSLLC, and Kilroy Realty TRS, Inc. We believe that relations with our employees are good.

Environmental Regulations and Potential Liabilities

Government Regulation Relating to the Environment. Many laws and governmental regulations relating to the environment are applicable to our properties, and changes in these laws and regulations, or their interpretation by agencies and the courts, occur frequently and may adversely affect us.

Existing conditions at some of our properties. Independent environmental consultants have conducted Phase I or similar environmental site assessments on all of our properties. We generally obtain these assessments prior to the acquisition of a property and may later update them as required for subsequent financing of the property or as requested by a tenant. Site assessments are generally performed to American Society for Testing and Materials standards then-existing for Phase I site assessments and typically include a historical review, a public records review, a visual inspection of the surveyed site, and the issuance of a written report. These assessments do not generally include any soil samplings or subsurface investigations. Depending on the age of the property, the Phase I may have included an assessment of asbestos-containing materials. For properties where asbestos-containing materials were identified or suspected, an operations and maintenance plan was generally prepared and implemented.

Historical operations at or near some of our properties, including the presence of underground or above ground storage tanks, may have caused soil or groundwater contamination. In some instances, the prior owners of the affected properties conducted remediation of known contamination in the soils on our properties, and we do not believe that further clean-up of the soils is required. We are not aware of any such condition, liability, or concern by any other means that would give rise to material environmental liability. However, the assessments may have failed to reveal all environmental conditions, liabilities, or compliance concerns; there may be material environmental conditions, liabilities, or compliance concerns that arose at a property after the review was completed; future laws, ordinances, or regulations may impose material additional environmental liability; and environmental conditions at our properties may be affected in the future by tenants, third parties, or the condition of land or operations near our properties, such as the presence of underground storage tanks. We cannot be certain that costs of future environmental compliance will not have an adverse effect on our financial condition, results of operations, cash flow, the quoted trading price of our securities, and our ability to satisfy our debt service obligations and to pay dividends and distributions to security holders.

Use of hazardous materials by some of our tenants. Some of our tenants handle hazardous substances and wastes on our properties as part of their routine operations. Environmental laws and regulations may subject these tenants, and potentially us, to liability resulting from such activities. We generally require our tenants in their leases to comply with these environmental laws and regulations and to indemnify us for any related liabilities. As of December 31, 2012, other than routine cleaning materials, approximately 5% of our tenants handled hazardous substances and/or wastes on less than 4% of the aggregate square footage of our properties as part of their routine operations. These tenants are primarily involved in the life sciences business. The hazardous substances and wastes are primarily comprised of diesel fuel for emergency generators and small quantities of lab and light manufacturing chemicals including, but not limited to, alcohol, ammonia, carbon dioxide, cryogenic gases, dichlorophenol, methane, naturalyte acid, nitrogen, nitrous oxide, and oxygen which are routinely used by life science companies. We are not aware of any material noncompliance, liability, or claim relating to hazardous or toxic substances or petroleum products in connection with any of our properties, and management does not believe that on-going activities by our tenants will have a material adverse effect on our operations.

Costs related to government regulation and private litigation over environmental matters. Under applicable environmental laws and regulations, we may be liable for the costs of removal, remediation, or disposal of certain hazardous or toxic substances present or released on our properties. These laws could impose liability without regard to whether we are responsible for, or even knew of, the presence or release of the hazardous materials. Government investigations and remediation actions may have substantial costs, and the presence or release of hazardous substances on a property could result in governmental clean-up actions, personal injury actions, or similar claims by private plaintiffs.

Potential environmental liabilities may exceed our environmental insurance coverage limits or transactional indemnities. We carry what we believe to be commercially reasonable environmental insurance. Our environmental insurance policies are subject to various terms, conditions and exclusions. Similarly, in connection with some transactions we obtain environmental indemnities that may not be honored by the indemnitors or may fail to address resulting liabilities adequately. Therefore, we cannot provide any assurance that our insurance coverage or transactional indemnities will be sufficient or that our liability, if any, will not have a material adverse effect on our financial condition, results of operations, cash flows, quoted trading price of our securities, and our ability to satisfy our debt service obligations and to pay dividends and distributions to security holders.

ITEM 1ARISK FACTORS

The following section sets forth material factors that may adversely affect our business and operations. The following factors, as well as the factors discussed in “Item 7: Management’s Discussion and Analysis of Financial Condition and Results of Operations —Factors That May Influence Future Results of Operations” and other information contained in this report, should be considered in evaluating us and our business.

Risks Related to our Business and Operations

Global market and economic conditions may adversely affect our liquidity and financial condition and those of our tenants. In the United States, market and economic conditions continue to be challenging with stricter regulations and modest growth. While recent economic data reflects moderate economic growth in the United States, the cost and availability of credit may continue to be adversely affected by governmental budget and global economic factors. Concern about continued stability of the economy and credit markets generally, and the strength of counterparties specifically, has led many lenders and institutional investors to reduce and, in some cases, cease to provide funding to borrowers. Volatility in the U.S. and international capital markets and concern over a return to recessionary conditions in global economies, and in the California economy in particular, may adversely affect our liquidity and financial condition and the liquidity and financial condition of our tenants. If these market conditions continue, they may limit our ability and the ability of our tenants to timely refinance maturing liabilities and access the capital markets to meet liquidity needs.

All of our properties are located in California and Greater Seattle, Washington and we may therefore be susceptible to adverse economic conditions and regulations, as well as natural disasters, in those areas. Because all of our properties are concentrated in California and Seattle, Washington we may be exposed to greater economic risks than if we owned a more geographically dispersed portfolio. Further, within California, our properties are concentrated in Los Angeles, Orange County, San Diego County, and the San Francisco Bay Area, exposing us to risks associated with those specific areas. We are susceptible to adverse developments in the economic and regulatory environments of California and Greater Seattle, Washington (such as business layoffs or downsizing, industry slowdowns, relocations of businesses, increases in real estate and other taxes, costs of complying with governmental regulations or increased regulation and other factors) as well as adverse weather conditions and natural disasters that occur in these areas (such as earthquakes, wind, landslides, fires and other events). In addition, California is also regarded as more litigious and more highly regulated and taxed than many other states, which may reduce demand for office space in California.

Any adverse developments in the economy or real estate market in California and the surrounding region, or in Seattle, Washington or any decrease in demand for office space resulting from the California or Seattle regulatory or business environment could impact our ability to generate revenues sufficient to meet our operating expenses or other obligations, which would adversely impact our financial condition, results of operations, cash flows, the quoted trading price of the Company's common stock and of the Operating Partnership's publicly-traded notes and our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders.

Our performance and the market value of our securities are subject to risks associated with our investments in real estate assets and with trends in the real estate industry. Our economic performance and the value of our real estate assets and, consequently the market value of the Company's securities, are subject to the risk that our properties may not generate revenues sufficient to meet our operating expenses or other obligations. A deficiency of this nature would adversely impact our financial condition, results of operations, cash flows, the quoted trading price of our securities, and our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders. Events and conditions applicable to owners and operators of real estate that are beyond our control and could impact our economic performance and the value of our real estate assets may include:

- local oversupply or reduction in demand for office or other commercial space, which may result in decreasing rental rates and greater concessions to tenants;
- inability to collect rent from tenants;

- vacancies or inability to rent space on favorable terms or at all;
- inability to finance property development and acquisitions on favorable terms or at all;
- increased operating costs, including insurance premiums, utilities, and real estate taxes;
- costs of complying with changes in governmental regulations;
- the relative illiquidity of real estate investments;

- changing submarket demographics;
- the development of harmful mold or other airborne toxins or contaminants that could damage our properties or expose us to third-party liabilities; and
- property damage resulting from seismic activity or other natural disasters.

We depend upon significant tenants and the loss of a significant tenant could adversely affect our financial condition, revenues and results of operations. As of December 31, 2012, our 15 largest tenants represented approximately 34.1% of total annualized base rental revenues. See further discussion on the composition of our tenants by industry and our largest tenants under “Item 2: Properties -Significant Tenants.”

Our financial condition, results of operations, ability to borrow funds, and cash flows would be adversely affected if any of our significant tenants fails to renew its lease(s), renew its lease(s) on terms less favorable to us, or becomes bankrupt or insolvent or otherwise unable to satisfy its lease obligations.

Downturn in tenants' businesses may reduce our cash flows. For the year ended December 31, 2012, we derived approximately 99.2% of our revenues from continuing operations from rental income and tenant reimbursements. A tenant may experience a downturn in its business, which may weaken its financial condition and result in its failure to make timely rental payments or result in defaults under our leases. In the event of default by a tenant, we may experience delays in enforcing our rights as landlord and may incur substantial costs in protecting our investment.

The bankruptcy or insolvency of a major tenant also may adversely affect the income produced by our properties. If any tenant becomes a debtor in a case under federal bankruptcy law, we cannot evict the tenant solely because of the bankruptcy. In addition, the bankruptcy court might permit the tenant to reject and terminate its lease with us. Our claim against the tenant for unpaid and future rent could be subject to a statutory cap that might be substantially less than the remaining rent actually owed under the lease. Therefore, our claim for unpaid rent would likely not be paid in full. Any losses resulting from the bankruptcy of any of our existing tenants could adversely impact our financial condition, results of operations, cash flows, the quoted trading price of our securities, and our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders.

A large percentage of our tenants' operate in a concentrated group of industries and downturns in these industries could adversely affect our financial condition, revenues and results of operations. As of December 31, 2012, as a percentage of our annualized base rental revenue, 36% of our tenants operated in the technology and media industry, 19% in the finance, insurance and real estate industry, 15% in the professional, business and other services industry, and 11% in the education and health services industry (of which approximately 5% are in the for profit education sector). As we expand our acquisition and development activities in markets populated by high growth tenants in the technology and media industry, our tenant mix may become more concentrated, further exposing us to risks associated with that industry. For a further discussion of the composition of our tenants by industry, see “Item 2: Properties—Significant Tenants.” An economic downturn in any of these industries, or in any industry in which a significant number of our tenants currently or may in the future operate, could negatively impact the financial condition of such tenants and cause them to fail to make timely rental payments or default on lease obligations, fail to renew their leases or renew their leases on terms less favorable to us, become bankrupt or insolvent, or otherwise become unable to satisfy their obligations to us. As a result, a downturn in an industry in which a significant number of our tenants operate could adversely affect our financial conditions and result of operations.

We may be unable to renew leases or re-lease available space. We had office space representing approximately 7.2%, of the total square footage of our properties that was not occupied as of December 31, 2012. In addition, leases representing approximately 7.1% and 10.4% of the leased rentable square footage of our properties are scheduled to expire in 2013 and 2014, respectively. Above market rental rates on some of our properties may force us to renew or re-lease expiring leases at rates below current lease rates. As of December 31, 2012, we believe that the weighted average cash rental rates for our overall portfolio, including recently acquired properties, are approximately at the current average quoted market rental rates, and weighted average cash rental rates for leases scheduled to expire during 2013 are approximately 5% below the current average quoted market rental rates, although individual properties within any particular submarket presently may be leased at, above, or below the current market rental rates within that submarket. We cannot provide any assurance that leases will be renewed or that available space will be re-leased at rental rates equal to or above the current rental rates. If the average rental rates for our properties decrease or existing tenants do not renew their leases, our financial condition, results of operations, cash flows, the quoted trading price of our securities, and our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders could be adversely affected.

We are subject to governmental regulations that may affect the development, redevelopment, and use of our properties. We are subject to governmental regulations that may have a material adverse effect on our financial condition, results of operations,

cash flow, the quoted trading price of our securities, and our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders.
Our properties are subject to regulation under federal laws, such as the Americans with Disabilities Act of 1990 (the "ADA") pursuant to which all public accommodations must meet federal requirements related to access and use by disabled persons, and state and local laws addressing earthquake, fire, and life safety requirements. Although we believe that our properties substantially comply with requirements under applicable governmental regulations, none of our properties have been audited or investigated for compliance by any regulatory agency. If we were not in compliance with material provisions of the ADA or other regulations affecting our properties, we might be required to take remedial action, which could include making modifications or renovations to properties. Federal, state, or local governments may also enact future laws and regulations that could require us to make significant modifications or renovations to our properties. If we were to incur substantial costs to comply with the ADA or any other regulations, our financial condition, results of operations, cash flows, the quoted trading price of our securities, and our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders could be adversely affected.
Our properties are subject to land use rules and regulations that govern our development, redevelopment, and use of our properties. Restrictions on our ability to develop, redevelop, or use our properties resulting from changes in the existing land use rules and regulations could have an adverse effect on our financial position, results of operations, cash flows, quoted trading price of our securities, our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders.

Our debt level reduces cash available for distribution and may expose us to the risk of default under our debt obligations. Payments of principal and interest on borrowings may leave us with insufficient cash resources to operate our properties or to pay in cash the distributions necessary to maintain the Company's REIT qualification. Our level of debt and the limitations imposed by our debt agreements may have substantial consequences to us, including the following:

- we may be unable to refinance our indebtedness at maturity, or the refinancing terms may be less favorable than the terms of our original indebtedness;

- cash flows may be insufficient to meet required principal and interest payments;

- we may be forced to dispose of one or more of our properties, possibly on disadvantageous terms;

- we may default on our obligations, and the lenders or mortgagees may foreclose on our properties that secure the loans and receive an assignment of rents and leases; and

- our default under one mortgage loan could result in a default on other indebtedness with cross default provisions.

If one or more of these events were to occur, our financial condition, results of operations, cash flow, the quoted trading price of our securities, and our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders could be adversely affected. In addition, foreclosures could create taxable income without accompanying cash proceeds,
which could require us to borrow or sell assets to raise the funds necessary to meet the REIT distribution requirements discussed below, even if such actions are not on favorable terms. As of December 31, 2012, we had approximately \$2.0 billion aggregate principal amount of indebtedness, \$90.9 million of which is contractually due prior to December 31, 2013. Our total debt and preferred equity at December 31, 2012 represented 38.1% of our total market capitalization (which we define as the aggregate of our long-term debt, liquidation value of our preferred equity, and the market value of the Company's common stock and the Operating Partnership's common units of limited partnership interest, or common units). In January 2013, we repaid \$83.1 million of the total amount contractually due prior to December 31, 2013. In addition, on January 14, 2013, the Operating Partnership issued \$300.0 million of

3.8% senior unsecured notes due 2023 and used the proceeds from the offering to repay the remaining outstanding balance on the Operating Partnership's $500 million unsecured revolving credit facility. For calculation of our market capitalization and additional information on debt maturities see "Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations —Liquidity and Capital Resources of the Company—Capitalization and Liquidity Uses."

The covenants in the Operating Partnership's revolving credit facility and term loan facility may limit our ability to make distributions to the holders of our common stock. The Operating Partnership's revolving credit facility and $150.0 million unsecured term loan facility contain financial covenants that could limit the amount of distributions payable by us on our common stock and preferred stock. We rely on cash distributions we receive from the Operating Partnership to pay distributions on our common stock and preferred stock and to satisfy our other cash needs, and the revolving credit facility and the term loan facility provide that the Operating Partnership may not, in any year, make partnership distributions to us or other holders of its partnership interests in an aggregate amount in excess of the greater of:

- 95% of the Operating Partnership's consolidated funds from operations (as similarly defined in each of the revolving credit facility and term loan facility agreements) for such year; and

- an amount which results in distributions to us (excluding any preferred partnership distributions to the extent the same have been deducted from consolidated funds from operations for such year) in an amount sufficient to permit us to pay dividends to our stockholders that we reasonably believe are necessary to (a) maintain our qualification as a REIT for federal and state income tax purposes and (b) avoid the payment of federal or state income or excise tax.

In addition, the revolving credit facility and term loan facility provide that, if the Operating Partnership fails to pay any principal of or interest on any borrowings under the revolving credit facility or term loan facility, respectively, when due, then the Operating Partnership may make only those partnership distributions to us and other holders of its partnership interests necessary to enable us to make distributions to our stockholders that we reasonably believe are necessary to maintain our status as a REIT for federal and state income tax purposes. Any limitation on our ability to make distributions to our stockholders, whether as a result of these provisions in the revolving credit facility, the term loan facility or otherwise, could have a material adverse effect on the market value of our common stock and preferred stock.

A downgrade in our credit ratings could materially adversely affect our business and financial condition. The credit ratings assigned to the debt securities of the Operating Partnership and our preferred stock could change based upon, among other things, our results of operations and financial condition. These ratings are subject to ongoing evaluation by credit rating agencies, and we cannot assure you that any rating will not be changed or withdrawn by a rating agency in the future if, in its judgment, circumstances warrant. Moreover, these credit ratings do not apply to our common stock and are not recommendations to buy, sell or hold any other securities. If any of the credit rating agencies that have rated the debt securities of the Operating Partnership or our preferred stock downgrades or lowers its credit rating, or if any credit rating agency indicates that it has placed any such rating on a so-called “watch list” for a possible downgrading or lowering or otherwise indicates that its outlook for that rating is negative, it could have a material adverse effect on our costs and availability of capital, which could in turn have a material adverse effect on our financial condition, results of operations, cash flows and our ability to satisfy our debt service obligations and to make dividends and distributions on our common stock and preferred stock.

We face significant competition, which may decrease the occupancy and rental rates of our properties. We compete with several developers, owners, and operators of office and other commercial real estate, many of which own properties similar to ours in the same submarkets in which our properties are located but which have lower occupancy rates than our properties. Therefore, our competitors have an incentive to decrease rental rates until their available space is leased. As previously mentioned, as of December 31, 2012 we believe that the weighted average cash rental rates for our overall portfolio are approximately at the current average quoted market rental rates. If our competitors offer space at rental rates below the rates currently charged by us for comparable space, we may be pressured to reduce our rental rates below those currently charged in order to retain tenants when our tenant leases expire. As a result, our financial condition, results of operations, cash flow, the quoted trading price of our securities, and our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders may be adversely affected.

In order to maintain the quality of our properties and successfully compete against other properties, we must periodically spend money to maintain, repair, and renovate our properties, which reduces our cash flows. If our properties are not as attractive to current and prospective tenants in terms of rent, services, condition, or location as properties owned by our competitors, we could lose tenants or suffer lower rental rates. As a result, we may from time to time be required to make significant capital expenditures to maintain the competitiveness of our properties. There can be no assurances that any such expenditure would result in higher occupancy or higher rental rates, or deter existing tenants from relocating to properties owned by our competitors.

Potential casualty losses, such as earthquake losses, may not be covered by insurance and payment of such losses may adversely affect our financial condition and results of operations. We carry comprehensive liability, fire, extended coverage, rental loss, and terrorism insurance covering all of our properties. Management believes the policy specifications and insured limits are appropriate given the relative risk of loss, the cost of the coverage, and industry practice. We do not carry insurance for generally uninsurable losses such as loss from riots or acts of God. In addition, all of our properties are located in earthquake-prone areas. We carry earthquake insurance on our properties in an amount and with deductibles that management believes are commercially reasonable. However, the amount of our earthquake insurance coverage may not be sufficient to cover losses from earthquakes. We may also discontinue earthquake insurance on some or all of our properties in the future if the cost of premiums for earthquake insurance exceeds the value of the coverage discounted for the risk of loss. If we experience a loss that is uninsured or which exceeds policy limits, we could lose the capital invested in the damaged properties as well as the anticipated future cash flows from those properties. Further, if the damaged properties are subject to recourse indebtedness, we would continue to be liable for the indebtedness, even if the properties were irreparable.

We are subject to environmental and health and safety laws and regulations, and any costs to comply with, or liabilities arising under, such laws and regulations could be material. As an owner, operator, manager, acquirer and developer of real properties, we are subject to environmental and health and safety laws and regulations. Certain of these laws and regulations impose joint and several liability, without regard to fault, for investigation and clean-up costs on current and former owners and operators of real property and persons who have disposed of or released hazardous substances into the environment. At some of the properties, there are asbestos-containing materials, or tenants routinely handle hazardous substances as part of their operations. In addition, historical operations, including the presence of underground storage tanks, have caused soil or groundwater contamination at or near some of the properties. Although we believe that the prior owners of the affected properties or other persons may have conducted remediation of known contamination at these properties, not all such contamination has been remediated. Unknown or unremediated contamination or the compliance with existing or new environmental or health and safety laws and regulations could require us to incur costs or liabilities that could be material. See "Item 1: Business — Environmental Regulations and Potential Liabilities."

We may be unable to complete acquisitions and successfully operate acquired properties. We continually evaluate the market of available properties and may continue to acquire office properties and undeveloped land when strategic opportunities exist. Our ability to acquire properties on favorable terms and successfully operate them is subject to the following risks:

- we may potentially be unable to acquire a desired property because of competition from other real estate investors with significant capital, including both publicly traded REITs and institutional investment funds;

- the possibility that, even if we enter into agreements for the acquisition of office properties, we may be unable to complete such acquisitions because they remain subject to customary conditions to closing including the completion of due diligence investigations to management's satisfaction;

- we may be unable to finance acquisitions on favorable terms or at all;

- we may spend more than budgeted amounts in operating costs or to make necessary improvements or renovations to acquired properties;

- we may lease acquired properties at economic lease terms different than projected;

- we may acquire properties that are subject to liabilities for which we may have limited or no recourse; and

- we may be unable to complete an acquisition after making a nonrefundable deposit and incurring certain other acquisition related costs.

If we cannot finance property acquisitions on favorable terms or operate acquired properties to meet financial expectations, our financial condition, results of operations, cash flows, the quoted trading price of our securities, and our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders could be adversely affected.

We may be unable to successfully complete and operate acquired, developed, and redeveloped properties. There are significant risks associated with property acquisition, development, and redevelopment including the possibility that:

- we may be unable to lease acquired, developed, or redeveloped properties at projected economic lease terms or within budgeted timeframes;

- we may not complete development or redevelopment properties on schedule or within budgeted amounts;

- we may expend funds on and devote management's time to acquisition, development, or redevelopment properties that we may not complete;

- we may encounter delays or refusals in obtaining all necessary zoning, land use, and other required entitlements, and building, occupancy, and other required governmental permits and authorizations;

- we may encounter delays, refusals, unforeseen cost increases, and other impairments resulting from third-party litigation; and

- we may fail to obtain the financial results expected from properties we acquire, develop, or redevelop.

If one or more of these events were to occur in connection with our acquired properties, undeveloped land, or development or redevelopment properties under construction, we could be required to recognize an impairment loss. These events could also have an adverse impact on our financial condition, results of operations, cash flow, the quoted trading price of our securities, and our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders.

While we historically have acquired, developed, and redeveloped office properties in California markets, over the past three years we have acquired ten properties in the state of Washington and may in the future acquire, develop, or redevelop properties for other uses and expand our business to other geographic regions where we expect the development or acquisition of property to result in favorable risk-adjusted returns on our investment. Presently, we do not possess the same level of familiarity with development of property types other than mixed-use, office, or with certain outside markets, which could adversely affect our ability to acquire, develop or redevelop properties or to achieve expected performance.

We could default on leases for land on which some of our properties are located. As of December 31, 2012, we owned eleven office buildings, located on various land parcels and regions, which we lease individually on a long-term basis. As of December 31, 2012, we had approximately 1.8 million aggregate rentable square feet, or 13.6% of our total stabilized portfolio, of rental space located on these leased parcels. In addition, we had ground lease obligations for the land at one redevelopment property encompassing approximately 98,000 rentable square feet. In 2012, we exercised our option to purchase this land for a purchase price of $27.5 million and we currently expect we will close the transaction in the second quarter of 2013. If we default under the terms of any particular lease, we may lose the ownership rights to the property subject to the lease. Upon expiration of a lease, we may not be able to renegotiate a new lease on favorable terms, if at all. The loss of the ownership rights to these properties or an increase of rental expense could have an adverse effect on our financial condition, results of operations, cash flow, the quoted trading price of our securities, and our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders.

Real estate assets are illiquid, and we may not be able to sell our properties when we desire. Our investments in our properties are relatively illiquid, limiting our ability to sell our properties quickly in response to changes in economic or other conditions. In addition, the Code generally imposes a 100% prohibited transaction tax on the Company on profits derived from sales of properties held primarily for sale to customers in the ordinary course of business, which effectively limits our ability to sell properties other than on a selected basis. These restrictions on our ability to sell our properties could have an adverse effect on our financial condition, results of operations, cash flow, the quoted trading price of our securities, and our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders.

We may invest in securities related to real estate, which could adversely affect our ability to pay dividends and distributions to our security holders. We may purchase securities issued by entities which own real estate and may, in the future, also invest in mortgages. In general, investments in mortgages are subject to several risks, including:

- borrowers may fail to make debt service payments or pay the principal when due;

- the value of the mortgaged property may be less than the principal amount of the mortgage note securing the property; and

- interest rates payable on the mortgages may be lower than our cost for the funds used to acquire these mortgages.

Owning these securities may not entitle us to control the ownership, operation, and management of the underlying real estate. In addition, we may have no control over the distributions with respect to these securities, which could adversely affect our ability to pay dividends and distributions to our security holders.

Future terrorist activity or engagement in war by the United States may have an adverse effect on our financial condition and operating results. Terrorist attacks in the United States and other acts of terrorism or war, may result in declining economic activity, which could harm the demand for and the value of our properties. In addition, the public perception that certain locations are at greater risk for attack, such as major airports, ports, and rail facilities, may decrease the demand for and the value of our properties near these sites. A decrease in demand could make it difficult for us to renew or re-lease our properties at these sites at lease rates equal to or above historical rates. Terrorist activities also could directly impact the value of our properties through damage, destruction, or loss, and the availability of insurance for these acts may be less, and cost more, which could adversely affect our financial condition. To the extent that our tenants are impacted by future attacks, their businesses similarly could be adversely affected, including their ability to continue to honor their existing leases.

Terrorist acts and engagement in war by the United States also may adversely affect the markets in which our securities trade and may cause further erosion of business and consumer confidence and spending and may result in increased volatility in national and international financial markets and economies. Any one of these events may cause a decline in the demand for our office leased space, delay the time in which our new or renovated properties reach stabilized occupancy, increase our operating expenses, such as those attributable to increased physical security for our properties, and limit our access to capital or increase our cost of raising capital.

The enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”) will subject us to substantial additional federal regulation. There are significant corporate governance and executive compensation-related requirements that have been, and will in the future be, imposed on publicly-traded companies under the Dodd-Frank Act. Several of these provisions require the SEC to adopt additional rules and regulations in these areas. For example, the Dodd-Frank Act requires publicly-traded companies to give stockholders a non-binding vote on executive compensation and so-called “golden parachute” payments, heightens certain independence standards for compensation advisers and authorizes the SEC to promulgate rules that would allow stockholders to nominate their own candidates for board seats using a registrant's proxy materials. Our efforts to comply with these requirements have resulted in, and are likely to continue to result in, an increase in expenses and a diversion of management's time from other business activities. In addition, if stockholders do not vote to approve our executive compensation practices and/or our equity plan amendments, these actions may interfere with our ability to attract and retain key personnel who are essential to our future success. Given the uncertainty associated with both the results of the existing Dodd-Frank Act requirements and the manner in which additional provisions of the Dodd-Frank Act will be implemented by various regulatory agencies and through regulations, the full extent of the impact that such requirements will have on our operations is unclear. Accordingly, the changes resulting from the Dodd-Frank Act may impact the profitability of business activities, require changes to certain business practices, or otherwise adversely affect our financial condition, results of operations, cash flows, the quoted trading price of the Company's common stock and of the Operating Partnership's publicly-traded notes and our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders.

Our property taxes could increase due to reassessment or property tax rate changes. We are required to pay some state and local taxes on our properties. In addition, the real property taxes on our properties may increase as our properties are reassessed by taxing authorities or as property tax rates change. For example, under a current California law commonly referred to as “Proposition 13,” property tax reassessment generally occurs as a result of a “change in ownership” of a property, as specially defined for purposes of those rules. Because the property taxing authorities may not determine whether there has been a “change in ownership” or the actual reassessed value of a property for a period of time after a transaction has occurred, we may not know the impact of a potential reassessment for a considerable amount of time following a particular transaction. Therefore, the amount of property taxes we are required to pay could increase substantially from the property taxes we currently pay or have paid in the past, including on a retroactive basis. In addition, from time to time voters and lawmakers have announced initiatives to repeal or amend Proposition 13 to eliminate its application to commercial and industrial property and/or introduce split tax roll legislation. Such initiatives, if successful, would increase the assessed value and/or tax rates applicable to commercial property in California, including our office properties. An increase in the assessed value of our properties or our property tax rates could adversely impact our financial condition, results of operations, cash flows, the quoted trading price of the Company's common stock and of the Operating Partnership's publicly-traded notes and our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders.

Our business could be adversely impacted if there are deficiencies in our disclosure controls and procedures or internal control over financial reporting. The design and effectiveness of our disclosure controls and procedures and internal control over financial reporting may not prevent all errors, misstatements or misrepresentations. While management will continue to review the effectiveness of our disclosure controls and procedures and internal control over financial reporting, there can be no guarantee that our internal control over financial reporting will be effective in accomplishing all control objectives all of the time. Deficiencies, including any material weakness, in our internal control over financial reporting which may occur in the future could result in misstatements of our results of operations, restatements of our financial statements, or otherwise adversely impact our financial condition, results of operations, cash flows, the quoted trading price of the Company's common stock and of the Operating Partnership's publicly-traded notes and our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders.

We face risks associated with security breaches through cyber attacks, cyber intrusions or otherwise, as well as other significant disruptions of our information technology (IT) networks and related systems. We face risks associated with security breaches, whether through cyber attacks or cyber intrusions over the Internet, malware, computer viruses, attachments to e-mails, persons inside our organization or persons with access to systems inside our organization, and other significant disruptions of our IT networks and related systems. The risk of a security breach or disruption, particularly through cyber attack or cyber intrusion, including by computer hackers, foreign governments and cyber terrorists, has generally increased as the number, intensity and sophistication of attempted attacks and intrusions from around the world have increased. Our IT networks and related systems are essential to the operation of our business and our ability to perform day-to-day operations (including managing our building systems), and, in some cases, may be critical to the operations of certain of our tenants. There can be no assurance that our efforts to maintain the security and integrity of these types of IT networks and related systems will be effective or that attempted security breaches or disruptions would not be successful or damaging. A security breach or other significant disruption involving our IT networks and related systems could adversely impact our financial condition, results of operations, cash flows, the quoted trading price of the Company's common stock and of the Operating Partnership's publicly-traded notes and our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders.

Risks Related to our Organizational Structure

Loss of our key personnel could harm our operations and adversely affect the quoted trading price of our securities
The leadership and performance of our executive and senior officers, particularly John B. Kilroy, Jr., President and Chief Executive Officer, Jeffrey C. Hawken, Executive Vice President and Chief Operating Officer, Eli Khouri, Executive Vice President and Chief Investment Officer, Tyler H. Rose, Executive Vice President and Chief Financial Officer, and Justin W. Smart, Executive Vice President, Development and Construction Services, play a key role in the success of the Company. They are integral to the Company's success for many reasons, including that each has a strong national or regional reputation in our industry and investment community. In addition, they have significant relationships with investors, lenders, tenants and industry personnel, which benefit the Company. Our future performance will be substantially dependent on our ability to retain and motivate these individuals. The loss or limited availability of the services of our key personnel could materially and adversely affect our business, results of operations and financial condition and could be negatively perceived in the capital markets.
Our growth depends on external sources of capital that are outside of our control and the inability to obtain capital on terms that are acceptable to us, or at all, could adversely affect our financial condition and results of operations. The Company is required under the Code to distribute at least 90% of its taxable income (subject to certain adjustments and excluding any net capital gain), and the Operating Partnership is required to make distributions to the Company to allow the Company to satisfy these REIT distribution requirements. Because of these distribution requirements, the Operating Partnership is required to make distributions to the Company, and we may not be able to fund future capital needs, including any necessary acquisition financing, from operating cash flow. Consequently, management relies on third-party sources of capital to fund our capital needs. We may not be able to obtain financing on favorable terms or at all. Any additional debt we incur will increase our leverage. Access to third-party sources of capital depends, in part, on general market conditions and the availability of credit, the market's perception of our growth potential, our current and expected future earnings, our cash flows and cash distributions, and the quoted trading price of our securities. If we cannot obtain capital from third-party sources, our financial condition, results of operations, cash flows, the quoted trading price of our securities, and our ability to satisfy our debt service obligations and to pay dividends and distributions to our security holders may be adversely affected.
Our common limited partners have limited approval rights, which may prevent us from completing a change of control transaction that may be in the best interests of all our security holders. The Company may not withdraw as the Operating Partnership's general partner or transfer its general partnership interest in the Operating Partnership without the approval of the holders of at least 60% of the units representing common limited partnership interests, including the common units held by the Company in its capacity as the Operating Partnership's general partner. In addition, the Company may not engage in a merger, consolidation, or other combination or the sale of substantially all of its assets or such similar transaction, without the approval of the holders of 60% of the common units, including the common units held by the Company in its capacity as the Operating Partnership's general partner. The right of our common limited partners to vote on these transactions could limit our ability to complete a change of control transaction that might otherwise be in the best interest of all our security holders.
In certain circumstances, our limited partners must approve our dissolution and the disposition of properties contributed by the limited partners. For as long as limited partners own at least 5% of all of the Operating Partnership's partnership interests, we must obtain the approval of limited partners holding a majority of the units representing common limited partnership interests before we may dissolve. As of December 31, 2012, limited partners owned approximately 2.4% of the Operating Partnership's partnership interests, of which 1.7% was owned by John B. Kilroy, Sr. and John B. Kilroy, Jr. In addition, we agreed to use commercially reasonable efforts to minimize the tax consequences to common limited partners resulting from the repayment, refinancing, replacement, or restructuring of debt, or any sale, exchange, or other disposition of any of our other assets. The exercise of one or more of these approval rights by the limited partners could delay or prevent us from completing a transaction that may be in the best interest of all our security holders.
The Chairman of our board of directors and our President and Chief Executive Officer each have substantial influence over our affairs. John B. Kilroy, Sr. is the Chairman of our board of directors and the father of John B. Kilroy, Jr., our

President and Chief Executive Officer. Each is a member of our board of directors, and together, as of December 31, 2012, they beneficially owned approximately 2.9% of the total outstanding shares of the Company's common stock. The percentage of outstanding shares of common stock beneficially owned includes 281,210 shares of common stock, 412,936 restricted stock units that were vested and held by John B. Kilroy, Jr. at December 31, 2012, and assumes the exchange into shares of the Company's common stock of the 1,335,135 common units of the Operating Partnership held by Messrs. Kilroy (which are redeemable in exchange for, at the option of the Company, an equal number of shares of the Company's common stock).

Pursuant to the Company's charter, no stockholder may own, actually or constructively, more than 7.0% (by value or by number of shares, whichever is more restrictive) of the outstanding Company common stock without obtaining a waiver from the board of directors. The board of directors has waived the ownership limits with respect to John B. Kilroy, Sr., John B. Kilroy, Jr., members of their families, and some of their affiliated entities. These named individuals and entities may own either actually or constructively, in the aggregate, up to 19.6% of the Company's outstanding common stock, excluding Operating Partnership units that are exchangeable into shares of Company common stock. Consequently, Messrs. Kilroy have substantial influence on the Company, and because the Company is the manager of the Operating Partnership, on the Operating Partnership, and could exercise their influence in a manner that is not in the best interest of our stockholders, noteholders or unitholders. Also, they may, in the future, have a substantial influence on the outcome of any matters submitted to our stockholders or unitholders for approval.

There are restrictions on the ownership of the Company's capital stock that limit the opportunities for a change of control at a premium to existing security holders. Provisions of the Maryland General Corporation Law, the Company's charter and bylaws, and the Operating Partnership's partnership agreement may delay, deter, or prevent a change of control of the Company, or the removal of existing management. Any of these actions might prevent our security holders from receiving a premium for their common shares or common units over the then-prevailing market price of the shares of the Company's common stock.

In order for the Company to qualify as a REIT under the Code its stock must be beneficially owned by 100 or more persons during at least 335 days of a taxable year of 12 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 the outstanding shares of the Company's stock may be owned, actually or constructively, by five or fewer individuals (as defined in the Code to include certain entities) during the last half of a taxable year (other than the first year for which an election to be a REIT has been made). The Company's charter contains restrictions on the ownership and transfer of its capital stock that are intended to assist the Company in complying with these requirements and continuing to qualify as a REIT. No single stockholder may own, either actually or constructively, absent a waiver from the board of directors, more than 7.0% (by value or by number of shares, whichever is more restrictive) of the Company's outstanding common stock. Similarly, absent a waiver from the board of directors, no single holder of the Company's 6.875% Series G Cumulative Redeemable Preferred stock (the "Series G Preferred Stock") may actually or constructively own more than 9.8% (by value or by number of shares, whichever is more restrictive) of the Company's Series G Preferred Stock; and no single holder of the Company's 6.375% Series H Cumulative Redeemable Preferred stock (the "Series H Preferred Stock") may actually or constructively own more than 9.8% (by value or by number of shares, whichever is more restrictive) of the Company's Series H Preferred Stock.

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 the applicable ownership limit of a particular class of the Company's capital stock could, nevertheless, cause that individual or entity, or another individual or entity, to constructively own stock in excess of, and thereby subject such stock to, the applicable ownership limit.

The board of directors may waive the ownership limits if it is satisfied that the excess ownership would not jeopardize the Company's REIT status and if it believes that the waiver would be in our best interest. The board of directors has waived the ownership limits with respect to John B. Kilroy, Sr., John B. Kilroy, Jr., members of their families, and some of their affiliated entities. These named individuals and entities may own either actually or constructively, in the aggregate, up to 19.6% of the Company's outstanding common stock, excluding common units that are exchangeable into shares of common stock. The board of directors has also waived the ownership limits with respect to the initial purchasers of the 4.25% Exchangeable Senior Notes due 2014 (the "4.25% Exchangeable Notes") and certain of their affiliated entities to beneficially own up to 9.8%, in the aggregate, of the Company's common stock in connection with hedging the capped call transactions.

If anyone acquires shares in excess of any ownership limits, the transfer to the transferee will be void with respect to the excess shares, the excess shares will be automatically transferred to a trust for the benefit of a qualified charitable organization, and the purported transferee or owner will have no rights with respect to those excess shares.

The Company's charter contains provisions that may delay, deter, or prevent a change of control transaction. The following provisions of the Company's charter may delay or prevent a change of control over us, even if a change of control might be beneficial to our security holders, deter tender offers that may be beneficial to our security holders, or limit security holders' opportunity to receive a potential premium for their shares and/or units if an investor attempted to gain shares beyond the Company's ownership limits or otherwise to effect a change of control:

- The Company's charter authorizes the board of directors to issue up to 30,000,000 shares of the Company's preferred stock, including convertible preferred stock, without stockholder approval. The board of directors may establish the preferences, rights, and other terms, including the right to vote and the right to convert into common stock any shares issued. The issuance of preferred stock could delay or prevent a tender offer or a change of control even if a tender offer or a change of control was in our security holder's interest. As of December 31, 2012, 8,000,000 shares of the Company's preferred stock were issued and outstanding, consisting of 4,000,000 shares of the Company's Series G Preferred Stock and 4,000,000 shares of the Company's Series H Preferred Stock; and

- The Company's charter states that any director, or the entire board of directors, may be removed from office at any time, but only for cause and then only by the affirmative vote of the holders of at least two thirds of the votes of the Company's capital stock entitled to be cast in the election of directors.

The board of directors may change investment and financing policies without unitholder or stockholder approval, causing us to become more highly leveraged, which may increase our risk of default under our debt obligations.

We are not limited in our ability to incur debt. Our financing policies and objectives are determined by the board of directors. Our goal is to limit our dependence on leverage and maintain a conservative ratio of debt to total market capitalization. However, our organizational documents do not limit the amount or percentage of indebtedness, funded or otherwise, that we may incur. As of December 31, 2012, we had approximately $2.0 billion aggregate principal amount of indebtedness outstanding, which represented 34.7% of our total market capitalization. Our total debt and the liquidation value of our preferred equity as a percentage of total market capitalization was approximately 38.1% as of December 31, 2012. In addition, on January 14, 2013, the Operating Partnership issued $300.0 million of 3.8% senior unsecured notes due 2023. See “Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations —Liquidity and Capital Resources of the Company— Capitalization” for a calculation of our market capitalization. These ratios may be increased or decreased without the consent of our unitholders or stockholders. Increases in the amount of debt outstanding would result in an increase in our debt service, which could adversely affect cash flow and our ability to pay dividends and distributions to our security holders. Higher leverage also increases the risk of default on our obligations and limits our ability to obtain additional financing in the future.
We may issue additional common units and shares of capital stock without unitholder or stockholder approval, as applicable, which may dilute unitholder or stockholder investment. The Company may issue shares of our common stock, preferred stock, or other equity or debt securities without stockholder approval, including the issuance of shares to satisfy REIT dividend distribution requirements. Similarly, the Operating Partnership may offer its common or preferred units for contributions of cash or property without approval by its unitholders. Further, under certain circumstances, the Company may issue shares of our common stock in exchange for the Operating Partnership's outstanding 4.25% Exchangeable Notes. Existing security holders have no preemptive rights to acquire any of these securities, and any issuance of equity securities under these circumstances may dilute a unitholder's or stockholder's investment.
Sales of a substantial number of shares of the Company's securities, or the perception that this could occur, could result in decreasing the quoted trading price per share of the Company's common stock and of the Operating Partnership's publicly-traded notes. Management cannot predict whether future issuances of shares of the Company's common stock or the availability of shares for resale in the open market will result in decreasing the market price per share of the Company's common stock. As of December 31, 2012, 74,926,981 shares of the Company's common stock and 8,000,000 shares of the Company's preferred stock, consisting of 4,000,000 shares of Series G Preferred Stock and 4,000,000 shares of Series H Preferred Stock, were issued and outstanding.

As of December 31, 2012, the Company had reserved for future issuance the following shares of common stock: 1,826,503 shares issuable upon the exchange, at the Company's option, of the Operating Partnership's common units; 639,487 shares remained available for grant under our 2006 Incentive Award Plan (see Note 12 to our consolidated financial statements); 1,048,863 shares issuable upon settlement of RSUs; and 1,540,000 shares issuable upon exercise of outstanding options, as well as 4,800,796 shares potentially issuable under certain circumstances, in exchange for the 4.25% Exchangeable Notes. The Company has a currently effective registration statement registering 1,708,131 shares of our common stock for possible issuance to the holders of the Operating Partnership's common units. That registration statement also registers 306,808 shares of common stock held by certain stockholders for possible resale. The Company also has a currently effective registration statement registering the 4,800,796 shares of our common stock that may potentially be issued in exchange for the Operating Partnership's presently outstanding 4.25% Exchangeable Notes. Consequently, if and when the shares are issued, they may be freely traded in the public markets.

Risks Related to Taxes and the Company's Status as a REIT

Loss of the Company's REIT status would have significant adverse consequences to us and the value of the Company's common stock. The Company currently operates in a manner that is intended to allow it to qualify as a REIT for federal income tax purposes under the Code. If the Company were to lose its REIT status, the Company would face adverse tax consequences that would substantially reduce the funds available for distribution to its stockholders for each of the years involved because:

- the Company would not be allowed a deduction for dividends paid to its stockholders in computing the Company's taxable income and would be subject to federal income tax at regular corporate rates;

- the Company could be subject to the federal alternative minimum tax and possibly increased state and local taxes; and

- unless entitled to relief under statutory provisions, the Company could not elect to be taxed as a REIT for four taxable years following the year during which the Company was disqualified.

In addition, if the Company failed to qualify as a REIT, it would not be required to make distributions to its stockholders. As a result of all these factors, the Company's failure to qualify as a REIT also could impair our ability to expand our business and raise capital and could adversely affect the value and quoted trading price of the Company's common stock.

Qualification as a REIT involves the application of highly technical and complex Code provisions for which there are only limited judicial and administrative interpretations. The complexity of these provisions and of the applicable Treasury regulations that have been promulgated under the Code is greater in the case of a REIT that, like the Company, holds its assets through a partnership. The determination of various factual matters and circumstances not entirely within our control may affect the Company's ability to continue to qualify as a REIT. For example, to qualify as a REIT, at least 95% of the Company's gross income in any year must be derived from qualifying sources. Also, the Company must make distributions to its stockholders aggregating annually at least 90% of the Company's net taxable income (excluding any net capital gains). In addition, legislation, new regulations, administrative interpretations, or court decisions may adversely affect the Company's security holders or the Company's ability to qualify as a REIT for federal income tax purposes or the desirability of an investment in a REIT relative to other investments. Although management believes that we are organized and operate in a manner to permit the Company to continue to qualify as a REIT, we cannot provide assurances that the Company has qualified or will continue to qualify as a REIT for tax purposes. We have not requested and do not plan to request a ruling from the IRS regarding the Company's qualification as a REIT.

To maintain the Company's REIT status, we may be forced to borrow funds during unfavorable market conditions. To qualify as a REIT, the Company generally must distribute to its stockholders at least 90% of the Company's net taxable income each year (excluding any net capital gains), and the Company will be subject to regular corporate income taxes to the extent that it distributes less than 100% of its net taxable income each year. In addition, the Company will be subject to a 4% nondeductible excise tax on the amount, if any, by which distributions it pays in any calendar year are less than the sum of 85% of its ordinary income, 95% of its net capital gains, and 100% of its undistributed income from prior years. To maintain the Company's REIT status and avoid the payment of federal income and excise taxes, the Operating Partnership may need to borrow funds and distribute or loan the proceeds to the Company so it can meet the REIT distribution requirements even if the then-prevailing market conditions are not favorable for these borrowings. These borrowing needs could result from differences in timing between the actual receipt of income and inclusion of income for federal income tax purposes, or the effect of nondeductible capital expenditures, the creation of reserves, or required debt or amortization payments.

If a transaction intended to qualify as a Section 1031 Exchange is later determined to be taxable, we may face adverse consequences. From time to time we dispose of properties in transactions that are intended to qualify as Section 1031 Exchanges. If the qualification of a transaction as a Section 1031 Exchange is successfully challenged and determined to be currently taxable, we generally would be required to pay taxes on any gain recognized upon the disposition of the property, including any interest and penalties, for the particular year in question, to the extent such amounts were not otherwise distributed to our stockholders. In such case, we would have less cash available to distribute to our stockholders and may be required to borrow funds in unfavorable conditions in order to pay such amounts. In addition, we may be required to amend our tax returns for the applicable year in question, including any information reports we sent to our stockholders.

Dividends payable by REITs, including us, generally do not qualify for the reduced tax rates available for some dividends. “Qualified dividends” payable to U.S. stockholders that are individuals, trusts and estates generally are subject to tax at preferential rates. Subject to limited exceptions, dividends payable by REITs are not eligible for these reduced rates and are taxable at ordinary income tax rates. The more favorable rates applicable to regular corporate qualified dividends could cause investors who are individuals, trusts and estates to perceive investments in REITs to be relatively less attractive than investments in the stocks of non-REIT corporations that pay dividends, which could adversely affect the value of the shares of REITs, including the shares of our capital stock.

The tax imposed on REITs engaging in “prohibited transactions” may limit our ability to engage in transactions which would be treated as sales for federal income tax purposes. A REIT's net income from prohibited transactions is subject to a 100% penalty tax. In general, prohibited transactions are sales or other dispositions of property, other than foreclosure property, held primarily for sale to customers in the ordinary course of business. Although we do not intend to hold any properties that would be characterized as held for sale to customers in the ordinary course of our business, unless a sale or disposition qualifies under certain statutory safe harbors, such characterization is a factual determination and no guarantee can be given that the IRS would agree with our characterization of our properties or that we will always be able to make use of the available safe harbors.

Complying with REIT requirements may cause us to forego otherwise attractive opportunities or liquidate otherwise attractive investments. To qualify as a REIT for federal income tax purposes, we must continually satisfy tests concerning, among other things, the sources of our income, the nature and diversification of our assets, the amounts we distribute to our stockholders and the ownership of our capital stock. If we fail to comply with one or more of the asset tests at the end of any calendar quarter, we must correct the failure within 30 days after the end of the calendar quarter or qualify for certain statutory relief provisions to avoid losing our REIT qualification and suffering adverse tax consequences. In order to meet these tests, we may be required to forego investments we might otherwise make or to liquidate otherwise attractive investments. Thus, compliance with the REIT requirements may hinder our performance and reduce amounts available for distribution to our stockholders.

Legislative or regulatory action could adversely affect us. In recent years, numerous legislative, judicial and administrative changes have been made to the federal income tax laws applicable to investments in REITs and similar entities. Additional changes to tax laws are likely to continue to occur in the future, and any such changes may impact our ability to qualify as a REIT, our tax treatment as a REIT or the tax treatment of our stockholders.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

General

As of December 31, 2012, our stabilized portfolio of properties was comprised of the following office properties.

	Number of Buildings	Rentable Square Feet	Number of Tenants	Percentage Occupied at December 31, 2012	
Office Properties	114	13,249,780	530	92.8	%

During the fourth quarter of 2012 we disposed of our entire portfolio of industrial properties and, as a result, no longer owned any industrial properties at December 31, 2012 (see Note 17 to our consolidated financial statements included in this report for additional information).

Our stabilized portfolio includes all of our properties with the exception of undeveloped land, development and redevelopment properties currently under construction or committed for construction, "lease-up" properties and properties held-for-sale. We define "lease-up" properties as properties we recently developed or redeveloped that have not yet reached 95% occupancy and are within one year following cessation of major construction activities. We define redevelopment properties as those projects for which we expect to spend significant development and construction costs on existing or acquired buildings pursuant to a formal plan, the intended result of which is a higher economic return on the property. Our stabilized portfolio also excludes our future development pipeline, which is comprised of nine potential development sites, including one office property moved from the stabilized portfolio to the development pipeline in the fourth quarter of 2012, representing 118.5 gross acres of undeveloped land.

As of December 31, 2012, the following properties were excluded from our stabilized portfolio:

	Number of Properties	Estimated Rentable Square Feet (1)
Development properties under construction	4	1,416,000
Redevelopment properties under construction	1	410,000
Lease-up properties	1	98,000

(1) Estimated rentable square feet upon completion.

As of December 31, 2012, all of our properties and development and redevelopment projects are owned and all of our business is currently conducted in the state of California with the exception of ten office properties located in the state of Washington. We own all of our properties through the Operating Partnership and the Finance Partnership. All our properties are held in fee, except for the 11 office buildings that are held subject to long-term ground leases for the land (See Note 15 to our consolidated financial statements included in this report for additional information regarding our ground lease obligations). We had no properties held-for-sale as of December 31, 2012.

In general, the office properties are leased to tenants on a full service gross, modified gross or triple net basis. Under a full service gross lease, we are obligated to pay the tenant's proportionate share of real estate taxes, insurance, and operating expenses up to the amount incurred during the tenant's first year of occupancy ("Base Year") or a negotiated amount approximating the tenant's pro- rata share of real estate taxes, insurance, and operating expenses ("Expense Stop"). The tenant pays its pro-rata share of increases in expenses above the Base Year or Expense Stop. A modified gross lease is similar to a full service gross lease, except tenants are obligated to pay their proportionate share of certain operating expenses, usually electricity, directly to the service provider. In addition, some office properties, primarily in the greater Seattle region, are leased to tenants on a triple net basis, pursuant to which the tenants pay their proportionate share of real estate taxes, operating costs, and utility costs.

We believe that all of our properties are well maintained and do not require significant capital improvements. As of December 31, 2012, we managed all of our properties through internal property managers.

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Office Properties

The following table sets forth certain information relating to each of the stabilized office properties owned as of December 31, 2012.

Property Location	No. of Buildings	Year Built/ Renovated	Rentable Square Feet	Percentage Occupied at 12/31/12[(1)]		Annualized Base Rent($000's)[(2)]	Annualized Rent Per Square Foot[(2)]
Los Angeles and Ventura Counties							
23925 Park Sorrento, Calabasas, California	1	2001	11,789	100.0	%	$ 421	$35.71
23975 Park Sorrento, Calabasas, California	1	2002	100,592	93.1	%	3,162	34.74
24025 Park Sorrento, Calabasas, California	1	2000	102,264	74.9	%	2,821	36.81
26541 Agoura Road Calabasas, California	1	1988	90,156	100.0	%	1,628	18.06
2240 E. Imperial Highway, El Segundo, California	1	1983/2008	122,870	100.0	%	4,458	36.28
2250 E. Imperial Highway, El Segundo, California	1	1983	298,728	100.0	%	10,144	34.29
2260 E. Imperial Highway, El Segundo, California	1	1983/2012	298,728	100.0	%	10,405	34.83
909 Sepulveda Blvd., El Segundo, California	1	1972/2005	241,607	89.8	%	5,609	26.27
999 Sepulveda Blvd., El Segundo, California	1	1962/2003	128,504	94.4	%	2,768	24.40
3750 Kilroy Airport Way, Long Beach, California[(4)]	1	1989	10,457	86.1	%	99	18.17
3760 Kilroy Airport Way, Long Beach, California	1	1989	165,278	92.7	%	4,379	28.85
3780 Kilroy Airport Way, Long Beach, California	1	1989	219,745	92.2	%	5,589	28.15
3800 Kilroy Airport Way, Long Beach, California	1	2000	192,476	100.0	%	5,538	28.77
3840 Kilroy Airport Way, Long Beach, California	1	1999	136,026	100.0	%	4,915	36.13
3900 Kilroy Airport Way, Long Beach, California	1	1987	126,840	90.9	%	2,588	23.62
12100 W. Olympic Blvd., Los Angeles, California	1	2003	150,167	92.3	%	5,392	38.90
12200 W. Olympic Blvd., Los Angeles, California	1	2000	150,302	99.7	%	4,504	39.39
12233 W. Olympic Blvd., Los Angeles, California[(21)]	1	1980/2011	151,029	96.8	%	2,580	48.18
12312 W. Olympic Blvd, Los Angeles, California[(3)]	1	1950/1997	78,000	100.0	%	1,475	18.91
6255 W. Sunset Blvd, Los Angeles, California	1	1971/1999	321,883	85.2	%	7,911	30.26

1633 26th Street, Santa Monica, California	1	1972/1997	44,915	100.0	%	1,271	28.30
2100/2110 Colorado Avenue, Santa Monica, California	3	1992/2009	102,864	100.0	%	3,846	37.39
3130 Wilshire Blvd., Santa Monica, California	1	1969/1998	88,339	76.5	%	2,329	34.48
501 Santa Monica Blvd., Santa Monica, California	1	1974	73,115	85.1	%	2,201	40.31
2829 Townsgate Road, Thousand Oaks, California	1	1990	81,067	90.6	%	1,977	27.46
Subtotal/Weighted Average—Los Angeles and Ventura Counties	27		3,487,741	94.0	%	98,010	31.66
San Diego County							
12225 El Camino Real, Del Mar, California(5)	1	1998	60,148	73.4	%	1,472	33.36

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Property Location	No. of Buildings	Year Built/ Renovated	Rentable Square Feet	Percentage Occupied at 12/31/12[1]		Annualized Base Rent($000's)[2]	Annualized Rent Per Square Foot[2]
12235 El Camino Real, Del Mar, California[5]	1	1998	54,673	81.0	%	1,608	36.31
12340 El Camino Real, Del Mar, California[5]	1	2002	87,405	86.9	%	3,276	43.14
12390 El Camino Real, Del Mar, California[5]	1	2000	72,332	100.0	%	3,069	42.43
12348 High Bluff Drive, Del Mar, California[5]	1	1999	38,710	82.0	%	1,123	35.38
12400 High Bluff Drive, Del Mar, California[5]	1	2004	208,464	100.0	%	9,897	47.48
3579 Valley Centre Drive, Del Mar, California[12]	1	1999	52,375	79.0	%	1,572	37.99
3611 Valley Centre Drive, Del Mar, California[20]	1	2000	130,178	80.0	%	4,373	44.79
3661 Valley Centre Drive, Del Mar, California[5]	1	2001	129,752	99.4	%	3,870	32.53
3721 Valley Centre Drive, Del Mar, California[5]	1	2003	114,780	100.0	%	3,767	32.82
3811 Valley Centre Drive, Del Mar, California[6]	1	2000	112,067	100.0	%	5,199	46.39
6200 Greenwich Drive, Governor Park, California[6]	1	1999	71,000	100.0	%	1,704	24.00
6220 Greenwich Drive, Governor Park , California[5]	1	1996	141,214	100.0	%	4,286	30.35
15051 Avenue of Science, I-15 Corridor, California[6]	1	2002	70,617	—	%	—	—
15073 Avenue of Science, I-15 Corridor, California[6]	1	2002	46,759	—	%	—	—
15231 Avenue of Science, I-15 Corridor, California[13]	1	2005	65,638	100.0	%	1,331	20.28
15253 Avenue of Science, I-15 Corridor, California[6]	1	2005	37,437	100.0	%	610	16.29
15333 Avenue of Science, I-15 Corridor, California[25]	1	2006	78,880	46.4	%	765	20.89
15378 Avenue of Science, I-15 Corridor, California[22]	1	1990	68,910	61.8	%	660	15.49
15435 Innovation Drive, I-15 Corridor, California[5]	1	2000	49,863	100.0	%	1,243	24.93
15445 Innovation Drive, I-15 Corridor, California[5]	1	2000	51,500	100.0	%	1,318	25.59
13280 Evening Creek Drive South, I-15 Corridor, California[5]	1	2008	41,665	67.0	%	598	21.41
13290 Evening Creek Drive South,	1	2008	61,176	—	%	—	—

I-15 Corridor, California							
13480 Evening Creek Drive North, I-15 Corridor, California[5]	1	2008	149,817	100.0	%	7,779	51.92
13500 Evening Creek Drive North, I-15 Corridor, California[5]	1	2004	147,533	100.0	%	6,280	42.57
13520 Evening Creek Drive North, I-15 Corridor, California[5]	1	2004	141,129	92.4	%	4,648	36.48
7525 Torrey Santa Fe, 56 Corridor, California[6]	1	2007	103,979	100.0	%	3,012	28.97
7535 Torrey Santa Fe, 56 Corridor, California[6]	1	2007	130,243	100.0	%	3,693	28.35
7545 Torrey Santa Fe, 56 Corridor, California[6]	1	2007	130,354	100.0	%	3,609	27.69
7555 Torrey Santa Fe, 56 Corridor, California[6]	1	2007	101,236	100.0	%	3,175	31.36
2355 Northside Drive, Mission Valley, California[5]	1	1990	53,610	84.5	%	1,235	27.25
2365 Northside Drive, Mission Valley, California[5]	1	1990	91,260	86.8	%	2,281	28.81

Property Location	No. of Buildings	Year Built/ Renovated	Rentable Square Feet	Percentage Occupied at 12/31/12[1]		Annualized Base Rent($000's)[2]	Annualized Rent Per Square Foot[2]
2375 Northside Drive, Mission Valley, California[5]	1	1990	51,516	100.0	%	1,429	28.84
2385 Northside Drive, Mission Valley, California[5]	1	2008	88,795	76.5	%	2,135	31.43
2305 Historic Decatur Road, Point Loma, California[16]	1	2009	103,900	100.0	%	3,980	38.31
10020 Pacific Mesa Blvd, Sorrento Mesa, California[3]	1	2007	318,000	100.0	%	7,683	24.16
4910 Directors Place, Sorrento Mesa, California[6]	1	2009	50,925	49.9	%	963	37.90
4921 Directors Place, Sorrento Mesa, California[5]	1	2008	56,136	100.0	%	1,347	24.00
4939 Directors Place, Sorrento Mesa, California[6]	1	2002	60,662	100.0	%	2,276	37.52
4955 Directors Place, Sorrento Mesa, California[6]	1	2008	76,246	100.0	%	2,881	37.79
5005 Wateridge Vista Drive, Sorrento Mesa, California[26]	1	1999	61,460	—	%	—	—
5010 Wateridge Vista Drive, Sorrento Mesa, California[6]	1	1999/2012	111,318	100.0	%	3,552	31.91
10770 Wateridge Circle, Sorrento Mesa, California[18]	1	1989	174,310	97.5	%	3,073	18.08
6055 Lusk Avenue, Sorrento Mesa, California[3]	1	1997	93,000	100.0	%	1,554	16.71
6260 Sequence Drive, Sorrento Mesa, California[6]	1	1997	130,536	100.0	%	1,269	9.72
6290 Sequence Drive, Sorrento Mesa, California[6]	1	1997	90,000	100.0	%	2,098	23.31
6310 Sequence Drive, Sorrento Mesa, California[6]	1	2000	62,415	100.0	%	1,133	18.15
6340 Sequence Drive, Sorrento Mesa, California[6]	1	1998	66,400	100.0	%	1,341	20.20
6350 Sequence Drive, Sorrento Mesa, California	1	1998	132,600	100.0	%	2,507	18.91
10390 Pacific Center Court, Sorrento Mesa, California[6]	1	2002	68,400	100.0	%	2,771	40.51
10394 Pacific Center Court, Sorrento Mesa, California[6]	1	1995	59,630	100.0	%	1,077	18.06
10398 Pacific Center Court, Sorrento Mesa, California[6]	1	1995	43,645	100.0	%	698	15.99
10421 Pacific Center Court, Sorrento Mesa, California[17]	1	1995/2002	75,899	100.0	%	1,076	14.18
10445 Pacific Center Court, Sorrento Mesa, California[6]	1	1995	48,709	100.0	%	1,029	21.13
10455 Pacific Center Court,	1	1995	90,000	100.0	%	1,112	12.36

Sorrento Mesa, California							
5717 Pacific Center Blvd, Sorrento Mesa, California[3]	1	2001/2005	67,995	100.0	%	1,503	22.10
4690 Executive Drive, UTC, California[8]	1	1999	47,212	100.0	%	1,134	24.02
9785 Towne Center Drive, UTC, California[3]	1	1999	75,534	100.0	%	1,374	18.19
9791 Towne Center Drive, UTC, California[3]	1	1999	50,466	100.0	%	916	18.15
Subtotal/Weighted Average—San Diego County	59		5,250,413	90.7	%	139,364	29.39
Orange County							
8101 Kaiser Blvd. Anaheim, California	1	1988	59,790	61.0	%	848	23.26
2211 Michelson, Irvine, California[19]	1	2007	271,556	94.0	%	9,704	38.51

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Property Location	No. of Buildings	Year Built/ Renovated	Rentable Square Feet	Percentage Occupied at 12/31/12[1]		Annualized Base Rent($000's)[2]	Annualized Rent Per Square Foot[2]
111 Pacifica, Irvine Spectrum, California	1	1991	67,496	100.0	%	1,377	21.77
999 Town & Country, Orange, California	1	1977/2009	98,551	100.0	%	2,919	29.62
Subtotal/Weighted Average—Orange County	4		497,393	92.0	%	14,848	32.98
San Francisco							
4100 Bohannon Drive, Menlo Park, California[6]	1	1985	46,614	100.0	%	1,719	36.88
4200 Bohannon Drive, Menlo Park, California[6]	1	1987	46,255	100.0	%	1,573	39.78
4300 Bohannon Drive, Menlo Park, California[6]	1	1988	62,920	41.7	%	876	33.42
4400 Bohannon Drive, Menlo Park, California[6]	1	1988	46,255	84.2	%	1,159	32.62
4500 Bohannon Drive, Menlo Park, California[6]	1	1990	62,920	100.0	%	2,041	32.44
4600 Bohannon Drive, Menlo Park, California[6]	1	1990	46,255	71.2	%	1,297	39.39
4700 Bohannon Drive, Menlo Park, California[6]	1	1989	62,920	100.0	%	2,275	36.16
303 Second Street, San Francisco, California	1	1988	740,047	95.5	%	26,232	37.26
100 First Street, San Francisco, California	1	1988	466,490	98.3	%	19,118	42.80
250 Brannan Street, San Francisco, California[5]	1	1907/2001	92,948	100.0	%	3,983	42.85
201 Third Street, San Francisco, California	1	1983	332,893	99.5	%	13,024	40.40
301 Brannan Street, San Francisco, California[5]	1	1909/1989	74,430	100.0	%	3,024	40.63
4040 Civic Center, San Rafael, California	1	1979/1994	130,237	98.1	%	2,528	20.30
599 Mathilda, Sunnyvale, California	1	2000	75,810	100.0	%	2,201	29.03
Subtotal/Weighted Average—San Francisco	14		2,286,994	95.5	%	81,050	37.74
Greater Seattle							
601 108th Avenue NE, Bellevue, Washington[23]	1	2000	488,470	90.4	%	11,851	27.24
10900 NE 4th Street, Bellevue, Washington	1	1983	416,755	90.5	%	12,691	33.68
10220 NE Points Drive, Kirkland, Washington[3]	1	1987	49,851	96.3	%	1,222	25.71
10230 NE Points Drive,	1	1988	98,982	100.0	%	2,661	27.28

Kirkland, Washington[3]							
10210 NE Points Drive, Kirkland, Washington[3]	1	1990	84,641	69.2	%	1,428	24.38
3933 Lake Washington Blvd NE, Kirkland, Washington[3]	1	1993	46,450	100.0	%	1,209	26.03
15050 N.E. 36th Street, Redmond, Washington[3]	1	1998	122,103	100.0	%	3,130	25.63
837 N. 34th Street, Lake Union, Washington[3]	1	2008	111,580	100.0	%	2,694	24.14
701 N. 34th Street, Lake Union, Washington[24]	1	1998	138,995	98.7	%	2,541	18.51
801 N. 34th Street, Lake Union, Washington[3]	1	1998	169,412	100.0	%	4,423	26.11
Subtotal/Weighted Average—Greater Seattle	10		1,727,239	93.3	%	43,850	27.37
TOTAL/WEIGHTED AVERAGE	114		13,249,780	92.8	%	$ 377,122	$31.33

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(1) Based on all leases at the respective properties in effect as of December 31, 2012. Includes month-to-month leases as of December 31, 2012.

(2) Annualized base rental revenue includes the impact of straight-lining rent escalations and the amortization of free rent periods and excludes the impact of the following: amortization of deferred revenue related tenant-funded tenant improvements, amortization of above/below market rents, amortization for lease incentives due under existing leases, and expense reimbursement revenue. Excludes month-to-month leases and vacant space as of December 31, 2012.

(3) For these properties, the leases are written on a triple net basis.

(4) For this property, leases of approximately 5,000 rentable square feet are written on a modified gross basis, and a lease of approximately 2,000 rentable square feet is written on a full service gross basis.

(5) For these properties, the leases are written on a modified gross basis.

(6) For these properties, the leases are written on a modified net basis.

(7) For this property, a lease of approximately 20,000 rentable square feet is written on a modified net basis, and leases of approximately 17,000 rentable square feet are written on a modified gross basis. The remaining 6,000 rentable square feet is currently being marketed for lease.

(8) For this property, leases of approximately 19,000 rentable square feet are written on a modified net basis, and leases of approximately 28,000 rentable square feet are written on a modified gross basis.

(9) For this property, leases of approximately 15,000 rentable square feet are written on a full service gross basis, leases of approximately 42,000 rentable square feet are written on a triple net basis, and leases of approximately 18,000 rentable square feet are written on a modified net basis.

(10) For this property, a lease of approximately 15,000 rentable square feet is written on a modified gross basis, and a lease of approximately 56,000 rentable square feet is written on a triple net basis.

(11) For these properties, leases of approximately 142,000 rentable square feet are written on a modified net basis, and a lease of approximately 37,000 rentable square feet is written on a modified gross basis.

(12) For this property, a lease of approximately 41,000 rentable square feet is written on a modified gross basis. The remaining 11,000 rentable square feet is currently being marketed for lease.

(13) For this property, a lease of approximately 47,000 rentable square feet is written on a modified net basis. A lease of approximately 18,000 rentable square feet is written on a modified gross basis.

(14) For this property, leases of approximately 30,000 rentable square feet are written on a modified gross basis.

(15) For this property, a lease of approximately 70,000 rentable square feet is written on a modified net basis, and a lease of approximately 15,000 rentable square feet is written on a triple net basis.

(16) For this property, leases of approximately 82,000 rentable square feet are written on a modified gross basis, and a lease of approximately 22,000 rentable square feet is written on a gross basis.

(17) For this property, leases of approximately 76,000 rentable square feet are written on a modified net basis.

(18) For this property, leases of approximately 123,000 rentable square feet are written on a modified net basis, and leases of 47,000 rentable square feet are written on a modified gross basis.

(19) For this property, leases of approximately 217,000 rentable square feet are written on a direct expense stop basis, and leases of 38,000 rentable square feet are written on a full service gross basis.

(20) For this property, leases of approximately 104,000 rentable square feet are written on a modified gross basis. The remaining 26,000 rentable square feet is currently being marketed for lease.

(21) For this property, leases of approximately 105,000 rentable square feet are written on a full service gross basis, and leases of 41,000 rentable square feet are written on a modified gross basis.

(22) For this property, a lease of approximately 69,000 rentable square feet is written on a modified net basis, and a lease of approximately 43,000 rentable square feet is written on a modified gross basis.

(23) For this property, a lease of approximately 360,000 rentable square feet are written on a triple net basis, and leases of approximately 73,000 rentable square feet are written on a full service gross basis.

(24) For this property, a lease of approximately 118,000 rentable square feet are written on a triple net basis, and leases of approximately 20,000 rentable square feet are written on a modified net basis.

For this property, leases of approximately 37,000 rentable square feet are written on a modified gross basis.

(25) Leases of approximately 38,000 rentable square feet were executed with two tenants during the fourth quarter of 2012. The new leases are expected to commence in the first and third quarters of 2013.

(26) For this property, a lease of approximately 61,000 rentable square feet was executed with one tenant during the fourth quarter of 2012. The new lease is expected to commence in the third quarter of 2013.

Completed and In-Process Redevelopment Projects

During the year ended December 31, 2012, we completed the following redevelopment projects, which were added to our stabilized portfolio of operating properties:

	Construction Period				
Completed Redevelopment Projects	Start Date	Completion Date	Rentable Square Feet	% Leased	
2260 E. Imperial Highway El Segundo, California [(1)]	3Q 2010	4Q 2012	299,000	100	%
5010 Wateridge Vista Drive Sorrento Mesa, California	3Q 2011	4Q 2012	111,000	100	%
			410,000	100	%

(1) Cash rent for this property commenced in December 2012. Completion of remaining tenant improvements and physical occupancy are expected to continue through April 2013.

As of December 31, 2012, we had the following redevelopment projects in lease up or under construction.

In-Process Redevelopment Projects	Estimated Construction Period Start Date	Estimated Compl. Date	Estimated Stabilization Date (1)	Estimated Rentable Square Feet	% Leased	
Projects In Lease-Up (2)						
3880 Kilroy Airport Way Long Beach, California (3)	3Q 2011	4Q 2012	4Q 2013	98,000	50	%
Under Construction						
360 Third Street San Francisco, California (4)(5)	4Q 2011	1Q 2013	1Q 2014	410,000	75	%
				508,000	70	%

(1) Based on management's estimation of the earlier of stabilized occupancy (95%) or one year from the date of substantial completion.
(2) Lease-up properties represent properties recently redeveloped that have not reached 95% occupancy and are within one year following cessation of major construction activities.
(3) This property was 50% leased prior to any redevelopment activity, which occurred in two phases. Redevelopment on the first half was completed during the second quarter of
2012, and the tenant has taken occupancy of this space. Redevelopment on the second half was completed in the fourth quarter of 2012.
(4) Approximately 91% of this project is being redeveloped because approximately 9% of the project was leased and occupied by an existing tenant upon acquisition in December
2011. In July 2012, approximately 17% of the building was completed and the tenant has taken occupancy of the space. The remaining 74% of the building remains under
redevelopment. Redevelopment costs are capitalized only on the portion of the building that is under redevelopment and not occupied by tenants.
(5) During the fourth quarter of 2012, the Company exercised its option to acquire the land underlying the current ground lease for $27.5 million. We currently expect that the
transaction will close in the second quarter of 2013.

In-Process and Future Development Pipeline and Other Land Holdings

The following table sets forth certain information relating to our in-process development pipeline as of December 31, 2012.

In-Process Development Pipeline	Location	Estimated Construction Period Start Date	Estimated Compl. Date	Estimated Stabilization Date (1)	Estimated Rentable Square Feet	% Leased
San Francisco Bay Area						
690 E. Middlefield Road	Mountain View	2Q 2012	1Q 2015	1Q 2015	341,000	100%
331 Fairchild Drive	Mountain View	4Q 2012	4Q 2013	4Q 2013	88,000	100%
350 Mission Street (2)	San Francisco	4Q 2012	1Q 2015	4Q 2015	400,000	100%

555 N. Mathilda Avenue	Sunnyvale	4Q 2012	3Q 2014	3Q 2014	587,000	100%
					1,416,000	100%

(1) Based on management's estimation of the earlier of stabilized occupancy (95%) or one year from the date of substantial completion.
(2) Estimated rentable square feet reflects existing entitlements for 27-story office tower. The Company is currently pursuing entitlements to increase this project to a 30-story office tower, which would increase the estimated rentable square feet and total estimated investment.

The following table sets forth certain information relating to our future development pipeline as of December 31, 2012.

Project	Location	Estimated Rentable Square Feet
Future Development Pipeline		
San Francisco Bay Area		
333 Brannan Street	San Francisco	170,000
Los Angeles		
Columbia Square [1]	Hollywood	600,000
San Diego		
9455 Towne Centre Drive [2]	San Diego	150,000
Carlsbad Oaks—Lots 4, 5, 7 & 8	Carlsbad	288,000
Pacific Corporate Center—Lot 8	Sorrento Mesa	170,000
Rancho Bernardo Corporate Center	I-15 Corridor	320,000 - 1,000,000
One Paseo [3]	Del Mar	500,000
Santa Fe Summit—Phase II and III	56 Corridor	600,000
Sorrento Gateway—Lot 2	Sorrento Mesa	80,000
Subtotal		2,108,000 - 2,788,000

(1) The Company is planning to redevelop an existing building encompassing approximately 100,000 rentable square feet and develop a mixed-use plan encompassing approximately 500,000 rentable square feet, which will include office, multi-family and retail components.

(2) The Company is planning to demolish the existing two-story 45,195 rentable square foot office building at this site and pursue entitlements to build a new 5-story 150,000 rentable square foot office building.

(3) Estimated rentable square feet reflects existing office entitlements. The Company is currently pursuing mixed-use entitlements for this project which would increase the estimated rentable square feet.

The following table sets forth certain information about our other land holdings as of December 31, 2012.

Other Land Holdings	
Project	Gross Site Acreage
17150 Von Karman Irvine, California	8.5

During the fourth quarter of 2011, the Company completed demolition of the industrial building at 17150 Von Karman. Simultaneously, the Company successfully obtained entitlements to reposition this site for residential use in preparation of a possible land sale. The Company's ultimate decision to sell this site and the timing of any potential future sale is dependent upon market conditions and other factors.

Significant Tenants

The following table sets forth information about our 15 largest tenants based upon annualized base rental revenues, as defined below, as of December 31, 2012.

Tenant Name	Annualized Base Rental Revenue[(1)] (in thousands)	Percentage of Total Annualized Base Rental Revenue[(1)]	Lease Expiration Date
DIRECTV, LLC	$23,377	6.2%	September 2027
Intuit, Inc.	15,193	4.0	Various[(2)]
Bridgepoint Education, Inc	15,105	4.0	Various[(3)]
Delta Dental of California	10,275	2.7	May 2015
CareFusion Corporation [(9)]	9,256	2.5	August 2017
AMN Healthcare, Inc.	8,192	2.2	July 2018
Adobe Systems, Inc. [(9)]	6,557	1.7	Various[(4)]
Fish & Richardson P.C.	6,071	1.6	October 2018
Wells Fargo [(9)]	5,346	1.4	Various[(5)]
Scripps Health	5,199	1.4	June 2021
BP Biofuels	5,128	1.4	Various[(6)]
Lucile Salter Packard Children's Hospital at Stanford	5,109	1.4	Various[(7)]
Epson America, Inc.	4,915	1.3	October 2019
Scan Health Plan [(9)]	4,505	1.2	June 2015
Avnet, Inc.	4,163	1.1	Various[(8)]
Total	$128,391	34.1%	

(1) Represents annualized contractual base rent calculated on a straight-line basis in accordance with GAAP, excluding the above/below market rent amortization and expense reimbursement revenue, for leases from which rental revenue is being recognized by us as of December 31, 2012.

(2) The Intuit Inc. leases, which contribute $1.7 million and $13.5 million expire in December 2012 and August 2017, respectively.

(3) The Bridgepoint Education Inc. leases, which contribute $1.0 million, $6.3 million and $7.8 million expire in February 2017, July 2018 and September 2018, respectively.

(4) The Adobe Systems Inc. leases, which contribute $1.6 million and $5.0 million expire in May 2013 and July 2020, respectively.

(5) The Wells Fargo leases, which contribute $0.05 million, $0.1 million, $1.0 million, $0.3 million, $0.4 million, $1.4 million, $2.0 million, $0.05 million and $0.1 million expire in March 2013, January 2014, November 2014, August 2015, July 2016, September 2016, September 2017, February 2018 and February 2019, respectively.

(6) The BP Biofuel leases, which contribute $2.8 million and $2.3 million expire in November 2015 and March 2017, respectively.

(7) The Lucile Salter Packard Children's Hospital at Stanford leases, which contribute $0.4 million and $4.7 million expire in November 2015 and September 2020, respectively.

(8) The Avnet Inc. leases, which contribute $3.8 million and $0.4 million expire in February 2013 and January 2018, respectively.

(9) The Company has entered into leases with various affiliates of the tenant name listed above.

The following pie chart sets forth the composition of our tenant base by industry and as a percentage of our annualized base rental revenue based on the Standard Industrial Classifications as of December 31, 2012.

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Lease Expirations

The following table sets forth a summary of our lease expirations for each of the next ten years beginning with 2013, assuming that none of the tenants exercise renewal options or termination rights. See further discussion of our lease expirations under "Item 1A: Risk Factors".

Lease Expirations [(1)]

Year of Lease Expiration	# of Expiring Leases	Total Square Feet	% of Total Leased Square Feet		Annualized Base Rent (000's)[(1)]	% of Total Annualized Base Rent[(1)]		Annualized Rent per Square Foot[(1)]
2013	94	855,902	7.1	%	$22,524	6.0	%	$26.32
2014	121	1,250,019	10.4	%	36,098	9.6	%	28.88
2015	151	2,124,976	17.7	%	65,432	17.4	%	30.79
2016	74	808,217	6.7	%	21,119	5.6	%	26.13
2017	99	1,951,623	16.2	%	58,162	15.4	%	29.80
2018	52	1,281,765	10.6	%	49,569	13.1	%	38.67
2019	31	902,246	7.5	%	31,315	8.3	%	34.71
2020	30	1,200,994	10.0	%	36,562	9.7	%	30.44
2021	18	445,767	3.7	%	14,960	4.0	%	33.56
2022	8	128,076	1.1	%	5,153	1.4	%	40.23
2023 and beyond	16	1,088,198	9.0	%	36,228	9.5	%	33.29
Total[(2)]	694	12,037,783	100.0	%	$377,122	100.0	%	$31.33

(1) Annualized base rent includes the impact of straight-lining rent escalations and the amortization of free rent periods and excludes the impact of the following: amortization of deferred revenue related tenant-funded tenant improvements, amortization of above/below market rents, amortization for lease incentives due under existing leases, and expense reimbursement revenue. Additionally, the underlying leases contain various expense structures including full service gross, modified gross and triple net. Amounts represent percentage of total portfolio annualized contractual base rental revenue.

(2) The information presented for all lease expiration activity reflects leasing activity through December 31, 2012 for our stabilized portfolio. For leases that have been renewed early or space that has been re-leased to a new tenant, the expiration date and annualized base rent information presented takes into consideration the renewed or re-leased lease terms. Excludes space leased under month-to-month leases, vacant space, and lease renewal options not executed as of December 31, 2012.

Secured Debt

As of December 31, 2012, the Operating Partnership had nine outstanding mortgage notes payable, which were secured by certain of our properties. Our secured debt represents an aggregate indebtedness of approximately $553.9 million. See additional information regarding our secured debt in "Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations —Liquidity and Capital Resources—Liquidity Sources," Notes 6 and 7 to our consolidated financial statements, and Schedule III—Real Estate and Accumulated Depreciation included with this report. Management believes that, as of December 31, 2012, the value of the properties securing the applicable secured obligations in each case exceeded the principal amount of the outstanding obligation.

ITEM 3. LEGAL PROCEEDINGS

We and our properties are subject to routine litigation incidental to our business. As of December 31, 2012, we are not a defendant in, and our properties are not subject to, any legal proceedings that we believe, if determined adversely to us, would have a material adverse effect upon our financial condition, results of operations, or cash flows.

ITEM 4. MINE SAFETY DISCLOSURES

None.

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PART II

ITEM 5. MARKET FOR KILROY REALTY CORPORATION'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

The Company's common stock is traded on the New York Stock Exchange (“NYSE”) under the symbol “KRC.” As of the date this report was filed, there were approximately 65 registered holders of the Company's common stock. The following table illustrates the high, low, and closing prices by quarter, as well as dividends declared, during 2012 and 2011 as reported on the NYSE.

2012	High	Low	Close	Per Share Common Stock Dividends Declared
First quarter	$46.61	$37.92	$46.61	$ 0.3500
Second quarter	48.58	44.84	48.41	0.3500
Third quarter	49.88	44.78	44.78	0.3500
Fourth quarter	47.52	42.47	47.37	0.3500
2011	High	Low	Close	Per Share Common Stock Dividends Declared
First quarter	$39.24	$36.61	$38.83	$ 0.3500
Second quarter	41.94	38.04	39.49	0.3500
Third quarter	41.58	30.01	31.30	0.3500
Fourth quarter	38.57	29.25	38.07	0.3500

The Company pays distributions to common stockholders quarterly each January, April, July, and October at the discretion of the board of directors. Distribution amounts depend on our FFO, financial condition, capital requirements, the annual distribution requirements under the REIT provisions of the Code, and such other factors as the board of directors deems relevant.

MARKET FOR KILROY REALTY, L.P.'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

There is no established public trading market for the Operating Partnership’s common units. As of the date this report was filed, there were 24 holders of record of common units (including through the Company’s general partnership interest).

The following table reports the distributions per common unit declared during the years ended December 31, 2012 and 2011.

2012	Per Unit Common Unit Distribution Declared
First quarter	$0.3500
Second quarter	0.3500
Third quarter	0.3500
Fourth quarter	0.3500
2011	Per Unit Common Unit Distribution Declared
First quarter	$0.3500
Second quarter	0.3500
Third quarter	0.3500
Fourth quarter	0.3500

During 2012 and 2011, the operating partnership redeemed 10,000 and 5,000 common units, respectively, for the same number of shares of the Company's common stock.

PERFORMANCE GRAPH

The following line graph compares the change in cumulative stockholder return on shares of the Company's common stock to the cumulative total return of the NAREIT All Equity REIT Index, the Standard & Poor’s 500 Stock Index, and the SNL REIT Office Index for the five-year period ended December 31, 2012. We include an additional index, the SNL REIT Office Index, to the performance graph since management believes it provides additional information to investors about our performance relative to a more specific peer group. The SNL REIT Office Index is a published and widely recognized index that comprises 19 office equity REITs, including us. The graph assumes the investment of $100 in us and each of the indices on December 31, 2007 and, as required by the SEC, the reinvestment of all distributions. The return shown on the graph is not necessarily indicative of future performance.

ITEM 6. SELECTED FINANCIAL DATA - KILROY REALTY CORPORATION

The following tables set forth selected consolidated financial and operating data on an historical basis for the Company. The following data should be read in conjunction with our financial statements and notes thereto and “Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations” included below in this report.

The consolidated balance sheet data as of December 31, 2012 and 2011 and the consolidated statement of operations data for the years ended December 31, 2012, 2011 and 2010 have been derived from the historical consolidated financial statements of Kilroy Realty Corporation audited by Deloitte & Touche LLP, an independent registered public accounting firm. The consolidated balance sheet data as of December 31, 2010, 2009 and 2008 and the consolidated statement of operations data for the years ended December 31, 2009 and 2008 have been derived from the historical consolidated financial statements of Kilroy Realty Corporation and adjusted for the impact of subsequent accounting changes requiring retrospective application, if any.
Kilroy Realty Corporation Consolidated
(in thousands, except share, per share, square footage and occupancy data)

	Year Ended December 31,				
	2012	2011	2010	2009	2008
Statements of Operations Data:					
Total revenues from continuing operations	$404,912	$337,629	$254,994	$230,571	$244,294
Income (loss) from continuing operations	5,447	(3,728)	(427)	15,569	28,181
Income from discontinued operations	271,654	71,217	20,313	22,446	18,730
Net income available to common stockholders	249,826	50,819	4,512	21,794	29,829
Per-Share Data:					
Weighted average common shares outstanding-basic	69,639,623	56,717,121	49,497,487	38,705,101	32,466,591
Weighted average common shares outstanding-diluted	69,639,623	56,717,121	49,497,487	38,732,126	32,540,872
(Loss) income from continuing operations available to common stockholders per common share-basic	$(0.24)	(0.35)	(0.33)	(0.02)	0.37
(Loss) income from continuing operations available to common stockholders per common share-diluted	$(0.24)	(0.35)	(0.33)	(0.02)	0.37
Net income available to common stockholders per share-basic	$3.56	0.87	0.07	0.53	0.91
Net income available to common stockholders per share-diluted	$3.56	0.87	0.07	0.53	0.91
Dividends declared per common share	$1.40	1.40	1.40	1.63	2.32

	December 31, 2012	2011	2010	2009	2008
Balance Sheet Data:					
Total real estate held for investment, before accumulated depreciation and amortization	$4,757,394	$3,798,690	$3,216,871	$2,520,083	$2,475,596
Total assets	4,616,084	3,446,795	2,816,565	2,084,281	2,102,918
Total debt	2,040,935	1,821,286	1,427,776	972,016	1,142,348
Total noncontrolling interest - preferred units(1)	—	73,638	73,638	73,638	73,638
Total preferred stock	192,411	121,582	121,582	121,582	121,582
Total equity(2)	2,235,933	1,327,482	1,117,730	883,838	714,886
Other Data:					
Funds From Operations(3)	$165,455	$136,173	$106,639	$107,159	$113,972
Cash flows provided by (used in):					
Operating activities	180,724	138,256	119,827	124,965	144,481
Investing activities	(706,506)	(634,283)	(701,774)	(50,474)	(93,825)
Financing activities	537,705	485,964	586,904	(74,161)	(52,835)
Property Data:					
Office Properties:					
Rentable square footage	13,249,780	11,421,112	10,395,208	8,708,466	8,650,126
Occupancy	92.8%	90.1%	87.5%	80.6%	86.2%
Industrial Properties:					
Rentable square footage	(4)	3,413,354	3,602,896	3,654,463	3,718,663
Occupancy	(4)	100.0%	93.9%	88.2%	96.3%

(1) Represents the redemption value, less issuance costs of our issued and outstanding 1,500,000 Series A Preferred Units. The Series A Preferred Units were redeemed in 2012. See Note 9 in our consolidated financial statements included in this report for additional information.

(2) Includes the noncontrolling interest of the common units of the Operating Partnership.

(3) The Company calculates FFO in accordance with the White Paper on FFO approved by the Board of Governors of NAREIT. The White Paper defines FFO as net income or loss calculated in accordance with GAAP, excluding extraordinary items, as defined by GAAP, gains and losses from sales of depreciable real estate and impairment write-downs associated with depreciable real estate, plus real estate-related depreciation and amortization (excluding amortization of deferred financing costs and depreciation of non-real estate assets), and after adjustment for unconsolidated partnerships and joint ventures.

Management believes that FFO is a useful supplemental measure of the Company's operating performance. The exclusion from FFO of gains and losses from the sale of operating real estate assets allows investors and analysts to readily identify the operating results of the assets that form the core of the Company's activity and assists in comparing those operating results between periods. Also, because FFO is generally recognized as the industry standard for reporting the operations of REITs, it facilitates comparisons of operating performance to other REITs. However, other REITs may use different methodologies to calculate FFO, and accordingly, the Company's FFO may not be comparable to all other REITs.

Implicit in historical cost accounting for real estate assets in accordance with GAAP is the assumption that the value of real estate assets diminishes predictably over time. Since real estate values have historically risen or fallen with market conditions, many industry investors and analysts have considered presentations of operating results for real estate companies using historical cost accounting alone to be insufficient. Because FFO excludes depreciation and amortization of real estate assets, management believes that FFO along with the required GAAP presentations provides a more complete measurement of the Company's performance relative to its competitors and a more appropriate basis on which to make decisions involving operating, financing, and investing activities than the required GAAP presentations alone would provide.

However, FFO should not be viewed as an alternative measure of the Company's operating performance since it does not reflect either depreciation and amortization costs or the level of capital expenditures and leasing costs necessary to maintain the operating performance of the Company's properties, which are significant economic costs and could materially impact the Company's results from operations.

Noncash adjustments to arrive at FFO were as follows: noncontrolling interest in earnings of the Operating Partnership, depreciation and amortization of real estate assets, and net gain (loss) from dispositions of operating properties. For additional information, see "Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations -Non-GAAP Supplemental Financial Measure: Funds From Operations" including a reconciliation of the Company's GAAP net income available for common stockholders to FFO for the periods presented.

(4) We sold all of our industrial properties during the fourth quarter of 2012.

SELECTED FINANCIAL DATA - KILROY REALTY, L.P.

The following tables set forth selected consolidated financial and operating data on an historical basis for the Operating Partnership. The following data should be read in conjunction with our financial statements and notes thereto and "Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations" included below in this report.

The consolidated balance sheet data as of December 31, 2012 and 2011 and the consolidated statement of operations data for the years ended December 31, 2012, 2011 and 2010 have been derived from the historical consolidated financial statements of Kilroy Realty, L.P. audited by Deloitte & Touche LLP, an independent registered public accounting firm. The consolidated balance sheet data as of December 31, 2010, 2009 and 2008 and the consolidated statement of operations data for the years ended December 31, 2009 and 2008 have been derived from the historical consolidated financial statements of Kilroy Realty, L.P. and adjusted for the impact of subsequent accounting changes requiring retrospective application, if any.

Kilroy Realty, L.P. Consolidated
(in thousands, except unit, per unit, square footage and occupancy data)

	Year Ended December 31,				
	2012	2011	2010	2009	2008
Statements of Operations Data:					
Total revenues from continuing operations	$404,912	$337,629	$254,994	$230,571	$244,294
Income (loss) from continuing operations	5,447	(3,728)	(427)	15,569	28,181
Income from discontinued operations	271,654	71,217	20,313	22,446	18,730
Net income available to common unitholders	255,375	51,764	4,528	22,618	31,478
Per Unit Data:					
Weighted average common units outstanding-basic	71,403,258	58,437,444	51,220,618	40,436,196	34,531,779
Weighted average common units outstanding-diluted	71,403,258	58,437,444	51,220,618	40,463,221	34,606,060
(Loss) income from continuing operations available to common unitholders per common unit-basic	(0.24)	(0.36)	(0.33)	(0.02)	0.39
(Loss) income from continuing operations available to common unitholders per common unit-diluted	(0.24)	(0.36)	(0.33)	(0.02)	0.39
Net income available to common unitholders per unit-basic	3.56	0.86	0.07	0.53	0.90
Net income available to common unitholders per unit-diluted	3.56	0.86	0.07	0.53	0.90
Distributions declared per common unit	1.40	1.40	1.40	1.63	2.32

	December 31, 2012	2011	2010	2009	2008
Balance Sheet Data:					
Total real estate held for investment, before accumulated depreciation and amortization	$4,757,394	$3,798,690	$3,216,871	$2,520,083	$2,475,596
Total assets	4,616,084	3,446,795	2,816,565	2,084,281	2,102,918
Total debt	2,040,935	1,821,286	1,427,776	972,016	1,142,348
Series A redeemable preferred units (1)	—	73,638	73,638	73,638	73,638
Total preferred capital	192,411	121,582	121,582	121,582	121,582
Total capital (2)	2,235,933	1,327,482	1,117,730	883,838	714,886
Other Data:					
Cash flows provided by (used in):					
Operating activities	180,724	138,256	119,827	124,965	144,481
Investing activities	(706,506)	(634,283)	(701,774)	(50,474)	(93,825)
Financing activities	537,705	485,964	586,904	(74,161)	(52,835)
Property Data:					
Office Properties:					
Rentable square footage	13,249,780	11,421,112	10,395,208	8,708,466	8,650,126
Occupancy	92.8%	90.1%	87.5%	80.6%	86.2%
Industrial Properties:					
Rentable square footage	(3)	3,413,354	3,602,896	3,654,463	3,718,663
Occupancy	(3)	100.0%	93.9%	88.2%	96.3%

(1) Represents the redemption value, less issuance costs of the Operating Partnership's issued and outstanding 1,500,000 Series A Preferred Units. All Series A Preferred Units were redeemed in 2012. See Note 9 in our consolidated financial statements included in this report for additional information.
(2) Includes the noncontrolling interests in consolidated subsidiaries.
(3) We sold all of our industrial properties during the fourth quarter of 2012.

ITEM 7. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion relates to our consolidated financial statements and should be read in conjunction with the financial statements and notes thereto appearing elsewhere in this report. The results of operations discussion is combined for the Company and the Operating Partnership because there are no material differences in the results of operations between the two reporting entities.

Forward-Looking Statements

Statements contained in this “Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations” that are not historical facts may be forward-looking statements, including statements or information concerning projected future occupancy and rental rates, lease expirations, debt maturity, potential investments, strategies such as capital recycling, development and redevelopment activity, projected construction costs, dispositions, future executive incentive compensation, pending, potential or proposed acquisitions and other forward-looking financial data, as well as the discussion in “-Factors That May Influence Future Results of Operations”, “-Liquidity and Capital Resource of the Company”, and “-Liquidity and Capital Resources of the Operating Partnership.” Forward-looking statements can be identified by the use of words such as “believes,” “expects,” “projects,” “may,” “will,” “should,” “seeks,” “approximately,” “intends,” “plans,” “pro forma,” “estimates” or “anticipates” and the negative of these wor phrases and similar expressions that do not relate to historical matters. Forward-looking statements are based on our current expectations, beliefs and assumptions, and are not guarantees of future performance. Forward-looking statements are inherently subject to uncertainties, risks, changes in circumstances, trends and factors that are difficult to predict, many of which are outside of our control. Accordingly, actual performance, results and events may vary materially from those indicated in the forward-looking statements, and you should not rely on the forward-looking statements as predictions of future performance, results or outcomes. Numerous factors could cause actual future events to differ materially from those indicated in forward-looking statements, including, among others:

- global market and general economic conditions and their effect on our liquidity and financial conditions and those of our tenants;
- adverse economic or real estate conditions in California and Washington including with respect to California's continuing budget deficits;
- risks associated with our investment in real estate assets, which are illiquid, and with trends in the real estate industry;
- defaults on or non-renewal of leases by tenants;
- any significant downturn in tenants' businesses;
- our ability to re-lease property at or above current market rates;
- costs to comply with government regulations, including environmental remediations;
- the availability of cash for distribution and debt service and exposure of risk of default under debt obligations;
- significant competition, which may decrease the occupancy and rental rates of properties;
- potential losses that may not be covered by insurance;
- the ability to successfully complete acquisitions and dispositions on announced terms;
- the ability to successfully operate acquired properties;
- the ability to successfully complete development and redevelopment properties on schedule and within budgeted amounts;
- defaults on leases for land on which some of our properties are located;
- adverse changes to, or implementations of, applicable laws, regulations or legislation;
- environmental uncertainties and risks related to natural disasters; and
- the Company's ability to maintain its status as a REIT.

The factors included in this report are not exhaustive and additional factors could adversely affect our business and financial performance. For a discussion of additional risk factors, see the factors included in this report under the caption “Risk Factors,” and in our other filings with the SEC. All forward-looking statements are based on currently available information and speak only as of the date of this report. We assume no obligation to update any forward-looking statement that becomes untrue because of subsequent events, new information or otherwise, except to the extent we are required to do so in connection with our ongoing requirements under federal securities laws.

Company Overview
We are a self-administered REIT active in office submarkets along the West Coast. We own, develop, acquire and manage real estate assets, consisting primarily of Class A properties in the coastal regions of Los Angeles, Orange County, San Diego County, the San Francisco Bay Area and greater Seattle, which we believe have strategic advantages and strong barriers to entry. We own our interests in all of our properties through the Operating Partnership and the Finance Partnership, and conduct substantially all of our operations through the Operating Partnership. We owned a 97.6% and 97.2% general partnership interest in the Operating Partnership as of December 31, 2012 and 2011, respectively. All our properties are held in fee except for the 11 office buildings which are held subject to long-term ground leases for the land (See Note 15 to our consolidated financial statements included in this report for additional information regarding our ground lease obligations).
2012 Highlights
We made significant progress on several fronts during 2012, and are well-positioned for continued long-term growth through our strong leasing performance, well timed acquisitions, development and redevelopment efforts, ongoing capital recycling program, and successful financing activities.
Leasing - During 2012, we executed new and renewal office leases on 2.3 million square feet, our highest annual leasing performance since our formation in 1997. This leasing activity included a lease signed with salesforce.com for approximately 445,000 rentable square feet. As a result of our consistent and successful leasing efforts, occupancy in our stabilized office portfolio increased to 92.8% as of December 31, 2012, up from 90.1% as of December 31, 2011.
Operating Property Acquisitions - We remain a disciplined buyer of office properties and continue to focus on value add opportunities in West Coast markets populated by high growth tenants in a variety of industries, including technology, media, healthcare, entertainment and services. During 2012, we continued to expand our portfolio in the San Francisco Bay Area, greater Seattle, and Los Angeles through the acquisitions of eight buildings, four buildings and two buildings, in each respective region, for a total purchase price of approximately $674.0 million. As a result of the 2012 acquisitions, our stabilized portfolio has increased by approximately 1.8 million rentable square feet (see Note 3 to our consolidated financial statements included in this report for additional information).
Development Site Acquisitions - During 2012, we increased our focus on value-add and highly accretive development opportunities and expanded our future development pipeline through targeted acquisitions of development opportunities on the West Coast.
We further expanded our presence in the San Francisco Bay Area and Los Angeles through the purchase of six ground-up development opportunities, five of which are located in the San Francisco Bay Area and one that is located in the Hollywood submarket of Los Angeles. We commenced construction on four of the development opportunities located in the San Francisco Bay Area upon acquisition and expect construction to be completed at various dates beginning in late 2013 through late 2015. The remaining two development opportunities located in San Francisco and Hollywood have been added to our future development pipeline and we expect to begin construction during the first and fourth quarter of 2013 (see "—Factors that May Influence Future Operations - In-Process and Future Development Pipeline" for additional information). The total purchase price of these acquisitions was approximately $340.3 million.
Redevelopment - During 2012, we completed two of our redevelopment projects and added these projects to our stabilized portfolio. We completed both projects at a total estimated investment of approximately $97.8 million, including the $31.3 million net carrying value of the projects at the commencement of redevelopment. The total estimated investment includes lease commissions and excludes tenant improvement overages. The aggregate rentable square feet of these projects is approximately 410,000 square feet. As of December 31, 2012, these properties were 100% leased. In addition, we continued the redevelopment of one of our properties which will have a total estimated investment of approximately $180.0 million at completion. We also had one redevelopment project in lease-up with a total estimated investment of approximately $19.5 million at completion (see "—Factors that May Influence Future Operations - Redevelopment Projects" for additional information).
Capital Recycling Program - We have continued to utilized our capital recycling program to provide additional capital to fund potential acquisitions, to finance development and redevelopment expenditures, to potentially repay long-term debt and for other general corporate purposes. Our general strategy is to target the disposition of mature properties or those that have limited upside for us and redeploy some or all of the capital into acquisitions where we can add

additional value to generate higher returns (see "—Factors that May Influence Future Operations" below for additional information).
In connection with our capital recycling strategy, during 2012, we completed the sale of seven office properties and our entire industrial portfolio, which was comprised of 39 industrial properties, with a combined 3,975,665 rentable square feet for a total gross sales price of approximately $500.3 million at a net gain of $259.2 million. The dispositions were structured to qualify as like-kind exchanges under Section 1031 of the Code ("Section 1031 Exchanges").
Financings - In addition to obtaining funding from our capital recycling program, we successfully completed a variety of financing and capital raising activities to fund our continued growth (see "— Liquidity and Capital Resources of the Operating Partnership" below for additional information).

Critical Accounting Policies

The preparation of financial statements in conformity with GAAP requires us to make estimates, assumptions, and judgments that affect the reported amounts of assets, liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses for the reporting periods. Certain accounting policies are considered to be critical accounting policies. Critical accounting policies are those policies that require our management team to make significant estimates and/or assumptions about matters that are uncertain at the time the estimates and/or assumptions are made or where we are required to make significant judgments and assumptions with respect to the practical application of accounting principles in our business operations. Critical accounting policies are by definition those policies that are material to our financial statements and for which the impact of changes in estimates, assumptions, and judgments could have a material impact to our financial statements.

The following critical accounting policies discussion reflects what we believe are the most significant estimates, assumptions, and judgments used in the preparation of our consolidated financial statements. This discussion of our critical accounting policies is intended to supplement the description of our accounting policies in the footnotes to our consolidated financial statements and to provide additional insight into the information used by management when evaluating significant estimates, assumptions, and judgments. For further discussion of our significant accounting policies, see Note 2 to the consolidated financial statements included in this report.

Rental Revenue Recognition

Rental revenue is our principal source of revenue. The timing of when we commence rental revenue recognition depends largely on our conclusion as to whether we are or the tenant is the owner for accounting purposes of the tenant improvements at the leased property. When we conclude that we are the owner of tenant improvements for accounting purposes, we record the cost to construct the tenant improvements as an asset, and we commence rental revenue recognition when the tenant takes possession of or controls the finished space, which is typically when such tenant improvements are substantially complete.

The determination of whether we are or the tenant is the owner of the tenant improvements for accounting purposes is subject to significant judgment. In making that determination, we consider numerous factors and perform a detailed evaluation of each individual lease. No one factor is determinative in reaching a conclusion. The factors we evaluate include but are not limited to the following:

- whether the lease agreement requires landlord approval of how the tenant improvement allowance is spent prior to installation of the tenant improvements;
- whether the lease agreement requires the tenant to provide evidence to the landlord supporting the cost and what the tenant improvement allowance was spent on prior to payment by the landlord for such tenant improvements;
- whether the tenant improvements are unique to the tenant or reusable by other tenants;
- whether the tenant is permitted to alter or remove the tenant improvements without the consent of the landlord or without compensating the landlord for any lost utility or diminution in fair value; and
- whether the ownership of the tenant improvements remains with the landlord or remains with the tenant at the end of the lease term.

In addition, we also record the cost of certain tenant improvements paid for or reimbursed by tenants when we conclude that we are the owner of such tenant improvements using the factors discussed above. For these tenant-funded tenant improvements, we record the amount funded or reimbursed by tenants as deferred revenue, which is amortized and recognized as rental revenue over the term of the related lease beginning upon substantial completion of the leased premises. During the years ended December 31, 2012, 2011, and 2010, we capitalized $24.0

million, $4.3 million, and $5.4 million, respectively, of tenant-funded tenant improvements. Leases at our development and redevelopment properties generally have higher tenant-funded tenant improvements and we expect the trend to continue to increase as our development and redevelopment activities increase. For those periods, we also recognized $9.1 million, $9.3 million, and $9.7 million, respectively, of noncash rental revenue related to the amortization of deferred revenue recorded in connection with tenant-funded tenant improvements.

When we conclude that we are not the owner and the tenant is the owner of tenant improvements for accounting purposes, we record our contribution towards those improvements as a lease incentive, which is amortized as a reduction to rental revenue on a straight-line basis over the term of the related lease, and rental revenue recognition begins when the tenant takes possession of or controls the space.

Our determination as to whether we are or the tenant is the owner of tenant improvements for accounting purposes is made on a lease-by-lease basis and has a significant impact on the amount of noncash rental revenue that we record related to the amortization of deferred revenue for tenant-funded tenant improvements, and can also have a significant effect on the timing of our overall revenue recognition.

Tenant Reimbursement Revenue

Reimbursements from tenants consist of amounts due from tenants for common area maintenance, real estate taxes, and other recoverable costs, including capital expenditures. Calculating tenant reimbursement revenue requires an in-depth analysis of the complex terms of each underlying lease. Examples of judgments and estimates used when determining the amounts recoverable include:

- estimating the final expenses, net of accruals, that are recoverable;
- estimating the fixed and variable components of operating expenses for each building;
- conforming recoverable expense pools to those used in establishing the base year or base allowance for the applicable underlying lease; and
- concluding whether an expense or capital expenditure is recoverable pursuant to the terms of the underlying lease.

During the year, we accrue estimated tenant reimbursement revenue in the period in which the tenant reimbursable costs are incurred based on our best estimate of the amounts to be recovered. Throughout the year, we perform analyses to properly match tenant reimbursement revenue with reimbursable costs incurred to date. Additionally, during the fourth quarter of each year, we perform preliminary reconciliations and accrue additional tenant reimbursement revenue or refunds. Subsequent to year end, we perform final detailed reconciliations and analyses on a lease-by-lease basis and bill or refund each tenant for any cumulative annual adjustments in the first and second quarters of each year for the previous year’s activity. Our historical experience for the years ended December 31, 2012, 2011, and 2010 has been that our final reconciliation and billing process resulted in final amounts that approximated the total annual tenant reimbursement revenues recognized.

Allowances for Uncollectible Current Tenant Receivables and Deferred Rent Receivables

Tenant receivables and deferred rent receivables are carried net of the allowances for uncollectible current tenant receivables and deferred rent receivables. Current tenant receivables consist primarily of amounts due for contractual lease payments and reimbursements of common area maintenance expenses, property taxes, and other costs recoverable from tenants. Deferred rent receivables represent the amount by which the cumulative straight-line rental revenue recorded to date exceeds cash rents billed to date under the lease agreement. As of December 31, 2012 and 2011, current receivables were carried net of an allowance for uncollectible amount of $2.6 million for each period and deferred rent receivables were carried net of an allowance for uncollectible accounts of $2.6 million and $3.4 million, respectively.

Management’s determination of the adequacy of the allowance for uncollectible current tenant receivables and the allowance for deferred rent receivables is performed using a methodology that incorporates a specific identification analysis and an aging analysis and includes an overall evaluation of our historical loss trends and the current economic and business environment. This determination requires significant judgment and estimates about matters that are uncertain at the time the estimates are made, including the creditworthiness of specific tenants, specific industry trends and conditions, and general economic trends and conditions. Since these factors are beyond our control, actual results can differ from our estimates, and such differences could be material.

With respect to the allowance for uncollectible tenant receivables, the specific identification methodology analysis relies on factors such as the age and nature of the receivables, the payment history and financial condition of the tenant, our assessment of the tenant’s ability to meet its lease obligations, and the status of negotiations of any disputes with the tenant. With respect to the allowance for deferred rent receivables, given the longer-term nature of these receivables, the specific identification methodology analysis evaluates each of our significant tenants and any tenants on our internal watchlist and relies on factors such as each tenant’s financial condition and its ability to meet its lease obligations. We evaluate our reserve levels quarterly based on changes in the financial condition of tenants and our assessment of the tenant's ability to meet its lease obligations, overall economic conditions, and the current business environment.

For the years ended December 31, 2012, 2011, and 2010, we recorded a total provision for bad debts for both current tenant receivables and deferred rent receivables of approximately (0.0)%, 0.2%, and (0.4)%, respectively, of rental revenue. The negative provision for the year ended December 31, 2010 reflects the reversal of approximately $1.0 million of a provision for bad debts recorded in prior years against outstanding receivables from a former tenant due to the settlement of outstanding litigation with the former tenant in 2010. Excluding the $1.0 million reversal of the provision in 2010, our historical experience has been that actual write-offs of current tenant receivables and deferred rent receivables has approximated the provision for bad debts recorded for the years ended December 31, 2012, 2011, and 2010. In the event our estimates were not accurate and we had to change our allowances by 1% of recurring revenue, the potential impact to our net income available to common stockholders would be approximately $4.0 million, $3.6 million, and $3.0 million for the years ended December 31, 2012, 2011, and 2010, respectively.

Acquisitions

We record the acquired tangible and intangible assets and assumed liabilities of acquisitions of all operating properties and those development and redevelopment opportunities that meet the accounting criteria to be accounted for as business combinations at fair value at the acquisition date. We assess and consider fair value based on estimated cash flow projections that utilize available market information and discount and/or capitalization rates that we deem appropriate. Estimates of future cash flows are based on a number of factors including historical operating results, known and anticipated trends, and market and economic conditions. The acquired assets and assumed liabilities for an operating property acquisition generally include but are not limited to: land, buildings and improvements, construction in progress and identified tangible and intangible assets and liabilities associated with in-place leases, including tenant improvements, leasing costs, value of above-market and below-market operating leases and ground leases, acquired in-place lease values and tenant relationships, if any.

The fair value of land is derived from comparable sales of land within the same submarket and/or region. The fair value of buildings and improvements, tenant improvements, and leasing costs are based upon current market replacement costs and other relevant market rate information.

The fair value of the above-market or below-market component of an acquired in-place operating lease is based upon the present value (calculated using a market discount rate) of the difference between (i) the contractual rents to be paid pursuant to the lease over its remaining non-cancellable lease term and (ii) management's estimate of the rents that would be paid using fair market rental rates and rent escalations at the date of acquisition measured over the remaining non-cancellable term of the lease for above-market operating leases and the initial non-cancellable term plus the term of any below-market fixed rate renewal options, if applicable, for below-market operating leases. The amounts recorded for above-market operating leases are included in deferred leasing costs and acquisition-related intangibles, net on the balance sheet and are amortized on a straight-line basis as a reduction of rental income over the remaining term of the applicable leases. The amounts recorded for below-market operating leases are included in deferred revenue and acquisition-related liabilities, net on the balance sheet and are amortized on a straight-line basis as an increase to rental income over the remaining term of the applicable leases plus the term of any below-market fixed rate renewal options, if applicable. Our below-market operating leases generally do not include fixed rate or below-market renewal options.

The fair value of acquired in-place leases is derived based on management's assessment of lost revenue and costs incurred for the period required to lease the “assumed vacant” property to the occupancy level when purchased. This fair value is based on a variety of considerations including, but not necessarily limited to: (1) the value associated with avoiding the cost of originating the acquired in-place leases; (2) the value associated with lost revenue related to tenant reimbursable operating costs estimated to be incurred during the assumed lease-up period; and (3) the value associated with lost rental revenue from existing leases during the assumed lease-up period. Factors considered by us in performing these analyses include an estimate of the carrying costs during the expected lease-up periods, current market conditions, and costs to execute similar leases. In estimating carrying costs, we include real estate taxes, insurance and other operating expenses, and estimates of lost rental revenue during the expected lease-up periods based on current market demand at market rates. In estimating costs to execute similar leases, we consider leasing commissions, legal and other related expenses. The amount recorded for acquired in-place leases is included in deferred leasing costs and acquisition-related intangibles, net on the balance sheet and amortized as an increase to depreciation and amortization expense over the remaining term of the applicable leases. If a lease were to be terminated or if termination were determined to be likely prior to its contractual expiration (for example resulting from bankruptcy), amortization of the related unamortized in-place lease intangible would be accelerated.

The determination of the fair value of any debt assumed in connection with a property acquisition is estimated by discounting the future cash flows using interest rates available for the issuance of debt with similar terms and remaining maturities.

The determination of the fair value of the acquired tangible and intangible assets and assumed liabilities of operating property acquisitions requires us to make significant judgments and assumptions about the numerous inputs discussed above. The use of different assumptions in these fair value calculations could significantly affect the reported amounts of the allocation of our acquisition related assets and liabilities and the related amortization and depreciation expense recorded for such assets and liabilities. In addition, because the value of above and below market leases are amortized as either a reduction or increase to rental income, respectively, our judgments for these intangibles could have a significant impact on our reported rental revenues and results of operations.

Costs directly associated with all operating property acquisitions and those development and redevelopment acquisitions that meet the accounting criteria to be accounted for as business combinations are expensed as incurred. During the years ended December 31, 2012, 2011, and 2010, we expensed $4.9 million, $4.1 million and $2.2 million of acquisition costs respectively, based on the level of our acquisition activity during those years. Our acquisition expenses are directly related to our acquisition activity and if our acquisition activity was to increase or decrease, so would our acquisition costs. Costs directly associated with development acquisitions accounted for as asset acquisitions are capitalized as part of the cost of the acquisition. During the year ended December 31, 2012, we capitalized $0.7 million of such acquisition costs. We did not capitalize any acquisition costs during the years ended December 31, 2011 and 2010.

Evaluation of Asset Impairment

We evaluate our real estate assets for potential impairment whenever events or changes in circumstances indicate that the carrying amount of a given asset may not be recoverable. We evaluate our real estate assets for impairment on a property-by-property basis. Indicators we use to determine whether an impairment evaluation is necessary include:

- low occupancy levels or forecasted low occupancy levels at a specific property;
- current period operating or cash flow losses combined with a historical pattern or future projection of potential continued operating or cash flow losses at a specific property;
- deterioration in rental rates for a specific property as evidenced by sudden significant rental rate decreases or continuous rental rate decreases over numerous quarters, which could signal a continued decrease in future cash flow for that property;
- deterioration of a given rental submarket as evidenced by significant increases in market vacancy and/or negative absorption rates or continuous increases in market vacancy and/or negative absorption rates over numerous quarters, which could signal a decrease in future cash flow for properties within that submarket;
- significant increases in property sales yields, continuous increases in property sales yields over several quarters, or recent property sales at a loss within a given submarket, each of which could signal a decrease in the market value of properties;
- significant change in strategy or use of a specific property or any other event that could result in a decreased holding period, including classifying a property as held for sale, or significant development delay;
- evidence of material physical damage to the property; and
- default by a significant tenant when any of the other indicators above are present.

When we evaluate for potential impairment our real estate assets to be held and used, we first evaluate whether there are any indicators of impairment. If any impairment indicators are present for a specific real estate asset, we then perform an undiscounted cash flow analysis and compare the net carrying amount of the real estate asset to the real estate asset's estimated undiscounted future cash flow over the anticipated holding period. If the estimated undiscounted future cash flow is less than the net carrying amount of the real estate asset, we perform an impairment loss calculation to determine if the fair value of the real estate asset is less than the net carrying value of the real estate asset. Our impairment loss calculation compares the net carrying amount of the real estate asset to the real estate asset's estimated fair value, which may be based on estimated discounted future cash flow calculations or third-party valuations or appraisals. We recognize an impairment loss if the amount of the asset's net carrying amount exceeds the asset's estimated fair value. If we recognize an impairment loss, the estimated fair value of the asset becomes its new cost basis. For a depreciable long-lived asset, the new cost basis will be depreciated (amortized) over the remaining useful life of that asset.

Our undiscounted cash flow and fair value calculations contain uncertainties because they require management to make assumptions and to apply judgment to estimate future cash flow and property fair values, including selecting the discount or capitalization rate that reflects the risk inherent in future cash flow. Estimating projected cash flow is highly subjective as it requires assumptions related to future rental rates, tenant allowances, operating expenditures, property taxes, capital improvements, and occupancy levels. We are also required to make a number of assumptions relating to future economic and market events and prospective operating trends. Determining the appropriate capitalization rate also requires significant judgment and is typically based on many factors including the prevailing rate for the market or submarket, as well as the quality and location of the properties. Further, capitalization rates can fluctuate resulting from a variety of factors in the overall economy or within regional markets. If the actual net cash flow or actual market capitalization rates significantly differ from our estimates, the impairment evaluation for an individual asset could be materially affected.

Because of the economic and market environment, circumstances indicated that an analysis for potential impairment of certain of our properties was necessary in each of the years ended December 31, 2012, 2011, and 2010. As a result, for each property where such an indicator occurred and/or for properties within a given submarket where such an indicator occurred, we completed an impairment evaluation. After completing this process, we determined that for each of the operating properties evaluated, undiscounted cash flows over the holding period were in excess of carrying value and, therefore, we did not record any impairment losses for these periods. We determined that for each of the properties held for sale, that the sale price less estimated costs to sell exceeded the carrying value and therefore we did not record any impairment losses for these properties.

Cost Capitalization and Depreciation

We capitalize costs associated with development and redevelopment activities, capital improvements, tenant improvements, and leasing activities. For the years ended December 31, 2012, 2011, and 2010 we capitalized $3.1 million, $1.7 million, and $1.6 million respectively, of internal costs to our qualifying redevelopment and development projects.

Amounts capitalized are depreciated or amortized over estimated useful lives determined by management. We depreciate buildings and improvements based on the estimated useful life of the asset, and we amortize tenant improvements and leasing costs over the shorter of the estimated useful life or estimated remaining life of the related lease. All capitalized costs are depreciated or amortized using the straight-line method.

Determining whether expenditures meet the criteria for capitalization and the assignment of depreciable lives requires management to exercise significant judgment. Expenditures that meet one or more of the following criteria generally qualify for capitalization:

- provide benefit in future periods;
- extend the useful life of the asset beyond our original estimates; and
- increase the quality of the asset beyond our original estimates.

Our historical experience has demonstrated that we have not had material write-offs of assets and that our depreciation and amortization estimates have been reasonable and appropriate.

Share-Based Incentive Compensation Accounting

At December 31, 2012, the Company had one share-based incentive compensation plan, the Kilroy Realty 2006 Incentive Award Plan, which is described more fully in Note 12 to the consolidated financial statements. The Executive Compensation Committee determines compensation for our Chief Executive Officer, Chief Operating Officer, Chief Investment Officer and Chief Financial Officer (“the Executive Officers”). Compensation cost for all share-based awards, including options, requires measurement at estimated fair value on the grant date and compensation cost is recognized over the service vesting period, which represents the requisite service period. The grant date fair value for compensation plans that contain market measures are performed using complex pricing valuation models that require the input of assumptions, including judgments to estimate expected stock price volatility, expected life, and forfeiture rate. Specifically, the grant date fair value of market measure-based share-based compensation plans are calculated using a Monte Carlo simulation pricing model and the grant date fair value of stock option grants are calculated using the Black-Scholes valuation model.

For the year ended December 31, 2012 we recorded approximately $3.9 million of compensation expense related to plans that contained market measures and were therefore subject to such valuation models. If the valuation of the grant date fair value for such plans changed by 10%, the potential impact to our net income available to common stockholders would be approximately $0.4 million for the year ended December 31, 2012. There was no compensation expense related to market measure-based plans recorded for the years ended December 31, 2011 and 2010 since our market measure-based share-based compensation plans and options were granted in 2012.

Factors That May Influence Future Results of Operations

Acquisitions. During the year ended December 31, 2012, we acquired 14 office buildings in seven transactions with an aggregate purchase price of approximately $674.0 million and six development and redevelopment opportunity projects in six transactions with an aggregate purchase price of approximately $340.3 million. During the year ended December 31, 2011, we acquired ten office buildings and one redevelopment opportunity project in eight transactions with an aggregate purchase price of approximately $637.8 million (see Note 3 to our consolidated financial statements included in this report for additional information). As of the date of this report, we have completed the acquisition of one additional office building with a purchase price of approximately $170.0 million. We generally finance our acquisitions through proceeds from the issuance of debt and equity securities, borrowings under our revolving revolving credit facility, proceeds from our capital recycling program and the assumption of existing debt.

As a key component of our growth strategy, we continually evaluate acquisition opportunities (including office properties, undeveloped land, and development and redevelopment opportunities) as they arise. As a result, at any point in time we may have one or more potential acquisitions under consideration that are in varying stages of evaluation, negotiation or due diligence review, which may include potential acquisitions under contract. As of the date of the filing of this report, we were also in negotiations to acquire an additional future development opportunity. We cannot provide assurance that we will acquire this property. In the future, we may enter into agreements to acquire other properties, either as wholly-owned properties or through joint ventures, and those agreements typically will be subject to the satisfaction of closing conditions. We cannot provide assurance that we will enter into any agreements to acquire properties, or that the potential acquisitions contemplated by any agreements we may enter into in the future will be completed. Costs associated with acquisitions accounted for as business combinations are expensed as incurred, and we may be unable to complete an acquisition after making a nonrefundable deposit or incurring acquisition–related costs. In addition, acquisitions are subject to various other risks and uncertainties.

Capital Recycling Program. During the year ended December 31, 2012, we disposed of seven office properties and our entire industrial portfolio, which was comprised of 39 Industrial Properties, with a combined 3,975,665 rentable square feet, for a total gross sales price of approximately $500.3 million at a net gain of $259.2 million (see Note 17 to our consolidated financial statements included in this report for more information). In connection with this transaction, the dispositions were structured to qualify as Section 1031 Exchanges. Approximately $228.8 million of the sales proceeds, which were included in restricted cash on the consolidated balance sheets at December 31, 2012, were reinvested into qualifying replacement properties as of the filing date of this report.

As part of our current and ongoing strategy, we continuously evaluate opportunities for the potential disposition of properties and undeveloped land in our portfolio with the intent of recycling the proceeds generated from the disposition of non-strategic properties into capital to fund new operating and development acquisitions, development and redevelopment expenditures, to repay long-term debt and for other general corporate purposes. As part of our capital recycling strategy, we intend, when practical, to enter into Section 1031 Exchanges to defer some or all of the taxable gains, if any, on the sales for federal and state income tax purposes.

The timing of any potential future deposition transactions will depend on market conditions and other factors, including but not limited to our capital needs and our ability to defer some or all of the taxable gains on the sales. We cannot assure you that we will dispose of any additional properties, or that future acquisitions and/or dispositions, if any, will qualify as Section 1031 Exchanges.

Leasing Activity and Changes in Rental Rates. The amount of net rental income generated by our properties depends principally on our ability to maintain the occupancy rates of currently leased space and to lease currently available space, newly developed or redeveloped properties, newly acquired properties with vacant space, and space available from unscheduled lease terminations. The amount of rental income we generate also depends on our ability to maintain or increase rental rates in our submarkets. Negative trends in one or more of these factors could adversely affect our rental income in future periods. The following tables set forth certain information regarding leasing activity for our stabilized portfolio during the year ended December 31, 2012.

Information on Leases Commenced and Executed

For Leases Commenced

	1st & 2nd Generation[1]				2nd Generation[1]				
	Number of Leases[2]		Rentable Square Feet[2]		TI/LC per Sq. Ft.[3]	Changes in Rents[4][6]	Changes in Cash Rents[5]	Retention Rates[7]	Weighted Average Lease Term (in months)
	New	Renewal	New	Renewal					
Year Ended December 31, 2012	86	63	895,345	629,664	$30.02	11.1 %	3.5 %	51.9 %	68

For Leases Executed[8]

	1st & 2nd Generation[1]				2nd Generation[1]			
	Number of Leases[2]		Rentable Square Feet[2]		TI/LC per Sq. Ft.[3]	Changes in Rents[4][6]	Changes in Cash Rents[5]	Weighted Average Lease Term (in months)
	New	Renewal	New	Renewal				
Year Ended December 31, 2012	83	68	998,659	779,959	$36.64	21.3 %	9.7 %	73

(1) First generation leasing includes space where we have made capital expenditures that result in additional revenue generated when the space is re-leased. Second generation leasing includes space where we have made capital expenditures to maintain the current market revenue stream.

(2) Represents leasing activity for leases that commenced or signed during the period, including first and second generation space, net of month-to-month leases. Excludes leasing on new construction.

(3) Amounts exclude tenant-funded tenant improvements.

(4) Calculated as the change between GAAP rents for new/renewed leases and the expiring GAAP rents for the same space. Excludes leases for which the space was vacant longer than one year or vacant when the property was acquired.

(5) Calculated as the change between stated rents for new/renewed leases and the expiring stated rents for the same space. Excludes leases for which the space was vacant longer than one year or vacant when the property was acquired.

(6) Excludes commenced and executed leases of approximately 469,000 and 394,000 rentable square feet, respectively, for the year ended December 31, 2012, for which the space was vacant longer than one year or being leased for the first time. Space vacant for more than one year is excluded from our change in rents calculations to provide a meaningful market comparison.

(7) Calculated as the percentage of space either renewed or expanded into by existing tenants or subtenants at lease expiration.

(8)

During the year, 14 leases totaling approximately 204,000 rentable square feet were signed but had not commenced as of December 31, 2012.

As of December 31, 2012, we believe that the weighted average cash rental rates for our stabilized portfolio, including recently acquired operating properties, are approximately at the current average market rental rates, although individual properties within any particular submarket presently may be leased either above, below, or at the current market rates within that submarket, and the average rental rates for individual submarkets may be above, below, or at the average cash rental rate of our portfolio.

In general, market rental rates increased in the majority of our submarkets during 2012. Our rental rates and occupancy are impacted by general economic conditions, including the pace of regional economic growth and access to capital. Therefore, we cannot give any assurance that leases will be renewed or that available space will be re-leased at rental rates equal to or above the current market rates. Additionally, decreased demand and other negative trends or unforeseeable events that impair our ability to timely renew or re-lease space could have further negative effects on our future financial condition, results of operations, and cash flows.

Scheduled Lease Expirations. The following table sets forth certain information regarding our lease expirations for our stabilized portfolio for future periods as of December 31, 2012:

Lease Expirations[1]

Year of Lease Expiration	Number of Expiring Leases	Total Square Feet	% of Total Leased Sq. Ft.		Annualized Base Rent [1]	% of Total Annualized Base Rent [1]		Annualized Base Rent per Sq. Ft. [1]
2013	94	855,902	7.1	%	$22,524	6.0	%	$26.32
2014	121	1,250,019	10.4	%	36,098	9.6	%	28.88
2015	151	2,124,976	17.7	%	65,432	17.4	%	30.79
2016	74	808,217	6.7	%	21,119	5.6	%	26.13
2017	99	1,951,623	16.2	%	58,162	15.4	%	29.80
2018	52	1,281,765	10.6	%	49,569	13.1	%	38.67
Total[2]	591	8,272,502	68.7	%	$252,904	67.1	%	$30.57

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(1) Annualized base rent includes the impact of straight-lining rent escalations and the amortization of free rent periods and excludes the impact of the following: amortization of deferred revenue related tenant-funded tenant improvements, amortization of above/below market rents, amortization for lease incentives due under existing leases, and expense reimbursement revenue. Additionally, the underlying leases contain various expense structures including full service gross, modified gross and triple net. Amounts represent percentage of total portfolio annualized contractual base rental revenue. For additional information on tenant improvement and leasing commission costs incurred by the Company for the current reporting period, please see further discussion under the caption "Information on Leases Commenced and Executed."

(2) The information presented for all lease expiration activity reflects leasing activity through December 31, 2012 for our stabilized portfolio. For leases that have been renewed early or space that has been re-leased to a new tenant, the expiration date and annualized base rent information presented takes into consideration the renewed or re-leased lease terms. Excludes space leased under month-to-month leases, vacant space, and lease renewal options not executed as of December 31, 2012.

In addition to the 1.0 million rentable square feet, or 7.2%, of currently available space in our stabilized portfolio, leases representing approximately 7.1% and 10.4% of the occupied square footage of our stabilized portfolio are scheduled to expire during the remainder of 2013 and in 2014, respectively. The leases scheduled to expire in 2013 and 2014 represent approximately 2.1 million rentable square feet of office space, or 15.6% of our total annualized base rental revenue. We believe that the weighted average cash rental rates are approximately 5% under the current average quoted market rates for leases scheduled to expire during 2013 and 2014, although individual properties within any particular submarket presently may be leased either above, below, or at the current quoted market rates within that submarket, and the average rental rates for individual submarkets may be above, below, or at the average cash rental rate of our overall portfolio. Our ability to re-lease available space depends upon both general market conditions and the market conditions in the specific regions in which individual properties are located.

Redevelopment Projects

We believe that a portion of our potential long-term future growth will continue to come from redevelopment opportunities both through acquired properties and within our existing portfolio. Redevelopment opportunities are those projects in which we spend significant development and construction costs on existing or acquired buildings pursuant to a formal plan, the intended result of which is a higher economic return on the property. During the fourth quarter ended December 31, 2012, we completed construction of the following two redevelopment projects.

- 2260 E. Imperial Highway, El Segundo, submarket of Los Angeles, on which we commenced redevelopment in the third quarter of 2010. The redevelopment project, encompassing approximately 299,000 rentable square feet, has a total estimated investment of approximately $60.4 million, including the $9.1 million net carrying value of the project at the commencement of redevelopment. The building was 100% pre-leased to DIRECTV, our largest tenant.

DIRECTV began paying cash rent on the entire building in December 2012.

- 5010 Wateridge Vista Drive, Sorrento Mesa, submarket of San Diego, on which we commenced redevelopment in the third quarter of 2011. The redevelopment project encompasses approximately 111,000 rentable square feet. As part of the redevelopment, we incorporated one of our undeveloped land parcels. The redevelopment project has a total estimated investment of approximately $37.4 million, including the $22.2 million net carrying value of the project at the commencement of redevelopment. The building was 100% pre-leased to TD Ameritrade and rent commenced in October 2012.

As of December 31, 2012, we had one redevelopment project in lease-up and another redevelopment project under construction.

- 3880 Airport Way, Long Beach, submarket of Los Angeles, on which we commenced redevelopment in the third quarter of 2011. This lease-up property, encompassing approximately 98,000 rentable square feet, was 50% leased prior to the commencement of redevelopment which was done in two phases. Redevelopment on the first half, which was leased, was completed during the second quarter of 2012, and redevelopment on the second half was completed in the fourth quarter of 2012. The lease-up project will have a total estimated investment of approximately $19.5 million upon completion, including the $6.3 million net carrying value of the project at the commencement of redevelopment.

- 360 Third Street, South of Market Area, submarket of San Francisco, on which we commenced redevelopment in the fourth quarter of 2011. The redevelopment project, which encompasses approximately 410,000 rentable square feet, will have a total estimated investment of approximately $180.0 million at completion, including the $88.5 million net carrying value of the project at the commencement of redevelopment plus $27.5 million that we expect to pay in the second quarter of 2013 to acquire the land that is currently subject to a ground lease. Construction is currently expected to be completed in the first quarter of 2014. As of December 31, 2012, the building was approximately 75% leased and 26% occupied.

In-Process and Future Development Pipeline

We believe that a portion of our long-term future growth will also come from the completion of our under construction and in-process projects as well as executing on our future development pipeline, subject to market conditions. During 2012, we increased our focus on value-add and highly accretive development opportunities and expanded our future development pipeline through targeted acquisitions of development opportunities on the West Coast.

We have a proactive planning process by which we continually evaluate the size, timing, costs and scope of our development program and, as necessary, scale activity to reflect the economic conditions and the real estate fundamentals that exist in our strategic submarkets. We expect to proceed in our development program with discipline and will be pursuing opportunities with attractive economic returns, in locations with transportation and retail amenities and in markets with strong fundamentals and visible demand. We plan to develop in phases as appropriate and we strongly favor starting projects that are pre-leased.

As of the date of this report, our near-term development pipeline consisted of the following four projects under construction and two projects expected to commence in 2013.

- 690 E. Middlefield Road, Mountain View, California, which we acquired in May 2012. We acquired the project for $84.0 million, comprised of a cash purchase price of $74.5 million plus $9.5 million of assumed leasing commissions and other net accrued liabilities. The development project, which is 100% pre-leased to Synopsis, Inc., has a total estimated investment of approximately $195.7 million and is expected to encompass approximately 341,000 rentable square feet upon completion. Construction is currently in process and is expected to be completed in the first quarter of 2015.

- 331 Fairchild Drive, Mountain View, California, which we acquired in December 2012 and is 100% pre-leased. We acquired the project for $18.9 million plus $2.9 million of development costs to be reimbursed to the seller and are planning to develop an approximately 88,000 square foot building. The development project has a total estimated investment of approximately $45.2 million. Construction is currently in process and is expected to be completed in the fourth quarter of 2013.

- 350 Mission Street, South of Market Financial District, San Francisco, California, which we acquired in October 2012 for approximately $52.0 million. Shortly after acquisition, we pre-leased the entire project to salesforce.com and are currently planning to develop an approximately 400,000 square foot, 27 story office tower that adapts our open-plan workspace concepts to a high-rise office environment. The property is expected to be LEED platinum certified and the first ground up development property in the city to receive this designation. The development project has a total estimated investment of approximately $254.7 million. We are currently pursuing entitlements to increase this project to a 30-story office tower, which would increase the estimated rentable square feet and total estimated investment. Construction is currently in process and is expected to be completed in the first quarter of 2015.

- 555-599 N. Mathilda Avenue, Sunnyvale, California, which we acquired in December 2012 for approximately $137.6 million. The project, which is comprised of one operating property and a future development site, is 100% pre-leased. Our plan at this project is to continue operating the existing building and develop an approximately 587,000 square foot office complex for LinkedIn, the tenant in the current existing building. The development project has a total estimated investment of approximately $313.2 million. Construction is currently in progress and is expected to be completed in the third quarter of 2014.

- 333 Brannan Street, South of Market Area, San Francisco, California, which we acquired in July 2012 for approximately $18.5 million. We currently expect to develop an approximately 170,000 rentable square foot office building on this site that will include all the features, amenities and systems that tech and media tenants need to accommodate their increased densities for a total estimated investment of approximately $85.0 million. We currently expect to begin construction in the fourth quarter of 2013.

• Columbia Square, in Hollywood, California, which we acquired in September 2012 for approximately $65.0 million. This project is a historic media campus located in the heart of Hollywood, two blocks from the corner of Sunset Boulevard and Vine Street. The site is fully entitled for the development of an 875,000 rentable square foot office, retail and multi-family mixed use project under a 15-year development agreement that includes three existing buildings and which we plan to develop in phases. We intend to redevelop the three existing buildings, which encompass approximately 100,000 rentable square feet, and to develop more than 500,000 square feet of office, retail and residential space. We currently expect to invest an additional $246.0 million for a total estimated investment of approximately $315.0 million. Our plan is to create a mixed-use campus that preserves the historical character while establishing a new center for many entertainment and media companies. We expect to commence redevelopment of the three historic buildings, and initial construction of the office component in early to mid-2013 with completion of phase one targeted for 2015.

As of the date of this report, we were also in negotiations to acquire an additional future development opportunity. We cannot provide assurance that we will acquire this project. In the future, we may also enter into agreements to acquire other development or redevelopment opportunities, either as wholly-owned properties or through joint ventures and those agreements typically will be subject to the satisfaction of closing conditions. In addition, as of December 31, 2012, we had additional undeveloped land holdings, located primarily in various submarkets in San Diego County with an aggregate cost basis of approximately $284.1 million.

This increase in our development and redevelopment activities, primarily as a result of acquisitions completed in the fourth quarter of 2012, will cause an increase in the average development asset balances qualifying for interest and other carry cost capitalization in future periods.

Incentive Compensation. Our Executive Compensation Committee determines compensation, including equity and cash incentive programs, for our executive officers in accordance with the terms and conditions of applicable agreements and incentive award programs. Incentive compensation for our executive officers for 2012 was structured to allow the Executive Compensation Committee to evaluate a variety of key factors and metrics at the end of the year and make a determination of incentive compensation for executive officers based on the Company's and management's overall performance. As a result, accrued incentive compensation and compensation expense for future incentive compensation awards could be affected by our operating and development performance, financial results, total shareholder return, market conditions and other performance conditions. Consequently, we cannot predict the amounts that will be recorded in future periods related to such incentive compensation.

Share-Based Compensation. As of December 31, 2012, there was $25.9 million of total unrecognized compensation cost related to outstanding nonvested shares of restricted common stock, RSUs and stock options issued under share-based compensation arrangements. Those costs are expected to be recognized over a weighted-average period of 2.6 years. Additional unrecognized compensation cost of $7.7 million related to 157,744 nonvested RSUs issued under share-based compensation arrangements subsequent to December 31, 2012 is expected to be recognized over a period of 5.0 years. Share-based compensation expense for potential future awards could be affected by our operating and development performance, financial results, total shareholder return and market conditions. Consequently, we cannot predict the amounts that will be recorded in future periods for such share-based awards. See Note 12 to our consolidated financial statements for additional information regarding our share-based incentive compensation plan.

Stabilized Portfolio Information

As of December 31, 2012, our stabilized portfolio was comprised of 114 office properties encompassing an aggregate of approximately 13.2 million rentable square feet. Our stabilized portfolio includes all of our properties with the exception of undeveloped land, development and redevelopment properties currently under construction or committed for construction, “lease-up” properties and properties held-for-sale. We define lease-up properties as properties recently developed or redeveloped that have not yet reached 95% occupancy and are within one year following cessation of major construction activities. We define redevelopment properties as those projects for which we expect to spend significant development and construction costs on existing or acquired buildings pursuant to a formal plan, the intended result of which is a higher economic return on the property. Our stabilized portfolio also excludes our future development pipeline, which is comprised of nine potential development sites, representing 118.5 gross acres of undeveloped land.

At December 31, 2012, our stabilized portfolio excluded one "lease-up" property, one redevelopment and four development properties currently under construction and one property moved from the stabilized portfolio to the development pipeline during the fourth quarter of 2012.

The following table reconciles the changes in the rentable square feet in our stabilized portfolio of operating properties from December 31, 2011 to December 31, 2012:

	Office Properties		Industrial Properties		Total	
	Number of Buildings	Rentable Square Feet	Number of Buildings	Rentable Square Feet	Number of Buildings	Rentable Square Feet
Total as of December 31, 2011	104	11,421,112	39	3,413,354	143	14,834,466
Acquisitions[1]	14	1,759,603			14	1,759,603
Completed redevelopment properties placed in-service	2	410,046			2	410,046
Property moved to the development pipeline	(1)	(45,195)			(1)	(45,195)
Dispositions	(5)	(308,635)	(39)	(3,413,354)	(44)	(3,721,989)
Remeasurement		12,849				12,849
Total as of December 31, 2012	114	13,249,780	—	—	114	13,249,780

(1) Excludes redevelopment and development property acquisitions.

Occupancy Information

The following table sets forth certain information regarding our stabilized portfolio:

Stabilized Portfolio Occupancy

Region	Number of Buildings	Rentable Square Feet	Occupancy at[1] 12/31/2012	12/31/2011	12/31/2010
Los Angeles and Ventura Counties	27	3,487,741	94.0 %	83.5 %	89.3 %
San Diego County	59	5,250,413	90.7	92.5	86.4
Orange County	4	497,393	92.0	93.4	93.1
San Francisco Bay Area	14	2,286,994	95.5	93.3	84.3
Greater Seattle	10	1,727,239	93.3	89.9	100.0
Total Stabilized Portfolio	114	13,249,780	92.8	90.1	87.5

	Average Occupancy 2012	2011
Stabilized Portfolio[1]	91.3%	91.3%
Same Store Portfolio[2]	91.5%	91.9%

(1) Occupancy percentages reported are based on our stabilized office portfolio as of the end of the period presented.

(2) Occupancy percentages reported are based on office properties owned and stabilized as of January 1, 2011 and still owned and stabilized as of December 31, 2012. See discussion under "Results of Operations" for additional information.

Current Regional Information

We have generally seen rental rates stabilize and start to improve in many of our submarkets. We have also seen vacancy rates in many of our submarkets are starting to decrease.

Los Angeles and Ventura Counties. Our Los Angeles and Ventura Counties stabilized portfolio of 3.5 million rentable square feet was 94.0% occupied with approximately 210,100 available rentable square feet as of December 31, 2012 compared to 83.5% occupied with approximately 491,300 available rentable square feet as of December 31, 2011. During 2012, we completed the sale of four buildings encompassing approximately 265,400 rentable square feet located in Ventura County that were included in this portfolio as of December 31, 2011. Excluding these four buildings, the Los Angeles and Ventura Counties stabilized portfolio would have been 90.2% as of December 31, 2011. The increase in occupancy, excluding the impact of the disposed properties, is primarily attributable to one redevelopment property encompassing approximately 299,000 rentable square feet that was added to the stabilized portfolio upon completion and was 100% occupied as of December 31, 2012. In addition, occupancy increased due to the acquisition of two office buildings during the year ended December 31, 2012 encompassing approximately 473,000 rentable square feet that were 88.9% occupied as of December 31, 2012.

As of December 31, 2012, leases representing an aggregate of approximately 333,700 and 353,500 rentable square feet are scheduled to expire during 2013 and in 2014, respectively, in this region. The aggregate rentable square feet under the leases scheduled to expire in this region during 2013 and in 2014 represents approximately 5.7% of our occupied rentable square feet and 5.4% of our annualized base rental revenues in our total stabilized portfolio.

San Diego County. Our San Diego County stabilized portfolio of 5.3 million rentable square feet was 90.7% occupied with approximately 486,800 available rentable square feet as of December 31, 2012 compared to 92.5% occupied with approximately 391,100 available rentable square feet as of December 31, 2011. The decrease in occupancy is primarily attributable to four leases that expired during the year ended December 31, 2012 offset by one office building placed in service in the fourth quarter of 2012 encompassing approximately 111,000 rentable square feet that was 100% occupied as of December 31, 2012. As of December 31, 2012, we have leased approximately 131,000 rentable square feet in this region that was vacant at December 31, 2012 to five tenants. The new leases are scheduled to commence during various quarters in 2013.

As of December 31, 2012, leases representing an aggregate of approximately 301,400 and 480,800 rentable square feet are scheduled to expire during 2013 and 2014, respectively, in this region. The aggregate rentable square feet under leases scheduled to expire in this region in 2013 and 2014 represents approximately 6.5% of our occupied rentable square feet and 4.5% of our annualized base rental revenues in our total stabilized portfolio occupied as of December 31, 2012.

Orange County. Our Orange County stabilized portfolio of approximately 497,400 rentable square feet was 92.0% occupied with approximately 39,700 available rentable square feet as of December 31, 2012, compared to 93.4% occupied with approximately 35,500 available rentable square feet as of December 31, 2011.

As of December 31, 2012, leases representing an aggregate of approximately 55,000 and 60,400 rentable square feet are scheduled to expire during 2013 and 2014, respectively, in this region. The aggregate rentable square feet under leases scheduled to expire in 2013 and 2014 represents approximately 1.0% of our occupied rentable square feet and 0.8% of our annualized base rental revenues in our total stabilized portfolio as of December 31, 2012.

San Francisco Bay Area. As of December 31, 2012, our San Francisco Bay Area stabilized portfolio of 2.3 million rentable square feet was 95.5% occupied with approximately 102,800 available rentable square feet, compared to 1.8 million rentable square feet that was 93.3% occupied with approximately 121,900 available rentable square feet as of December 31, 2011. The increase in occupancy is primarily attributable to 2 new leases that commenced during the year ended December 31, 2012, offset by the acquisition of eight office buildings during the year ended December 31, 2012 encompassing approximately 449,900 rentable square feet that were 87.3% occupied as of December 31, 2012. We have leased 9,500 rentable square feet in this region that was vacant at December 31, 2012 to three tenants, with new leases scheduled to commence in the first quarter of 2013.

As of December 31, 2012, leases representing an aggregate of approximately 128,400 and 247,200 rentable square feet are scheduled to expire during 2013 and 2014, respectively, in this region. The aggregate rentable square feet under leases scheduled to expire in this region during 2013 and 2014 represents approximately 3.2% of our occupied rentable square feet and 3.6% of our annualized base rental revenues in our total stabilized portfolio as of December 31, 2012.

Greater Seattle. As of December 31, 2012, our Greater Seattle stabilized portfolio of 1.7 million rentable square feet was 93.3% occupied with approximately 116,100 available rentable square feet, compared to 89.9% occupied with approximately 90,300 available rentable square feet as of December 31, 2011. The increase in occupancy is primarily attributable to the acquisition of four office buildings during the year ended December 31, 2012 encompassing approximately 836,700 rentable square feet that were 94.6% occupied as of December 31, 2012. We have leased 37,800 rentable square feet in this region that was vacant at December 31, 2012 to two tenants, with new leases scheduled to commence in the first half of 2013.

As of December 31, 2012, leases representing an aggregate of approximately 37,400 and 108,100 rentable square feet are scheduled to expire during 2013 and 2014, respectively. The aggregate rentable square feet under leases scheduled to expire in this region during 2013 and 2014 represents approximately 1.2% of our occupied rentable square feet and

1.2% of our annualized base rental revenues in our total stabilized portfolio as of December 31, 2012.

Results of Operations

Year Ended December 31, 2012 Compared to Year Ended December 31, 2011

Net Operating Income

Management internally evaluates the operating performance and financial results of our stabilized portfolio based on Net Operating Income. We define "Net Operating Income" as operating revenues (rental income, tenant reimbursements, and other property income) less operating expenses (property expenses, real estate taxes, provision for bad debts, and ground leases).

Net Operating Income is considered by management to be an important and appropriate supplemental performance measure to net income (loss) because we believe it helps both investors and management to understand the core operations of our properties excluding corporate and financing-related costs and non-cash depreciation and amortization. Net Operating Income is an unlevered operating performance metric of our properties and allows for a useful comparison of the operating performance of individual assets or groups of assets. This measure thereby provides an operating perspective not immediately apparent from GAAP income (loss) from operations or net income (loss). In addition, Net Operating Income is considered by many in the real estate industry to be a useful starting point for determining the value of a real estate asset or group of assets. Other real estate companies may use different methodologies for calculating Net Operating Income, and accordingly, our presentation of Net Operating Income may not be comparable to other real estate companies. Because of the exclusion of the items shown in the reconciliation below, Net Operating Income should only be used as a supplemental measure of our financial performance and not as an alternative to GAAP income (loss) from operations or net income (loss).

Management further evaluates Net Operating Income by evaluating the performance from the following property groups:

- Same Store Properties - which includes the results of all of the office properties that were owned and included in our stabilized portfolio as of January 1, 2011 and still owned and included in the stabilized portfolio as of December 31, 2012;
- Acquisition Properties - which includes the results, from the dates of acquisition through the periods presented, for the ten office buildings we acquired during 2011 and the fourteen office buildings we acquired during 2012;
- Stabilized Redevelopment Properties - which includes the results generated by two office buildings that were moved into the stabilized portfolio upon completion of redevelopment in the fourth quarter of 2012. Both office buildings were moved into redevelopment during 2011, thus the prior year results reflect operating results for the properties prior to redevelopment.
- Other Properties - which includes the results of properties not included in our stabilized portfolio. These properties consist of one office building in "lease-up", one redevelopment project under construction and one office building that was moved from the stabilized portfolio during 2012 to development since the property is being repositioned.

The following table sets forth certain information regarding the property groups within our stabilized portfolio as of December 31, 2012:

Group	# of Buildings	Rentable Square Feet
Same Store Properties	88	9,506,919
Acquisition Properties	24	3,332,815
Stabilized Redevelopment Properties	2	410,046
Total Stabilized Portfolio	114	13,249,780

The following table reconciles our Net Operating Income, as defined, to our net income for the years ended December 31, 2012 and 2011.

	Year Ended December 31, 2012	2011	Dollar Change	Percentage Change
	($ in thousands)			
Reconciliation to Net Income:				
Net Operating Income, as defined	$287,755	$238,615	$49,140	20.6 %
Unallocated (expense) income:				
General and administrative expenses	(36,188)	(28,148)	(8,040)	28.6
Acquisition-related expenses	(4,937)	(4,053)	(884)	21.8
Depreciation and amortization	(162,917)	(124,928)	(37,989)	30.4
Interest income and other net investment gains	848	571	277	48.5
Interest expense	(79,114)	(85,785)	6,671	(7.8)
Income (loss) from continuing operations	5,447	(3,728)	9,175	(246.1)%
Income from discontinued operations	12,409	19,630	(7,221)	(36.8)%
Net gain on dispositions of discontinued operations	259,245	51,587	207,658	402.5 %
Net income	$277,101	$67,489	$209,612	310.6 %

The following tables summarize the Net Operating Income (Loss), as defined, for our total portfolio for the years ended December 31, 2012 and 2011.

	2012 Same Store	Acquisition Properties	Stabilized Redevelopment	Other	Total	2011 Same Store	Acquisition Properties	Stabilized Redevelopment	Other	Total
	(in thousands)					(in thousands)				
Operating revenues:										
Rental income	$285,043	$78,555	$ 957	$4,961	$369,516	$281,180	$24,403	$ —	$1,535	$307,118
Tenant reimbursements	19,193	12,626	173	317	32,309	19,262	4,462	59	194	23,977
Other property income	2,713	365	—	9	3,087	6,031	471	32	—	6,534
Total	306,949	91,546	1,130	5,287	404,912	306,473	29,336	91	1,729	337,629
Property and related expenses:										
Property expenses	60,501	17,051	542	1,263	79,357	59,454	5,977	534	856	66,821
Real estate taxes	25,303	7,567	89	1,520	34,479	25,747	2,255	143	1,488	29,633
Provision for bad debts	153	—	—	—	153	781	—	—	—	781
Ground leases	897	1,512	4	755	3,168	1,137	446	13	183	1,779
Total	86,854	26,130	635	3,538	117,157	87,119	8,678	690	2,527	99,014
Net Operating Income (Loss), as defined	$220,095	$65,416	$ 495	$1,749	$287,755	$219,354	$20,658	$ (599)	$(798)	$238,615

	Year Ended December 31, 2012 as compared to the Year Ended December 31, 2011									
	Same Store		Acquisition Properties		Stabilized Redevelopment		Other		Total Portfolio	
	Dollar Change	% Change	Dollar Change	% Change	Dollar Change	% Change	Dollar Change	% Change	Dollar Change	% Change
					($ in thousands)					
Operating revenues:										
Rental income	$3,863	1.4 %	$54,152	221.9 %	$957	100.0 %	$3,426	223.2 %	$62,398	20.3 %
Tenant reimbursements	(69)	(0.4)	8,164	183.0	114	193.2 %	123	63.4 %	8,332	34.7
Other property income	(3,318)	(55.0)	(106)	(22.5)	(32)	(100.0)%	9	100.0 %	(3,447)	(52.8)
Total	476	0.2	62,210	212.1	1,039	1,141.8 %	3,558	205.8 %	67,283	19.9
Property and related expenses:										
Property expenses	1,047	1.8	11,074	185.3	8	1.5 %	407	47.5 %	12,536	18.8
Real estate taxes	(444)	(1.7)	5,312	235.6	(54)	(37.8)%	32	2.2 %	4,846	16.4
Provision for bad debts	(628)	(80.4)	—	—	—	— %	—	— %	(628)	(80.4)
Ground leases	(240)	(21.1)	1,066	239.0	(9)	(69.2)%	572	312.6 %	1,389	78.1
Total	(265)	(0.3)	17,452	201.1	(55)	(8.0)%	1,011	40.0 %	18,143	18.3
Net Operating Income, as defined	$741	0.3 %	$44,758	216.7 %	$1,094	182.6 %	$2,547	319.2 %	$49,140	20.6 %

Net Operating Income increased $49.1 million, or 20.6%, for the year ended December 31, 2012 as compared to the year ended December 31, 2011 primarily resulting from:

- An increase of $44.8 million attributable to the Acquisition Properties;

- An increase of $0.7 million attributable to the Same Store Properties primarily resulting from:

  - An increase in rental income of $3.9 million primarily resulting from an increase in tenant renewals at higher rental rates;

  - An offsetting decrease in other property income of $3.3 million primarily due to cash distributions received under a bankruptcy claim related to a former tenant that defaulted on their lease in 2009. During the year ended December 31, 2011, we received a $4.3 million initial cash distribution and during the year ended December 31, 2012, we received a final $0.9 million cash distribution. Other property income for both periods consist primarily of lease termination fees and other miscellaneous income; and

- A decrease in property and related expenses of $0.3 million primarily resulting from:
  - An increase of $1.0 million in property expenses primarily as a result of an increase in certain recurring operating costs such as property management expenses and janitorial and other service-related costs;
  - An offsetting decrease in real estate taxes of $0.4 million as a result of property tax refunds;
  - An offsetting decrease in provision for bad debts of $0.6 million due to a higher provision recorded in the prior year period for two watchlist tenants and
  - An offsetting decrease in ground lease expense of $0.2 million as a result of the expiration of a ground lease;
- An increase of $1.1 million attributable to the two completed redevelopment properties added to the stabilized portfolio during the fourth quarter of 2012:

- The net operating loss included in the results for the year ended December 31, 2011 related to one of the properties that was moved to the redevelopment portfolio during the third quarter of 2011.
- An increase in net operating income of $2.5 million attributable to the Other Properties primarily resulting from income generated in 2012 from:
- one redevelopment property in lease-up that was 50% occupied at December 31, 2012. The tenant took occupancy of this space in June 2012; and
- one in-process redevelopment property that was 17% occupied at December 31, 2012. The tenant took occupancy of this space in July 2012.

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Other Income and Expenses

General and Administrative Expenses

General and administrative expenses increased $8.0 million, or 28.6%, for the year ended December 31, 2012 compared to the year ended December 31, 2011 primarily as a result of an increase in compensation expense related to the February 2012 stock option grants made to our senior management team, higher payroll costs associated with the renegotiation of our Chief Executive Officer's employment agreement and an increase in payroll and administrative costs associated with the growth of the Company.

Depreciation and Amortization

Depreciation and amortization increased by $38.0 million, or 30.4%, for the year ended December 31, 2012 compared to the year ended December 31, 2011, primarily related to the Acquisition Properties.

Interest Expense

The following table sets forth our gross interest expense from continuing operations, including debt discounts/premiums and loan cost amortization, net of capitalized interest, including capitalized debt discounts/premiums and loan cost amortization for the years ended December 31, 2012 and 2011:

	2012	2011	Dollar Change	Percentage Change
	($ in thousands)			
Gross interest expense	$98,906	$94,915	$3,991	4.2 %
Capitalized interest	(19,792)	(9,130)	(10,662)	116.8 %
Interest expense	$79,114	$85,785	$(6,671)	(7.8)%

Gross interest expense, before the effect of capitalized interest, increased $4.0 million, or 4.2% for the year ended December 31, 2012 compared to the year ended December 31, 2011 resulting from an increase in our average outstanding debt balances primarily as a result of acquisition activity, partially offset by a decrease in our weighted average GAAP effective interest rate from approximately 5.2% during the year ended December 31, 2011 to approximately 4.7% during the year ended December 31, 2012.

Capitalized interest increased $10.7 million, or 116.8%, for the year ended December 31, 2012 compared to the year ended December 31, 2011 primarily as a result of an increase in our development and redevelopment activity, which resulted in higher average asset balances qualifying for interest capitalization. We anticipate capitalized interest to continue to increase in the upcoming year due to increased development and redevelopment activity that commenced in 2012 (see "Factors That May Influence Future Results of Operations" for additional information)

Year Ended December 31, 2011 Compared to Year Ended December 31, 2010

The prior year discussion of the results from operations is separated into following property groups:

- Same Store Properties - which includes the results of all of the office properties that were owned and included in our stabilized portfolio as of January 1, 2010 and still owned and included in the stabilized portfolio as of December 31, 2012;
- Acquisition Properties - which includes the results, from the dates of acquisition through the periods presented, for the ten office buildings we acquired in 2011 and the ten office buildings we acquired during 2010;
- Other Properties - which includes the results of properties not included in our stabilized portfolio. These properties consist of two office buildings that were moved from the stabilized portfolio during 2010, one office property that was moved from the stabilized portfolio during 2011, one redevelopment project under construction and one office building that was moved from the stabilized portfolio during 2012 to development since the property is being repositioned.

The following table sets forth certain information regarding the property groups within our stabilized portfolio as of December 31, 2011:

Group	# of Buildings	Rentable Square Feet
Same Store Properties	78	7,422,273
Acquisition Properties[1]	20	3,645,009
Total Stabilized Portfolio[2]	98	11,067,282

(1) Includes the ten office buildings we acquired in 2011 and the ten office buildings we acquired during 2010.
(2) We had no stabilized redevelopment properties in our stabilized portfolio during the comparison period.

The following table reconciles our Net Operating Income, as defined, to our net income for the years ended December 31, 2011 and 2010.

	Year Ended December 31, 2011	Year Ended December 31, 2010	Dollar Change	Percentage Change
	($ in thousands)			
Reconciliation to Net Income:				
Net Operating Income, as defined	$238,615	$179,302	$59,313	33.1 %
Unallocated (expense) income:				
General and administrative expenses	(28,148)	(27,963)	(185)	0.7
Acquisition-related expenses	(4,053)	(2,248)	(1,805)	80.3
Depreciation and amortization	(124,928)	(90,836)	(34,092)	37.5
Interest income and other net investment gains	571	964	(393)	(40.8)
Interest expense	(85,785)	(55,082)	(30,703)	55.7
Loss on early extinguishment of debt	—	(4,564)	4,564	100.0
Loss from continuing operations	(3,728)	(427)	(3,301)	773.1 %
Income from discontinued operations	19,630	19,364	266	1.4 %
Net gain on dispositions of discontinued operations	51,587	949	50,638	5,335.9 %
Net income	$67,489	$19,886	$47,603	239.4 %

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The following tables summarize the Net Operating Income, as defined, for our total portfolio for the years ended December 31, 2011 and 2010.

	2011 Same Store	Acquisition Properties	Other	Total	2010 Same Store	Acquisition Properties	Other	Total
	($ in thousands)				($ in thousands)			
Operating revenues:								
Rental income	$211,063	$ 94,520	$1,535	$307,118	$201,633	$ 28,901	$4,770	$235,304
Tenant reimbursements	16,437	7,287	253	23,977	16,212	471	1,313	17,996
Other property income	5,935	569	30	6,534	1,288	106	300	1,694
Total	233,435	102,376	1,818	337,629	219,133	29,478	6,383	254,994
Property and related expenses:								
Property expenses	41,907	23,524	1,390	66,821	41,485	7,045	2,639	51,169
Real estate taxes	17,890	10,112	1,631	29,633	18,529	3,033	1,912	23,474
Provision for bad debts	781	—	—	781	65	—	—	65
Ground leases	1,136	446	197	1,779	972	—	12	984
Total	61,714	34,082	3,218	99,014	61,051	10,078	4,563	75,692
Net Operating Income, as defined	$171,721	$ 68,294	$(1,400)	$238,615	$158,082	$ 19,400	$1,820	$179,302

	Year Ended December 31, 2011 as compared to the Year Ended December 31, 2010							
	Same Store		Acquisition Properties		Other		Total	
	Dollar Change	% Change	Dollar Change	% Change	Dollar Change	% Change	Dollar Change	% Change
	($ in thousands)							
Operating revenues:								
Rental income	$9,430	4.7 %	$65,619	227.0 %	$(3,235)	(67.8)%	$71,814	30.5 %
Tenant reimbursements	225	1.4	6,816	1,447.1	(1,060)	(80.7)	5,981	33.2
Other property income	4,647	360.8	463	436.8	(270)	(90.0)	4,840	285.7
Total	14,302	6.5	72,898	247.3	(4,565)	(71.5)	82,635	32.4
Property and related expenses:								
Property expenses	422	1.0	16,479	233.9	(1,249)	(47.3)	15,652	30.6
Real estate taxes	(639)	(3.4)	7,079	233.4	(281)	(14.7)	6,159	26.2
Provision for bad debts	716	1,101.5	—	—	—	—	716	1,101.5
Ground leases	164	16.9	446	100.0	185	1,541.7	795	80.8
Total	663	1.1	24,004	238.2	(1,345)	(29.5)	23,322	30.8
Net Operating Income, as defined	$13,639	8.6 %	$48,894	252.0 %	$(3,220)	(176.9)%	$59,313	33.1 %

Net Operating Income increased $59.3 million, or 33.1%, for the year ended December 31, 2011 as compared to the year ended December 31, 2010 primarily resulting from:

- An increase of $48.9 million attributable to the Acquisition Properties;
- An increase of $13.6 million attributable to the Same Store Properties primarily resulting from:
- An increase of $9.4 million in rental income primarily resulting from an increase in average occupancy of 5.6%, from 86.4% for the year ended December 31, 2010, to 92.0% for the year ended December 31, 2011;
-

- An increase in other property income primarily due to the receipt of a $4.3 million cash distribution under a bankruptcy claim related to a former tenant that defaulted on its lease in 2009;
- A decrease in real estate taxes of $0.6 million due to successful property tax appeals and lower than expected supplemental tax increases;

- An offsetting increase in our provision for bad debts of $0.7 million primarily as a result of changes in our estimates of collectability for two watchlist tenants; and
- An offsetting decrease of $3.2 million related to one office building that was moved from the stabilized portfolio to the redevelopment portfolio in 2010 and two office buildings that were moved to the redevelopment portfolio from the stabilized portfolio upon commencement of redevelopment in 2011. The reduction in Net Operating Income is due to the expiration of the leases at two of the office buildings. Upon expiration of these leases, we commenced redevelopment of these properties. We successfully completed the redevelopment of two of the office buildings in 2012 and moved them back into our stabilized portfolio during the fourth quarter of 2012. The third office building was in "lease-up" as of December 31, 2012.

Other Income and Expenses

General and Administrative Expense

General and administrative expenses increased $0.2 million, or 0.7%, for the year ended December 31, 2011 compared to the year ended December 31, 2010 primarily as a result of a net increase in compensation expense.

Depreciation and Amortization Expense

Depreciation and amortization expense increased $34.1 million, or 37.5%, for the year ended December 31, 2011 compared to the year ended December 31, 2010 primarily related to the Acquisition Properties.

Interest Income and Other Net Investment Gains

Total interest income and other net investment gains decreased by approximately $0.4 million, or 40.8%, for the year ended December 31, 2011 compared to the year ended December 31, 2010, primarily as a result of a decrease in the fair value of the marketable securities held in connection with our deferred compensation plan (see Note 16 to our consolidated financial statements included in this report for additional information).

Interest Expense

The following table sets forth our gross interest expense from continuing operations, including debt discounts/premiums and loan cost amortization, net of capitalized interest, including capitalized debt discounts/premiums and loan cost amortization for the years ended December 31, 2011 and 2010.

	2011	2010	Dollar Change	Percentage Change
	($ in thousands)			
Gross interest expense	$94,915	$65,097	$29,818	45.8 %
Capitalized interest	(9,130)	(10,015)	885	(8.8)%
Interest expense	$85,785	$55,082	$30,703	55.7 %

Gross interest expense, before the effect of capitalized interest, increased $29.8 million, or 45.8%, for the year ended December 31, 2011 compared to the year ended December 31, 2010 resulting from an increase in our average outstanding debt balances primarily as a result of our acquisition activity.

Capitalized interest decreased $0.9 million, or 8.8% for the year ended December 31, 2011 compared to the year ended December 31, 2010 primarily attributable to a decrease in our average development and redevelopment asset balances qualifying for interest capitalization for 2011 as compared to 2010.

Liquidity and Capital Resources of the Company

In this "Liquidity and Capital Resources of the Company" section, the term the "Company" refers only to Kilroy Realty Corporation on an unconsolidated basis, and excludes the Operating Partnership and all other subsidiaries.
The Company's business is operated primarily through the Operating Partnership. Distributions from the Operating Partnership are the Company's source of capital. The Company believes the Operating Partnership's sources of working capital, specifically its cash flow from operations and borrowings available under its revolving credit facility, are adequate for it to make its distribution payments to the Company and, in turn, for the Company to make its dividend payments to its preferred and common stockholders for the next 12 months. Cash flows from operating activities generated by the Operating Partnership for the year ended December 31, 2012 were sufficient to cover the Company's payment of cash dividends to its stockholders. However, there can be no assurance that the Operating Partnership's sources of capital will continue to be available at all or in amounts sufficient to meet its needs, including its ability to make distributions to the Company. The unavailability of capital could adversely affect the Operating Partnership's ability to make distributions to the Company, which would in turn, adversely affect the Company's ability to pay cash dividends to its stockholders.
The Company is a well-known seasoned issuer, and the Company and the Operating Partnership have an effective shelf registration statement that provides for the public offering and sale from time to time by the Company of its preferred stock, common stock, debt securities and guarantees of debt securities and by the Operating Partnership of its debt securities, in each case in unlimited amounts. The Company evaluates the capital markets on an ongoing basis and, as circumstances warrant, the Company and the Operating Partnership may issue securities of all of these types in one or more offerings at any time and from time to time on an opportunistic basis, depending upon, among other things, market conditions, available pricing and capital needs. When the Company receives proceeds from the sales of its preferred or common stock, it is required by the Operating Partnership's partnership agreement to contribute the net proceeds from those sales to the Operating Partnership in exchange for corresponding preferred or common units of the Operating Partnership. The Operating Partnership may use these proceeds and proceeds from the sale of its debt securities to repay debt, including borrowings under its revolving credit facility, to develop new or existing properties, to make acquisitions of properties or portfolios of properties, or for general corporate purposes.
As the sole general partner with control of the Operating Partnership, the Company consolidates the Operating Partnership for financial reporting purposes, and the Company does not have significant assets other than its investment in the Operating Partnership. Therefore, the assets and liabilities and the revenues and expenses of the Company and the Operating Partnership are substantially the same on their respective financial statements. The section entitled "Liquidity and Capital Resources of the Operating Partnership" should be read in conjunction with this section to understand the liquidity and capital resources of the Company on a consolidated basis and how the Company is operated as a whole.

Distribution Requirements

The Company is required to distribute 90% of its taxable income (subject to certain adjustments and excluding net capital gain) on an annual basis to maintain qualification as a REIT for federal income tax purposes and is required to pay income tax at regular corporate rates to the extent it distributes less than 100% of its taxable income (including capital gains). As a result of these distribution requirements, the Operating Partnership cannot rely on retained earnings to fund its on−going operations to the same extent as other companies whose parent companies are not REITs. In addition, the Company may be required to use borrowings under the Operating Partnership's revolving credit facility, if necessary, to meet REIT distribution requirements and maintain its REIT status. The Company may also need to continue to raise capital in the equity markets to fund the Operating Partnership's working capital needs, as well as potential developments of new or existing properties or acquisitions.
The Company intends to continue to make, but has not committed to make, regular quarterly cash distributions to common stockholders and common unitholders from cash flow from operating activities. All such distributions are at the discretion of the board of directors. The Company has historically distributed amounts in excess of our taxable income resulting in a return of capital to its stockholders and the Company currently believes it has the ability to

maintain distributions at the 2012 levels to meet its REIT requirements for 2013. The Company considers market factors and its performance in addition to REIT requirements in determining our distribution levels. Amounts accumulated for distribution to stockholders are invested primarily in interest−bearing accounts and short−term interest−bearing securities, which are consistent with the Company's intention to maintain its qualification as a REIT. Such investments may include, for example, obligations of the Government National Mortgage Association, other governmental agency securities, certificates of deposit, and interest−bearing bank deposits.

On December 6, 2012, the Board of Directors declared a regular quarterly cash dividend of $0.35 per common share payable on January 15, 2013 to stockholders of record on December 31, 2012 and caused a $0.35 per Operating Partnership common unit cash distribution to be paid in respect of the Operating Partnership's common limited partnership interests, including those owned by the Company. These dividends and distributions are equivalent to an annual rate of $1.40 per share, which in aggregate totals approximately $108.9 million of annualized common dividends and distributions per year based on shares of common stock, RSUs, and common units outstanding at December 31, 2012.

On March 27, 2012 and August 6, 2012, the Company issued 4,000,000 shares of its 6.875% Series G Cumulative Redeemable Preferred Stock ("Series G Preferred Stock") and 4,000,000 shares of its 6.375% Series H Cumulative Redeemable Preferred Stock ("Series H Preferred Stock"), respectively, at a public offering price of $25.00 per share, for a total of approximately $96.2 million of net proceeds for each offering, after deducting underwriting discounts and other offering-related costs. The net proceeds were used to redeem preferred stock and units as discussed below. Dividends on the Series G Preferred Stock and the Series H Preferred Stock are paid quarterly in arrears on the 15th day of each February, May, August and November and began on May 15, 2012 and November 15, 2012, respectively.

On December 6, 2012, the Board of Directors declared a dividend of $0.4296875 per share on the Series G Preferred Stock and $0.3984375 per share on the Series H Preferred Stock for the period commencing on and including November 15, 2012, and ending on and including February 14, 2013. The dividend will be paid on February 15, 2013, to Series G Preferred and Series H Preferred stockholders of record on January 31, 2013. Dividends and distributions payable to the Series G and Series H Preferred stockholders, total approximately $13.3 million of annualized preferred dividends and distributions.

On August 15, 2012 (the "Series A Redemption Date"), the Operating Partnership redeemed all 1,500,000 outstanding 7.45% Series A Cumulative Redeemable Preferred Units representing preferred limited partnership interests in the Operating Partnership ("Series A Preferred Units"). On the Series A Redemption Date, the Series A Preferred Units were redeemed at a redemption price equal to $50.00 per unit, representing $75.0 million in aggregate, plus all accrued and unpaid distributions to the Series A Redemption Date. We have no further distribution requirements with respect to the Series A Preferred Units.

On April 16, 2012 (the "Series E and F Redemption Date"), the Company redeemed all 1,610,000 outstanding shares of its 7.80% Series E Cumulative Redeemable Preferred Stock ("Series E Preferred Stock") and all 3,450,000 outstanding shares of its 7.50% Series F Cumulative Redeemable Preferred Stock ("Series F Preferred Stock"). On the Series E and F Redemption Date, the shares of Series E and Series F Preferred Stock (together, the "Redeemed Preferred Stock") were redeemed at a redemption price equal to their stated liquidation preference of $25.00 per share plus $2.9 million of dividends, which included $0.5 million of additional dividends attributable to the acceleration of the Series E Preferred Stock and Series F Preferred Stock dividend payment from April 1, 2012 to April 16, 2012 and redemption-related costs. We have no further distribution requirements with respect to the Series E and Series F Preferred Stock.

Debt Covenants

The covenants contained within the revolving credit facility and the term loan facility prohibit the Company from paying dividends in excess of 95% of FFO.

Capitalization

As of December 31, 2012, our total debt as a percentage of total market capitalization was 34.7% and our total debt and liquidation value of our preferred equity as a percentage of total market capitalization was 38.1%, which was calculated based on the closing price per share of the Company's common stock of $47.37 on December 31, 2012 as shown in the table below.

	Shares/Units at December 31, 2012	Aggregate Principal Amount or $ Value Equivalent ($ in thousands)	% of Total Market Capitalization	
Debt:				
Unsecured Revolving Credit Facility		$185,000	3.1	%
Unsecured Term Loan Facility		150,000	2.6	
4.25% Exchangeable Notes due 2014 (2)		172,500	2.9	
Unsecured Senior Notes due 2014		83,000	1.4	
Unsecured Senior Notes due 2015 (2)		325,000	5.5	
Unsecured Senior Notes due 2018 (2)		325,000	5.5	
Unsecured Senior Notes due 2020 (2)		250,000	4.3	
Secured debt (1) (2)		553,919	9.4	
Total debt		$2,044,419	34.7	%
Equity and Noncontrolling Interests:				
6.875% Series G Cumulative Redeemable Preferred stock (3)	4,000,000	100,000	1.7	
6.375% Series H Cumulative Redeemable Preferred stock (3)	4,000,000	100,000	1.7	
Common limited partnership units outstanding (4)(5)	1,826,503	86,521	1.5	
Common shares outstanding (5)	74,926,981	3,549,291	60.4	
Total equity and noncontrolling interests		3,835,812	65.3	
Total Market Capitalization (1)		$5,880,231	100.0	%

(1) At December 31, 2012, the Company had restricted cash balances on its consolidated balance sheet of approximately $247.5 million primarily due to disposition proceeds that were temporarily being held at a qualified intermediary, per our direction, for the purpose of facilitating Section 1031 Exchanges under the Code. Subsequent to December 31, 2012, we completed the Section 1031 Exchanges and the restricted cash balances were released and used for general corporate purposes, which included repaying an $83.1 million secured mortgage loan that was scheduled to mature on April 1, 2013, repaying borrowings under the Operating Partnership's revolving credit facility, as well as acquiring a two building office complex in Seattle, Washington for approximately $170.0 million that included the assumption of an approximate $83.9 million mortgage. In addition, on January 14, 2013, the Operating Partnership issued $300.0 million of 3.8% senior unsecured notes due 2023 and used the proceeds from the offering to repay the remaining outstanding balance on the Operating Partnership's revolving credit facility. As a result of the aforementioned transactions, the Company had a cash balance of approximately $150 million, a restricted cash balance of approximately $19 million, and no outstanding borrowings under the Operating Partnership's revolving credit facility as of January 30, 2013.

(2) Represents gross aggregate principal amount due at maturity before the effect of the unamortized discounts and premiums as of December 31, 2012.

(3) Value based on $25.00 per share liquidation preference.

(4) Represents common units not owned by the Company.

(5) Value based on closing price per share of the Company's common stock of $47.37 as of December 31, 2012.

Liquidity and Capital Resources of the Operating Partnership

In this "Liquidity and Capital Resources of the Operating Partnership" section, the terms "we," "our," and "us" refer to the Operating Partnership or the Operating Partnership and the Company together, as the context requires.

General

Our primary liquidity sources and uses are as follows:

Liquidity Sources

- Net cash flow from operations;
- Borrowings under the revolving credit facility;
- Proceeds from additional secured or unsecured debt financings;
- Proceeds from public or private issuance of debt or equity securities; and
- Proceeds from the disposition of nonstrategic assets through our capital recycling program.

Liquidity Uses

- Property or undeveloped land acquisitions;
- Property operating and corporate expenses;
- Capital expenditures, tenant improvement and leasing costs;
- Debt service and principal payments, including debt maturities;
- Distributions to common and preferred security holders;
- Development and redevelopment costs; and
- Outstanding debt repurchases.

General Strategy

Our general strategy is to maintain a conservative balance sheet with a top credit profile and to maintain a capital structure that allows for financial flexibility and diversification of capital resources. We manage our capital structure to reflect a long-term investment approach and utilize multiple sources of capital to meet our long-term capital requirements. We believe that our current projected liquidity requirements for the next 12-month period, as set forth above under the caption " —Liquidity Uses," will be satisfied using a combination of the liquidity sources listed above. We believe our conservative leverage and staggered debt maturities provide us with financial flexibility and enhances our ability to obtain additional sources of liquidity if necessary, and, therefore, we are well−positioned to refinance or repay maturing debt and to pursue our strategy of seeking attractive acquisition opportunities, which we may finance, as necessary, with future public and private issuances of debt and equity securities.

Summary of 2012 Funding Transactions

We have been active in the capital markets, loan originations and assumptions, and our capital recycling program to finance our acquisition activity and our continued desire to improve our debt maturities and lower our overall weighted average cost of capital. This was primarily as a result of the following transactions:

Capital Markets

- During 2012, we issued 787,118 shares under our at−the−market stock program. The net offering proceeds of approximately $36.3 million, after deducting sales agent compensation, were contributed to the Operating Partnership (see "— Liquidity Sources" below for additional information).
- In August 2012, the Company issued 4,000,000 shares of its 6.375% Series H Preferred Stock at a public offering price of $25.00 per share. The net proceeds of $96.2 million, after deducting the underwriting discount and other offering-related costs, were contributed to the Operating Partnership (see Notes 10 and 11 to our consolidated financial statements included in this report for additional information).
- In August 2012, the Company completed an underwritten public offering of 5,750,000 shares of its common stock. The net offering proceeds of approximately $253.8 million, after deducting underwriting discounts and commissions and offering expenses, were contributed to the Operating Partnership (see Notes 10 and 11 to our consolidated financial statements included in this report for additional information).

- In August 2012, the Operating Partnership redeemed all 1,500,000 outstanding Series A Preferred Units at a redemption price equal to $50.00 per unit, representing $75.0 million in aggregate, plus all accrued and unpaid distributions up to and including the redemption date of August 15, 2012 (see Notes 9 and 11 to our consolidated financial statements included in this report for additional information).
- In April 2012, the Company redeemed all 1,610,000 outstanding shares of its Series E Preferred Stock and all 3,450,000 outstanding shares of its Series F Preferred Stock at a redemption price of $25.00 per share plus all accumulated and unpaid dividends up to and including the redemption date of April 16, 2012, for total payment of $129.4 million (see Note 10 to our consolidated financial statements included in this report for additional information).
- In March 2012, the Company issued 4,000,000 shares of its 6.875% Series G Preferred Stock at a public offering price of $25.00 per share. The net proceeds of $96.2 million, after deducting the underwriting discount and other accrued offering-related costs, were contributed to the Operating Partnership (see Notes 10 and 11 to our consolidated financial statements included in this report for additional information).
- In February 2012, the Company completed an underwritten public offering of 9,487,500 shares of its common stock. The net offering proceeds of approximately $382.1 million, after deducting underwriting discounts and commissions and offering expenses, were contributed to the Operating Partnership (see Notes 10 and 11 to our consolidated financial statements included in this report for additional information).

Debt Activity

- In November 2012, the Operating Partnership completed an amendment to its $500 million unsecured revolving credit facility, which reduced the interest rate and borrowing costs and extended the maturity date to April 3, 2017. The revolving credit facility now bears interest at LIBOR plus 1.45% and includes a 30 basis point facility fee.
- During the year ended December 31, 2012, the Operating Partnership assumed four secured mortgage loans with a combined principal balance of $212.2 million and a combined premium balance of $8.9 million in connection with four acquisitions. The Operating Partnership also obtained a $97.0 million secured mortgage loan and repaid two secured mortgage loans with a combined outstanding principal balance of $101.0 million that were scheduled to mature in August 2012 (see Notes 3 and 7 to our consolidated financial statements included in this report for additional information).
- In April 2012, the Operating Partnership repaid its 3.25% Exchangeable Notes with an aggregate principal amount of $148.0 million and entered into a new $150.0 million unsecured term loan facility in March 2012 (see Note 7 to our consolidated financial statements included in this report for additional information).

Capital Recycling Program

- During the year ended December 31, 2012, the Company completed the sale of its entire industrial portfolio, which was comprised of 39 industrial properties, and seven office buildings with a combined total 3,975,665 rentable square feet for a total gross sales price of $500.3 million (see Note 17 to our consolidated financial statements included in this report for additional information). As of December 31, 2012, approximately $228.8 million of the sales proceeds were included in restricted cash on our consolidated balance sheet for the purpose of facilitating Section 1031 Exchanges.

Capital Events Subsequent to December 31, 2012

- As a result of the aforementioned events discussed above, we ended the year with restricted cash of $247.5 million and an outstanding balance of $185.0 million on our revolving credit facility. In January 2013, we completed two Section 1031 Exchanges and the restricted cash balances related to our fourth quarter dispositions were released and used to acquire a two building office complex in Seattle, Washington for approximately $170.0 million (the purchase price includes an assumption of debt of approximately $83.9 million) and to repay a $83.1 million secured mortgage loan that matured in the first quarter of 2013. In addition, on January 14, 2013 the Operating Partnership issued $300.0 million of its 3.800% unsecured senior notes due 2023 and used the proceeds from the offering to repay the outstanding balance on the revolving credit facility.

Liquidity Sources

Credit Facility

In March 2012, we amended the revolving credit facility to reduce the FMV Cap Rate (as defined in the revolving credit facility agreement), which is used to calculate the fair value of our assets for certain covenants under the revolving credit facility, from 7.50% to 6.75%. In November 2012, we amended and restated the revolving credit facility to extend the maturity date and reduce the interest rate and facility fee. We previously amended our revolving credit facility in June 2011, to extend the maturity date and reduce the interest rate and facility fee. The following table summarizes the terms of our revolving credit facility as of December 31, 2011 and as amended as of December 31, 2012:

	December 31, 2012		December 31, 2011	
	(in thousands)			
Outstanding borrowings	$185,000		$182,000	
Remaining borrowing capacity	315,000		318,000	
Total borrowing capacity (1)	$500,000		$500,000	
Interest rate (2)	1.66	%	2.05	%
Facility fee - annual rate (3)	0.300	%	0.350	%
Maturity date (4)	April 2017		August 2015	

(1) We may elect to borrow, subject to bank approval, up to an additional $200.0 million under an accordion feature under the terms of the revolving credit facility.

(2) The revolving credit facility interest rate was calculated based on an annual rate of LIBOR plus 1.450% and 1.75% as of December 31, 2012 and December 31, 2011, respectively.

(3) The facility fee is paid on a quarterly basis and is calculated based on the total borrowing capacity. In addition to the facility fee, we also incurred debt origination and legal costs of approximately $5.0 million when we entered into the revolving credit facility in 2010, an additional $3.3 million when we amended the terms of the revolving credit facility in June 2011 and an additional $1.9 million when we amended the terms of the revolving credit facility in November 2012. The unamortized balance of these costs will be amortized through the extended maturity date of the revolving credit facility.

(4) Under the original and amended terms of the Credit Facility, we may exercise an option to extend the maturity date by one year.

We intend to borrow under the revolving credit facility from time to time for general corporate purposes, to fund potential acquisitions, to finance development and redevelopment expenditures, and to potentially repay long-term debt.

Capital Recycling Program

In connection with our capital recycling program, we continuously evaluate opportunities for the potential disposition of properties and undeveloped land in our portfolio with the intent of recycling the proceeds generated from the dispositions of non-strategic or lower return assets into capital used to fund new operating and development acquisitions, to finance development and redevelopment expenditures, to repay long-term debt and for other general corporate purposes. As part of our strategy, we intend, when practical, to enter into Section 1031 Exchanges to defer some or all of the taxable gains, if any, on the sales for federal and state income tax purposes.

During the fourth quarter ended December 31, 2012, we disposed of five office properties and our entire industrial portfolio, which was comprised of 39 industrial properties, with a combined 3,721,989 rentable square feet, for a total of approximately $354.2 million at a net gain of $186.4 million (see Note 17 to our consolidated financial statements included in this report for more information). In connection with this transaction, the dispositions were structured to qualify as Section 1031 Exchanges, and approximately $228.8 million of the sales proceeds were included in restricted cash on our consolidated balance sheet. Subsequent to December 31, 2012, we were able to successfully complete Section 1031 Exchanges and the amounts were reinvested into qualifying replacement properties (see "—Capital Events Subsequent to December 31, 2012" above for additional information).

In addition, in January 2012, we disposed of two office buildings in one transaction for approximately $146.1 million at a gain of approximately $72.8 million. We were able to successfully complete Section 1031 Exchanges for these properties and reinvest the funds into qualified replacement acquisition properties.

The timing of any potential future disposition transactions will depend on market conditions and other factors including but not limited to our capital needs and our ability to defer some or all of the taxable gains on the sales. We cannot assure you that we will dispose of any additional properties, or that future acquisitions and/or dispositions, if any, will qualify as Section 1031 Exchanges.

At-the-Market Stock Offering Program

Under our at-the-market stock offering program, which commenced in July 2011, we may offer and sell shares of our common stock having an aggregate gross sales price of up to $200.0 million from time to time in "at the market" offerings. During the year ended December 31, 2012, we sold 787,118 shares of common stock under the program for aggregate gross proceeds of approximately $37.0 million and net proceeds of approximately $36.3 million, after sales agent compensation. The proceeds from the sales were used to fund acquisitions and general corporate purposes including repayment of borrowings under the revolving credit facility. Since commencement of the program, we have sold 1,142,423 shares of common stock and, as of December 31, 2012, approximately $150.0 million remains available to be sold under this program. Actual sales will depend upon a variety of factors including but not limited to market conditions, the trading price of the Company's common stock and our capital needs. We have no obligation to sell the remaining shares available for sale under this program.

Shelf Registration Statement

As discussed above under "-Liquidity and Capital Resources of the Company," the Company is a well-known seasoned issuer and the Company and the Operating Partnership have an effective shelf registration statement that provides for the public offering and sale from time to time by the Company of its preferred stock, common stock, debt securities and guarantees of debt securities and by the Operating Partnership of its debt securities, in each case in unlimited amounts. The Company evaluates the capital markets on an ongoing basis and, as circumstances warrant, the Company and the Operating Partnership may issue securities of all of these types in one or more offerings at any time and from time to time on an opportunistic basis, depending upon, among other things, market conditions, available pricing and capital needs. When the Company receives proceeds from the sales of its preferred or common stock, it is required by the Operating Partnership's partnership agreement to contribute the net proceeds from those sales to the Operating Partnership in exchange for corresponding preferred or common units of the Operating Partnership. The Operating Partnership may use these proceeds and proceeds from the sale of its debt securities to repay debt, including borrowings under its revolving credit facility, to develop new or existing properties, to make acquisitions of properties or portfolios of properties, or for general corporate purposes.

Unsecured Term Loan Facility

In March 2012, we entered into a new term loan facility, which is included in unsecured debt, net on our consolidated balance sheets. The term loan facility bears interest at an annual rate of LIBOR plus 1.750% and is scheduled to mature on March 29, 2016. Under the terms of the term loan facility, we may exercise an option to extend the maturity date by one year. We may elect to borrow up to an additional $100.0 million under an accordion option, subject to bank approval. We used the borrowings under the term loan facility to repay the 3.25% Exchangeable Notes in April 2012 upon maturity.

Exchangeable Notes, Unsecured Senior Notes, and Secured Debt

The aggregate principal amount of our 4.25% Exchangeable Notes, unsecured debt, and secured debt of the Operating Partnership outstanding as of December 31, 2012 was as follows:

	Aggregate Principal Amount Outstanding ($ in thousands)
Unsecured Term Loan Facility due 2016	$150,000
4.25% Exchangeable Notes due 2014 (1)	172,500

Unsecured Senior Notes due 2014	83,000
Unsecured Senior Notes due 2015 [(1)]	325,000
Unsecured Senior Notes due 2018 [(1)]	325,000
Unsecured Senior Notes due 2020 [(1)]	250,000
Secured Debt [(1)]	553,919
Total Exchangeable Notes, Unsecured Senior Notes, and Secured Debt	$1,859,419

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(1) Represents gross aggregate principal amount before the effect of the unamortized discounts and premiums as of December 31, 2012.

On January 14, 2013, the Operating Partnership issued $300.0 million of 3.8% unsecured senior notes due 2023 and used the proceeds from the offering to repay the remaining outstanding balance on the Operating Partnership's revolving credit facility.

Debt Composition

The composition of the Operating Partnership's aggregate debt balances between secured and unsecured and fixed-rate and variable-rate debt as of December 31, 2012 and 2011 was as follows:

	Percentage of Total Debt		Weighted Average Interest Rate	
	2012	2011	2012	2011
Secured vs. unsecured:				
Unsecured (1)	72.9 %	80.9 %	4.5 %	4.7 %
Secured	27.1	19.1	5.2	5.2
Variable-rate vs. fixed-rate:				
Variable-rate	16.4	9.9	1.8	2.0
Fixed-rate (1)	83.6	90.1	5.3	5.1
Total stated rate (1)			4.7	4.8
GAAP effective rate (2)			4.7	5.2
Total GAAP effective rate including debt issuance costs			5.1 %	5.6 %

(1) Excludes the impact of the amortization of any debt discounts/premiums.
(2) Includes the impact of the amortization of any debt discounts/premiums, excluding debt issuance costs.

Liquidity Uses

Contractual Obligations

The following table provides information with respect to our contractual obligations as of December 31, 2012. The table: (i) indicates the maturities and scheduled principal repayments of our secured debt, 4.25% Exchangeable Notes, unsecured debt, and revolving credit facility; (ii) indicates the scheduled interest payments of our fixed-rate and variable-rate debt as of December 31, 2012; (iii) provides information about the minimum commitments due in connection with our ground lease obligations and other lease and contractual commitments; and (iv) provides estimated redevelopment and development commitments as of December 31, 2012. Note that the table does not reflect our available debt maturity extension options and reflects gross aggregate principal amounts before the effect of unamortized discounts/premiums.

	Payment Due by Period				
	Less than 1 Year (2013)	1–3 Years (2014-2015)	3–5 Years (2016-2017)	More than 5 Years (After 2017)	Total
	(in thousands)				
Principal payments—secured debt (1)	$90,881	$77,124	$167,858	$218,056	$553,919
Principal payments—4.25% Exchangeable Notes (2)	—	172,500	—	—	172,500
Principal payments—unsecured debt (3)	—	408,000	150,000	575,000	1,133,000
Principal payments—Credit Facility	—	—	185,000	—	185,000
Interest payments—fixed-rate debt (4)	86,024	150,021	89,550	87,717	413,312
Interest payments—variable-rate debt (5)	6,581	13,162	5,252	—	24,995
Ground lease obligations (6)	3,685	6,190	6,190	160,007	176,072
Lease and contractual commitments (7)	76,976	3,791	—	—	80,767
	239,000	282,000	—	—	521,000

Development and redevelopment commitments (8)					
Total	$503,147	$1,112,788	$603,850	$1,040,780	$3,260,565

(1) Represents gross aggregate principal amount before the effect of the unamortized premium of approximately $7.2 million as of December 31, 2012.

(2) Represents gross aggregate principal amount before the effect of the unamortized discount of approximately $8.6 million as of December 31, 2012.

(3) Represents gross aggregate principal amount before the effect of the unamortized discount of approximately $2.1 million as of December 31, 2012.

(4) As of December 31, 2012, 83.6% of our debt was contractually fixed. The information in the table above reflects our projected interest rate obligations for these fixed-rate payments based on the contractual interest rates, interest payment dates, and scheduled maturity dates.

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(5) As of December 31, 2012, 16.4% of our debt bore interest at variable rates all of which was incurred under the term loan facility and revolving credit facility. The variable interest rate payments are based on LIBOR plus a spread of 1.450% and 1.750% as of December 31, 2012, respectively per facility. The information in the table above reflects our projected interest rate obligations for these variable-rate payments based on outstanding principal balances as of December 31, 2012, the scheduled interest payment dates, and the contractual maturity dates.

(6) Reflects minimum lease payments as discussed in Note 15 to our consolidated financial statements, through the contractual lease expiration date before the impact of extension options.

(7) Amounts represent commitments under signed leases and contracts for operating properties, excluding tenant-funded tenant improvements. The timing of these expenditures may fluctuate.

(8) Amounts represent commitments under signed leases for pre-leased development projects and contractual commitments for redevelopment contracts and projects under construction as of December 31, 2012 and trailing costs for stabilized redevelopment properties. The timing of these expenditures may fluctuate based on the ultimate progress of construction. This table also reflects the November 2012 exercise of the purchase option to acquire the land under a ground lease at one of our redevelopment properties in the second quarter of 2013 for a purchase price of $27.5 million to be paid upon closing. See Note 15 to our consolidated financial statements included in this report for additional information.

Potential Future Capital Requirements

Debt Maturities

As of December 31, 2012, we had one secured loan with a principal balance of $83.1 million scheduled to mature in 2013, which we repaid subsequent to year-end with a portion of the remaining proceeds from the sale of our industrial portfolio.

Potential Future Acquisitions

In 2011, we acquired 11 buildings for approximately $603.3 million in cash. In 2012, we acquired 14 buildings for approximately $454.8 million in cash, all of which we funded through various capital raising activities, and in selected instances, the assumption of existing indebtedness. In addition, in 2012 we acquired six development property project opportunities for approximately $333.9 million in cash and other assumed liabilities Subsequent to December 31, 2012, we acquired a two building office complex in Seattle, Washington for approximately $170.0 million with a portion of the remaining proceeds from the sale of our industrial portfolio. We continually evaluate selected acquisition opportunities as they arise. As a result, at any point in time, we may have one or more potential acquisitions under consideration that are in varying stages of evaluation, negotiation or due diligence review, which may include potential acquisitions under contract. We expect that any material acquisitions will be funded with borrowings under our revolving credit facility, the public or private issuance of debt or equity securities, or through the disposition of assets under our capital recycling program.

Redevelopment and Development Opportunities

As of December 31, 2012, we had one redevelopment and four development projects under construction. These projects have a total estimated investment of approximately $988.8 million, of which we have incurred approximately $411.3 million as of December 31, 2012. Of the remaining $577.5 million yet to be incurred, we are currently contractually obligated to pay approximately $239.0 million over the next year, which are included in our contractual obligations table above. We may also incur up to approximately $8.7 million in additional leasing related costs for these projects over the next year, depending on leasing activity. In addition, we currently have additional development and redevelopment projects that are scheduled to commence construction in 2013. If these projects commence as currently projected, we will invest between $80 million and $100 million in addition to the above commitments. This estimate is based on market conditions and our anticipation of project approvals. Actual costs could vary depending on changes in circumstances. Ultimate timing of these expenditures may fluctuate given the ultimate progress and leasing status of the projects.

Potential Future Leasing Costs and Capital Improvements

Given the current economic conditions, the amounts we are required to spend on tenant improvements and leasing costs would need to remain at current levels for us to be able to execute leases at current market terms, as evidenced in the table below. The amounts we ultimately incur for tenant improvements and leasing costs will depend on actual leasing activity. Tenant improvements and leasing costs generally fluctuate in any given period depending on factors such as the type of property, the term of the lease, the type of the lease, the involvement of external leasing agents, and overall market conditions. Capital expenditures may fluctuate in any given period subject to the nature, extent, and timing of improvements required to maintain our properties.

We believe we could spend between $45 to $65 million in capital improvements, tenant improvements, and leasing costs in 2013 for properties within our stabilized portfolio, depending on leasing activity, in addition to approximately $77 million of lease and contractual commitments discussed in our capital commitments table above.

The following tables set forth our historical actual capital expenditures, and tenant improvements and leasing costs for deals commenced, excluding tenant-funded tenant improvements, for renewed and re-tenanted space within our stabilized portfolio for each of the three years during the period ended December 31, 2012 on a per square foot basis.

	Year Ended December 31,		
	2012	2011	2010
Office Properties:			
Capital Expenditures:			
Capital expenditures per square foot	$0.78	$0.71	$1.36
Tenant Improvement and Leasing Costs (1)			
Replacement tenant square feet	607,118	468,530	637,155
Tenant improvements per square foot commenced	$31.75	$24.95	$28.03
Leasing commissions per square foot commenced	$11.22	$11.46	$9.30
Total per square foot	$42.97	$36.41	$37.33
Renewal tenant square feet	629,664	709,427	691,531
Tenant improvements per square foot commenced	$9.63	$27.73	$12.67
Leasing commissions per square foot commenced	$7.91	$9.27	$8.31
Total per square foot	$17.53	$37.00	$20.98
Total per square foot per year	$5.30	$4.01	$5.49
Average remaining lease term (in years)	5.7	9.2	5.3

(1) Includes only tenants with lease terms of 12 months or longer. Excludes leases for month-to-month and first generation tenants.

Capital expenditures per square foot increased moderately in 2012. As all of our properties are well-maintained and do not require significant capital improvements, we currently anticipate future capital expenditure levels to be consistent with historical levels. The 2012 increase in replacement tenant improvements per square foot commenced is primarily due to increased activity in San Diego and San Francisco, which command higher lease and tenant improvement rates. The 2012 decrease in renewal tenant improvements per square foot commenced is primarily due to the commencement of one significant lease renewal in 2011. Excluding this one lease, office tenant improvements per square foot leased would be materially consistent with the previous year.

Distribution Requirements

For a discussion of our dividend and distribution requirements, see "Liquidity and Capital Resources of the Company - Distribution Requirements."

Other Potential Future Liquidity Uses

As of the filing date, we are in various stages of negotiation on other potential future acquisition opportunities, including potential joint venture opportunities. We expect that any material acquisitions or development activities will be funded with borrowings under our revolving credit facility, the public or private issuance of debt or equity securities, the disposition of assets under our capital recycling program or through the assumption of existing debt.

In addition, the amounts we are required to spend on tenant improvements and leasing costs we ultimately incur will depend on actual leasing activity. Tenant improvements and leasing costs generally fluctuate in any given period depending on factors such as the type of property, the term of the lease, the type of the lease, the involvement of external leasing agents, and overall market conditions. Capital expenditures may fluctuate in any given period subject to the nature, extent, and timing of improvements required to maintain or improve our properties.

Factors That May Influence Future Sources of Capital and Liquidity of the Company and Operating Partnership

We continue to evaluate sources of financing for our business activities, including borrowings under the revolving credit facility, issuance of public and private equity securities, unsecured debt and fixed-rate secured mortgage financing, and proceeds from the disposition of nonstrategic assets through our capital recycling program. However, the Operating Partnership's ability to obtain new financing or refinance existing borrowings on favorable terms could be impacted by various factors, including the state of economic conditions, the state of the credit and equity markets, significant tenant defaults, a decline in the demand for office properties, a decrease in market rental rates or market values of real estate assets in our submarkets, and the amount of future borrowings. These events could result in the following:

- Decreases in our cash flows from operations, which could create further dependence on our revolving credit facility;

- An increase in the proportion of variable-rate debt, which could increase our sensitivity to interest rate fluctuations in the future; and
- A decrease in the value of our properties, which could have an adverse effect on the Operating Partnership's ability to incur additional debt, refinance existing debt at competitive rates, or comply with its existing debt obligations.

In addition to the factors noted above, the Operating Partnership's credit ratings are subject to ongoing evaluation by credit rating agencies and may be changed or withdrawn by a rating agency in the future if, in its judgment, circumstances warrant. In the event that the Operating Partnership's credit ratings are downgraded, we may incur higher borrowing costs and may experience difficulty in obtaining additional financing or refinancing existing indebtedness.

Debt Covenants

The revolving credit facility, term loan facility, unsecured senior notes, and certain other secured debt arrangements contain covenants and restrictions requiring us to meet certain financial ratios and reporting requirements. Key existing financial covenants and their covenant levels include:

Credit Facility and Unsecured Term Loan Facility (as defined in the Credit Agreement):	Covenant Level	Actual Performance at December 31, 2012 (1)
Total debt to total asset value	less than 60%	36%
Fixed charge coverage ratio	greater than 1.5x	2.5x
Unsecured debt ratio	greater than 1.67x	2.45x
Unencumbered asset pool debt service coverage	greater than 2.0x	3.3x
Unsecured Senior Notes due 2015, 2018 and 2020 (as defined in the Indentures):		
Total debt to total asset value	less than 60%	40%
Interest coverage	greater than 1.5x	3.6x
Secured debt to total asset value	less than 40%	11%
Unencumbered asset pool value to unsecured debt	greater than 150%	268%

(1) In March 2012, we amended the revolving credit facility to reduce the FMV Cap Rate (as defined in the revolving credit facility), which is used to calculate the fair value of our assets for certain covenants under the revolving credit facility, from 7.50% to 6.75%.

The Operating Partnership was in compliance with all its debt covenants as of December 31, 2012. Our current expectation is that the Operating Partnership will continue to meet the requirements of its debt covenants in both the short and long term. However, in the event of an economic slowdown or continued volatility in the credit markets, there is no certainty that the Operating Partnership will be able to continue to satisfy all the covenant requirements.

Historical Cash Flow Summary
Our historical cash flow activity for the year ended December 31, 2012 as compared to the year ended December 31, 2011 was as follows:

	Year Ended December 31,			
	2012	2011	Dollar Change	Percentage Change
	($ in thousands)			
Net cash provided by operating activities	$180,724	$138,256	$42,468	30.7 %
Net cash used in investing activities	(706,506)	(634,283)	(72,223)	11.4
Net cash provided by financing activities	537,705	485,964	51,741	10.6

Operating Activities
Our cash flows from operations depends on numerous factors including the occupancy level of our portfolio, the rental rates achieved on our leases, the collectability of rent and recoveries from our tenants, the level of operating expenses, the impact of property acquisitions and related financing activities, and other general and administrative costs. Our net cash provided by operating activities increased by $42.5 million, or 30.7%, for the year ended December 31, 2012 compared to the year ended December 31, 2011 primarily as the result of an increase in cash Net Operating Income generated primarily from our Acquisitions Portfolio partially offset by increased interest expense attributable to the increase in our average outstanding debt balances as a result of our acquisition activity. See additional information under the capital "—Rental Operations."
Investing Activities
Our net cash used in investing activities is generally used to fund property acquisitions, recurring and nonrecurring capital expenditures for our operating properties, and development and redevelopment projects. Our net cash used in investing activities increased $72.2 million, or 11.4%, for the year ended December 31, 2012 compared to the year ended December 31, 2011. This net increase was primarily attributable to year over year increases of approximately $185.5 million due to acquisitions, $54.8 million due to the increased activity in our redevelopment and development pipeline, $23.6 million of operating portfolio expenditures due to increased leasing activity, offset by an increase of $199.4 million of net proceeds received from dispositions.

Financing Activities
Our net cash provided by financing activities is generally impacted by our capital raising activities net of dividends and distributions paid to common and preferred security holders. Net cash provided by financing activities increased by $51.7 million, or 10.6%, for the year ended December 31, 2012 compared to the year ended December 31, 2011. We were active in the capital markets in 2012, with a net increase of approximately $71.7 million provided by our various capital raising activities. This net increase was partially offset by our year over year increase in dividend payments to common stockholders of approximately $17.4 million as a result of our increased common share count from common equity offerings. See additional information under the caption "Liquidity and Capital Resources of the Operating Partnership—Summary of 2012 Funding Transactions."

Off-Balance Sheet Arrangements
As of December 31, 2012