

Piedmont Office Realty Trust, Inc.  
Form 10-Q  
November 14, 2008  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**

**FORM 10-Q**

(Mark One)

**Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**  
for the quarterly period ended September 30, 2008

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 000-25739

**PIEDMONT OFFICE REALTY TRUST, INC.**

(Exact name of registrant as specified in its charter)

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

**58-2328421**  
(I.R.S. Employer Identification Number)

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11695 Johns Creek Parkway

Ste. 350

Johns Creek, Georgia 30097

(Address of principal executive offices)

(Zip Code)

(770) 418-8800

(Registrant's telephone number, including area code)

N/A

(Former name, former address, and former fiscal year, if changed since last report)

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

Yes  No

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

Large Accelerated filer

Non-Accelerated filer  (Do not check if a smaller reporting company)

Accelerated filer

Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

**Number of shares outstanding of the registrant's**

**only class of common stock, as of October 31, 2008: 475,352,910 shares**

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**FORM 10-Q**

**PIEDMONT OFFICE REALTY TRUST, INC.**

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**CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS**

Certain statements contained in this Form 10-Q and other written or oral statements made by or on behalf of Piedmont Office Realty Trust, Inc. ( Piedmont ) may constitute forward-looking statements within the meaning of the federal securities laws. In addition, Piedmont, or the executive officers on Piedmont s behalf, may from time to time make forward-looking statements in reports and other documents Piedmont files with the Securities and Exchange Commission or in connection with oral statements made to the press, potential investors, or others. Statements regarding future events and developments and Piedmont s future performance, as well as management s expectations, beliefs, plans, estimates, or projections relating to the future, are forward-looking statements within the meaning of these laws. Forward-looking statements include statements preceded by, followed by, or that include the words may, will, expect, intend, anticipate, estimate, believe, continue, or similar words. Examples of such statements in this report include descriptions of our real estate, financing, and operating objectives; descriptions of our share redemption program and our ability to purchase additional shares under such program; discussions regarding future distributions; and discussions regarding the potential impact of economic conditions on our portfolio.

These statements are based on beliefs and assumptions of Piedmont s management, which in turn are based on currently available information. Important assumptions relating to the forward-looking statements include, among others, assumptions regarding the demand for office space in the sectors in which Piedmont operates, competitive conditions, and general economic conditions. These assumptions could prove inaccurate. The forward-looking statements also involve risks and uncertainties, which could cause actual results to differ materially from those contained in any forward-looking statement. Many of these factors are beyond Piedmont s ability to control or predict. Such factors include, but are not limited to, the following:

Lease terminations or lease defaults, particularly by one of Piedmont s large lead tenants;

The impact of competition on Piedmont s efforts to renew existing leases or re-let space on terms similar to existing leases;

Changes in the economies and other conditions of the office market in general and of the specific markets in which Piedmont operates, particularly in Chicago, Washington, D.C., and the New York metropolitan area;

Economic and regulatory changes that impact the real estate market generally;

Potential development and construction delays and resultant increased costs and risks;

The success of Piedmont s real estate strategies and investment objectives;

Costs of complying with governmental laws and regulations;

Uncertainties associated with environmental and other regulatory matters;

Piedmont s ability to continue to qualify as a REIT under the Internal Revenue Code of 1986, as amended; and

Other factors, including the risk factors discussed under Item 1A. of this Form 10-Q and Piedmont s Annual Report on Form 10-K for the year ended December 31, 2007.

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Management believes these forward-looking statements are reasonable; however, undue reliance should not be placed on any forward-looking statements, which are based on current expectations. Further, forward-looking statements speak only as of the date they are made, and management undertakes no obligation to update publicly any of them in light of new information or future events.

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**PART I. FINANCIAL STATEMENTS**

**ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS**

The information furnished in the accompanying consolidated balance sheets and related consolidated statements of income, stockholders' equity, and cash flows reflects all adjustments, that are, in management's opinion, necessary for a fair and consistent presentation of financial position, results of operations, and cash flows in accordance with U.S. generally accepted accounting principles.

The accompanying financial statements should be read in conjunction with the notes to Piedmont's financial statements and Management's Discussion and Analysis of Financial Condition and Results of Operations included in this report on Form 10-Q and with Piedmont's Annual Report on Form 10-K for the year ended December 31, 2007. Piedmont's results of operations for the three months and nine months ended September 30, 2008 are not necessarily indicative of the operating results expected for the full year.

**Table of Contents****PIEDMONT OFFICE REALTY TRUST, INC.****CONSOLIDATED BALANCE SHEETS**

(in thousands, except for share and per share amounts)

	(Unaudited) September 30, 2008	December 31, 2007
<b>Assets:</b>		
Real estate assets, at cost:		
Land	\$ 659,637	\$ 645,881
Buildings and improvements, less accumulated depreciation of \$539,198 and \$468,359 as of September 30, 2008 and December 31, 2007, respectively	3,106,654	3,066,494
Intangible lease assets, less accumulated amortization of \$169,283 and \$160,837 as of September 30, 2008 and December 31, 2007, respectively	140,321	172,425
Construction in progress	14,960	38,014
<b>Total real estate assets</b>	<b>3,921,572</b>	<b>3,922,814</b>
Investments in unconsolidated joint ventures	48,603	52,468
Cash and cash equivalents	47,977	65,016
Tenant receivables, net of allowance for doubtful accounts of \$854 and \$549 as of September 30, 2008 and December 31, 2007, respectively	125,761	122,130
Notes receivable	46,750	854
Due from unconsolidated joint ventures	1,174	1,244
Prepaid expenses and other assets	25,323	21,864
Goodwill	180,390	180,371
Deferred financing costs, less accumulated amortization of \$5,803 and \$4,224 as of September 30, 2008 and December 31, 2007, respectively	10,539	10,075
Deferred lease costs, less accumulated amortization of \$111,816 and \$95,229 as of September 30, 2008 and December 31, 2007, respectively	196,618	202,910
<b>Total assets</b>	<b>\$ 4,604,707</b>	<b>\$ 4,579,746</b>
<b>Liabilities:</b>		
Line of credit and notes payable	\$ 1,548,625	\$ 1,301,530
Accounts payable, accrued expenses, and accrued capital expenditures	115,299	110,548
Deferred income	29,157	28,882
Intangible lease liabilities, less accumulated amortization of \$61,149 and \$52,100 as of September 30, 2008 and December 31, 2007, respectively	76,233	84,886
Interest rate swap	1,045	
<b>Total liabilities</b>	<b>1,770,359</b>	<b>1,525,846</b>
<b>Commitments and Contingencies</b>		
<b>Minority Interest</b>	<b>5,145</b>	<b>6,546</b>
<b>Redeemable Common Stock</b>	<b>86,972</b>	<b>166,809</b>
<b>Stockholders' Equity:</b>		
Common stock, \$.01 par value; 900,000,000 shares authorized; 475,797,584 shares issued and outstanding at September 30, 2008; and 488,974,478 shares issued and outstanding at December 31, 2007	4,758	4,890
Additional paid-in capital	3,461,713	3,568,801
Cumulative distributions in excess of earnings	(636,223)	(526,337)
Redeemable common stock	(86,972)	(166,809)
Other comprehensive income (loss)	(1,045)	

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Total stockholders' equity	2,742,231	2,880,545
Total liabilities, minority interest, redeemable common stock, and stockholders' equity	<b>\$ 4,604,707</b>	<b>\$ 4,579,746</b>

*See accompanying notes.*

**Table of Contents****PIEDMONT OFFICE REALTY TRUST, INC.****CONSOLIDATED STATEMENTS OF INCOME**

(in thousands, except for share and per share amounts)

	(Unaudited)		(Unaudited)	
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
<b>Revenues:</b>				
Rental income	\$ 113,483	\$ 110,601	\$ 341,796	\$ 332,729
Tenant reimbursements	37,111	37,815	112,844	108,555
Property management fee revenue	746	682	2,382	1,111
Other rental income	3,955	382	9,527	1,429
Gain on sale of real estate assets				50
	<b>155,295</b>	<b>149,480</b>	<b>466,549</b>	<b>443,874</b>
<b>Expenses:</b>				
Property operating costs	53,726	55,678	166,417	160,722
Asset and property management fees:				
Related party				8,453
Other	535	489	1,491	3,633
Depreciation	25,248	24,026	73,747	70,914
Amortization	15,019	17,531	47,148	52,181
General and administrative	7,976	8,021	24,292	20,880
	<b>102,504</b>	<b>105,745</b>	<b>313,095</b>	<b>316,783</b>
<b>Real estate operating income</b>	<b>52,791</b>	<b>43,735</b>	<b>153,454</b>	<b>127,091</b>
<b>Other income (expense):</b>				
Interest expense	(19,798)	(15,616)	(55,159)	(47,282)
Interest and other income	1,076	806	2,854	3,657
Equity in (loss) income of unconsolidated joint ventures	(1,438)	485	(362)	3,168
Loss on extinguishment of debt		(104)		(164)
Loss on interest rate swap	(620)		(647)	
	<b>(20,780)</b>	<b>(14,429)</b>	<b>(53,314)</b>	<b>(40,621)</b>
<b>Income from continuing operations before minority interest</b>	<b>32,011</b>	<b>29,306</b>	<b>100,140</b>	<b>86,470</b>
<b>Minority interest in earnings of consolidated entities</b>	<b>(123)</b>	<b>(163)</b>	<b>(430)</b>	<b>(530)</b>
<b>Income from continuing operations</b>	<b>31,888</b>	<b>29,143</b>	<b>99,710</b>	<b>85,940</b>
<b>Discontinued operations:</b>				
Operating income		6	10	862
Gain on sale of real estate assets		10		20,680
<b>Income from discontinued operations</b>		<b>16</b>	<b>10</b>	<b>21,542</b>
<b>Net income</b>	<b>\$ 31,888</b>	<b>\$ 29,159</b>	<b>\$ 99,720</b>	<b>\$ 107,482</b>
<b>Per share information basic:</b>				

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Income from continuing operations	\$	<b>0.07</b>	\$	0.06	\$	<b>0.21</b>	\$	0.18
Income from discontinued operations	\$	<b>0.00</b>	\$	0.00	\$	<b>0.00</b>	\$	0.04
Net income available to common stockholders	\$	<b>0.07</b>	\$	0.06	\$	<b>0.21</b>	\$	0.22
<b>Per share information diluted:</b>								
Income from continuing operations	\$	<b>0.07</b>	\$	0.06	\$	<b>0.21</b>	\$	0.18
Income from discontinued operations	\$	<b>0.00</b>	\$	0.00	\$	<b>0.00</b>	\$	0.04
Net income available to common stockholders	\$	<b>0.07</b>	\$	0.06	\$	<b>0.21</b>	\$	0.22
<b>Weighted-average common shares outstanding</b>	<b>basic</b>	<b>473,964,303</b>		488,623,792		<b>479,733,105</b>		478,682,376
<b>Weighted-average common shares outstanding</b>	<b>diluted</b>	<b>474,357,292</b>		488,831,780		<b>480,065,677</b>		478,785,990

*See accompanying notes.*

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**PIEDMONT OFFICE REALTY TRUST, INC.**  
**CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY**  
**FOR THE YEAR ENDED DECEMBER 31, 2007**  
**AND FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2008 (UNAUDITED)**

(in thousands, except per share amounts)

	Common Stock		Additional Paid-In Capital	Cumulative Distributions in Excess of Earnings	Redeemable Common Stock	Other Comprehensive Income	Total Stockholders Equity
	Shares	Amount					
<b>Balance, December 31, 2006</b>	465,880	\$ 4,659	\$ 3,358,933	\$ (376,766)	\$ (136,129)		\$ 2,850,697
Issuance of common stock	37,152	371	310,965				311,336
Redemptions of common stock	(14,237)	(142)	(119,165)				(119,307)
Redeemable common stock					(30,680)		(30,680)
Dividends (\$0.5868 per share)				(283,181)			(283,181)
Premium on stock sales			14,728				14,728
Shares issued under the 2007 Omnibus Incentive Plan, net of tax	179	2	3,375				3,377
Other offering costs			(35)				(35)
Net income				133,610			133,610
<b>Balance, December 31, 2007</b>	488,974	4,890	3,568,801	(526,337)	(166,809)		2,880,545
<b>Issuance of common stock</b>	<b>12,928</b>	<b>129</b>	<b>108,200</b>				<b>108,329</b>
<b>Redemptions and purchases of common stock</b>	<b>(26,362)</b>	<b>(264)</b>	<b>(220,653)</b>				<b>(220,917)</b>
Redeemable common stock					79,837		79,837
Dividends (\$0.4401 per share)				(209,606)			(209,606)
Premium on stock sales			2,678				2,678
Shares issued under the 2007 Omnibus Incentive Plan, net of tax	258	3	2,687				2,690
<b>Components of comprehensive income:</b>							
Net income				99,720			99,720
Loss on interest rate swap						(1,045)	(1,045)
<b>Comprehensive income</b>							<b>98,675</b>
<b>Balance, September 30, 2008</b>	<b>475,798</b>	<b>\$ 4,758</b>	<b>\$ 3,461,713</b>	<b>\$ (636,223)</b>	<b>\$ (86,972)</b>	<b>\$ (1,045)</b>	<b>\$ 2,742,231</b>

See accompanying notes.

**Table of Contents****PIEDMONT OFFICE REALTY TRUST, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in thousands)

	(Unaudited) Nine months ended September 30,	
	2008	2007
<b>Cash Flows from Operating Activities:</b>		
Net income	\$ 99,720	\$ 107,482
Operating distributions received from unconsolidated joint ventures	3,572	3,866
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	73,747	71,226
Other amortization	47,164	52,474
Amortization of deferred financing costs and fair market value adjustments on notes payable	1,209	911
Accretion of note receivable discount	(569)	
Stock compensation expense	3,033	2,931
Loss on extinguishment of debt		164
Equity in (loss) income of unconsolidated joint ventures	362	(3,168)
Minority interest in earnings of consolidated entities	430	530
Gain on sale of real estate assets		(20,730)
Changes in assets and liabilities:		
Increase in tenant receivables, net	(4,189)	(13,731)
Increase in prepaid expenses and other assets	(6,796)	(11,684)
Increase in accounts payable, accrued expenses, and accrued capital expenditures	15,920	18,913
Decrease in due to affiliates		(1,232)
Increase (decrease) in deferred income	275	(103)
Net cash provided by operating activities	233,878	207,849
<b>Cash Flows from Investing Activities:</b>		
Investment in real estate and earnest money paid	(105,466)	(45,896)
Cash acquired upon internalization acquisition		1,212
Investment in internalization costs goodwill	(19)	(4,623)
Investment in mezzanine debt	(45,645)	
Investment in corporate tenant improvements	(2,146)	
Net sale proceeds from wholly owned properties		75,492
Net sale proceeds received from unconsolidated joint ventures		4,281
Investments in unconsolidated joint ventures		(613)
Deferred lease costs paid	(17,128)	(15,067)
Net cash (used in) provided by investing activities	(170,404)	14,786
<b>Cash Flows from Financing Activities:</b>		
Deferred financing costs paid	(2,069)	(1,915)
Proceeds from lines of credit and notes payable	701,500	111,450
Repayments of lines of credit and notes payable	(454,009)	(164,441)
Prepayment penalty on extinguishment of debt		(1,617)
Issuance of common stock	108,975	112,603
Redemptions of common stock and private equity purchases	(225,196)	(53,042)
Dividends paid	(209,714)	(210,929)
Other offering costs paid		(28)
Net cash used in financing activities	(80,513)	(207,919)
<b>Net (decrease) increase in cash and cash equivalents</b>	<b>(17,039)</b>	<b>14,716</b>

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<b>Cash and cash equivalents, beginning of period</b>	<b>65,016</b>	44,131
<b>Cash and cash equivalents, end of period</b>	<b>\$ 47,977</b>	\$ 58,847

*See accompanying notes.*

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**PIEDMONT OFFICE REALTY TRUST, INC.**

**CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**September 30, 2008**

**(unaudited)**

**1. Organization**

Piedmont Office Realty Trust, Inc. ( Piedmont ) is a Maryland corporation that operates in a manner so as to qualify as a real estate investment trust ( REIT ) for federal income tax purposes and engages in the acquisition and ownership of commercial real estate properties throughout the United States, including properties that are under construction, are newly constructed, or have operating histories. Piedmont was incorporated in 1997 and commenced operations on June 5, 1998. Piedmont conducts business primarily through Piedmont Operating Partnership, LP ( Piedmont OP ), a Delaware limited partnership. Piedmont is the sole general partner and possesses full legal control and authority over the operations of Piedmont OP. Piedmont OP owns properties directly, through wholly owned subsidiaries, through certain joint ventures with real estate limited partnerships sponsored by its former advisor, and through certain joint ventures with other third parties. References to Piedmont herein shall include Piedmont and all of its subsidiaries, including Piedmont OP, its subsidiaries, and consolidated joint ventures.

As of September 30, 2008, Piedmont owned interests in 84 buildings, either directly or through joint ventures. Piedmont s wholly-owned buildings comprise approximately 21 million square feet of commercial office and industrial space, and are located in 23 states and the District of Columbia. As of September 30, 2008, these wholly-owned buildings were approximately 92% leased.

Since its inception, Piedmont has completed four public offerings of common stock for sale at \$10 per share. Combined with Piedmont s dividend reinvestment plan (the DRP ), such offerings have provided approximately \$5.7 billion in total offering proceeds. From these proceeds, Piedmont has paid costs related to the offerings of (1) approximately \$171.1 million in acquisition and advisory fees and reimbursements of acquisition expenses; (2) approximately \$460.4 million in commissions on stock sales and related dealer-manager fees; and (3) approximately \$62.7 million in organization and other offering costs. In addition, Piedmont has used approximately \$860.2 million to redeem shares pursuant to Piedmont s share redemption program, transact private equity purchases, and in one instance to purchase shares as a result of a legal settlement in October 2004. The remaining net offering proceeds of approximately \$4.1 billion are invested in real estate. Piedmont s fourth public offering closed on July 25, 2004.

Piedmont registered an additional 100 million shares of common stock with the Securities and Exchange Commission (the SEC ) for issuance pursuant to its DRP under a Registration Statement on Form S-3 (Commission File No. 333-114212), which became effective on April 5, 2004. Additionally, Piedmont registered 14.0 million shares of common stock with the SEC for issuance under its 2007 Omnibus Incentive Plan under a Registration Statement on Form S-8 (Commission File No. 333-142448), which became effective on April 30, 2007.

Piedmont s stock is not listed on a national exchange. Piedmont s charter requires Piedmont to begin the process of liquidating its investments and distributing the resulting proceeds to the stockholders if its common stock is not listed on a national securities exchange or over-the-counter market by July 30, 2009 (the Liquidation Date ). The board of directors may, at its sole discretion, further extend the Liquidation Date from July 30, 2009 to January 30, 2011.

**2. Summary of Significant Accounting Policies**

*Basis of Presentation*

The consolidated financial statements of Piedmont have been prepared in accordance with the rules and regulations of the SEC, including the instructions to Form 10-Q and Article 10 of Regulation S-X, and do not include all of the information and footnotes required by U.S. generally accepted accounting principles ( GAAP ) for complete financial statements. In the opinion of management, the statements for the unaudited interim periods presented include all adjustments, which are of a normal and recurring nature, necessary for a fair presentation of the results for such periods. Results for these interim periods are not necessarily indicative of a full year s results. Piedmont s consolidated financial statements include the accounts of Piedmont, Piedmont OP, and certain entities in which Piedmont or Piedmont OP has a controlling financial interest. For further information, refer to the financial statements and footnotes included in Piedmont s Annual Report on Form 10-K for the year ended

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December 31, 2007.

### *Redeemable Common Stock*

Subject to certain limitations, shares of Piedmont's common stock are contingently redeemable at the option of the stockholder. Such limitations include, but are not limited to, the following: (i) Piedmont may not redeem during any calendar year in excess of 5% of the weighted-average common shares outstanding during the prior calendar year; and (ii) in no event shall the life-to-date aggregate amount paid for redemptions under the Piedmont share redemption program exceed the life-to-date aggregate amount of proceeds received from the sale of shares pursuant to the DRP. Accordingly, Piedmont has recorded redeemable common stock equal to the aggregate amount of proceeds received under the DRP, less the aggregate amount incurred to redeem shares under Piedmont's share redemption program of approximately \$87.0 million and \$166.8 million as of September 30, 2008 and December 31, 2007,

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respectively. Further, upon being tendered for redemption by the holder, Piedmont reclassifies redeemable common shares from mezzanine equity to a liability at settlement value. As of September 30, 2008 and December 31, 2007, respectively, approximately \$0 and \$6.0 million of shares tendered for redemption have not been redeemed, and are, therefore, included in accounts payable, accrued expenses, and accrued capital expenditures in the accompanying consolidated balance sheets.

### *Income Taxes*

Piedmont has elected to be taxed as a REIT under the Internal Revenue Code of 1986, as amended (the Code), and has operated as such, beginning with its taxable year ended December 31, 1998. To qualify as a REIT, Piedmont must meet certain organizational and operational requirements, including a requirement to distribute at least 90% of its annual REIT taxable income. As a REIT, Piedmont is generally not subject to federal income taxes. Accordingly, neither a provision nor a benefit for federal income taxes has been made in the accompanying consolidated financial statements. Piedmont is subject to certain state and local taxes related to the operations of properties in certain locations, which have been provided for in the consolidated financial statements.

### *Investment in Mezzanine Debt*

FIN 46R, a modification of FIN No. 46, *Consolidation of Variable Interest Entities*, clarified the methodology for determining whether an entity is a Variable Interest Entity (VIE) and the methodology for assessing who is the primary beneficiary of a VIE. VIEs are defined as entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. If an entity is determined to be a VIE, it must be consolidated by the primary beneficiary. The primary beneficiary is the enterprise that absorbs the majority of the entity's expected losses, receives a majority of the entity's expected residual returns, or both. Generally, expected losses and expected residual returns are the expected negative and positive variability, respectively, in the fair value of the VIE's net assets.

When Piedmont makes an investment, it assesses whether it has a variable interest in a VIE and, if so, whether it is the primary beneficiary of the VIE. These analyses require considerable judgment in determining the primary beneficiary of a VIE since they involve subjective probability weighting of various cash flow scenarios. Incorrect assumptions or estimates of future cash flows may result in an inaccurate determination of the primary beneficiary. The result could be the consolidation of an entity acquired or formed in the future that would otherwise not have been consolidated or the nonconsolidation of such an entity that would otherwise have been consolidated.

Piedmont has evaluated its investment in mezzanine debt to determine whether it has variable interests in a VIE. For this investment, Piedmont has evaluated the sufficiency of the entities' equity investment at risk to absorb expected losses, and whether as a group, the equity has the characteristics of a controlling financial interest. Piedmont has determined that its investment in mezzanine debt is a variable interest in a VIE and Piedmont is the primary beneficiary. However, Piedmont has determined that the special-purpose entity that holds the debt (the Borrowing Entity) is not the primary beneficiary of the other VIEs in the overall property debt structure. The primary effect of these determinations is that Piedmont consolidates the Borrowing Entity (i.e., reflects the note receivable, discount on note receivable, interest income, and amortization of the discount on note receivable related to this investment in its consolidated financial statements) but does not consolidate the assets, liabilities, or operations of the other VIEs in the overall property debt structure.

Piedmont's maximum exposure to loss as a result of its investment in mezzanine debt is \$46.2 million as of September 30, 2008.

### *Interest Rate Swap*

Piedmont has entered into an interest rate swap agreement to hedge its exposure to changing interest rates on one of its variable rate debt instruments (see Note 6). As required by Statement of Financial Accounting Standards (SFAS) No. 133, *Accounting for Derivative Instruments and Hedging Activities* (SFAS 133), Piedmont records all derivatives on the balance sheet at fair value. Piedmont reassesses the effectiveness of its derivatives designated as cash flow hedges on a regular basis to determine if they continue to be highly effective and also to determine if the forecasted transactions remain highly probable. The changes in fair value of derivatives designated as cash flow hedges are recorded in other comprehensive income (OCI), and the amounts in OCI will be reclassified to earnings when the hedged transactions occur. Changes in the fair values of derivatives designated as cash flow hedges that do not qualify for hedge accounting treatment are recorded as gain/(loss) on interest rate swap in the consolidated statements of income. The fair value of the interest rate swap agreement is recorded as prepaid expenses and other assets or as interest rate swap liability in the accompanying consolidated balance sheets. Amounts received or paid under interest rate swap agreements are also recorded as gain/(loss) on interest rate swap in the consolidated income statements as incurred. Currently, Piedmont does not use derivatives for trading or speculative purposes and does not have any derivatives that are not designated as cash flow hedges.

### *Reclassifications*

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Certain prior period amounts have been reclassified to conform to the current period financial statement presentation.

**Table of Contents***Recent Accounting Pronouncements*

On October 10, 2008, the Financial Accounting Standards Board ( FASB ) issued Staff Position No. SFAS 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset is Not Active* ( FSP 157-3 ). FSP 157-3 includes guidance for how companies should value illiquid assets under the fair value accounting method prescribed in SFAS No. 157, *Fair Value Measurements* ( SFAS 157 ), but does not change any of the provisions of SFAS 157. FSP 157-3 is effective upon issuance; however, retrospective application is prohibited. Piedmont does not expect the provisions of FSP 157-3 will have a material effect on its consolidated financial statements.

In May 2008, the FASB issued SFAS No. 162, *The Hierarchy of Generally Accepted Accounting Principles* ( SFAS 162 ). SFAS 162 identifies the sources of accounting principles and the hierarchy to be used in selecting the principles to be used in the preparation of financial statements that are presented in conformity with GAAP. SFAS 162 is effective on November 15, 2008. Piedmont will continue to adopt the GAAP hierarchy prescribed by SFAS 162 in the preparation of its consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities – an amendment to FASB Statement No. 133* ( SFAS 161 ). SFAS 161 requires enhanced disclosures about an entity’s derivative and hedging activities, improving the transparency of financial reporting. The enhanced disclosures include descriptions of how and why the entity uses derivative instruments, how such instruments are accounted for under FASB Statement No. 133, and how derivative instruments affect the entity’s financial position, operations, and cash flows. SFAS 161 will be effective for Piedmont beginning January 1, 2009, with early adoption encouraged. Piedmont does not expect the provisions of SFAS 161 will have a material effect on its consolidated financial statements.

In February 2008, the FASB issued Staff Position No. SFAS 157-2, *Effective Date of FASB Statement No. 157* ( FSP 157-2 ). FSP 157-2 delays the effective date of SFAS 157, for all nonrecurring, nonfinancial assets and liabilities until fiscal years beginning after November 15, 2008. Accordingly, FSP 157-2 will be effective for Piedmont beginning January 1, 2009. Piedmont will continue to assess the provisions and evaluate the financial statement impact of SFAS 157-2 on its consolidated financial statements. However, Piedmont has adopted the other aspects of SFAS 157 which are not excluded by FSP 157-2 for its financial assets and liabilities effective beginning January 1, 2008. SFAS 157 defines fair value, establishes a framework for fair value, and expands disclosures required for fair value measurements under GAAP.

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements* ( SFAS 160 ). SFAS 160 requires that noncontrolling interests should be reported as an element of consolidated equity, thus eliminating the practice of classifying minority interests within a mezzanine section of the balance sheet. SFAS 160 also requires that net income encompass the total income of all consolidated subsidiaries with an additional separate disclosure on the face of the income statement of the attribution of that income between the controlling and noncontrolling interests. All increases and decreases in the noncontrolling ownership interest amount will be accounted for as equity transactions. SFAS 160 will be effective for Piedmont beginning January 1, 2009. Piedmont will continue to assess the provisions and evaluate the financial statement impact of SFAS 160 on its consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141R, *Business Combinations* ( SFAS 141R ). SFAS 141R requires, among other things, that transaction costs incurred in business combinations, including acquisitions of real estate assets which qualify as a business, be expensed as incurred by the acquirer. Preacquisition contingencies, such as environmental or legal issues, as well as contingent consideration, will generally be accounted for in purchase accounting at fair value. SFAS 141R is effective January 1, 2009. Piedmont expects the provisions of SFAS 141R, to the extent it enters into material acquisition activity in 2009, to have a material financial statement impact on its consolidated financial statements.

In June 2007, the American Institute of Certified Public Accountants ( AICPA ) issued Statement of Position ( SOP ) 07-1, *Clarification of the Scope of the Audit and Accounting Guide – Investment Companies and Accounting by Parent Companies and Equity Method Investors for Investments in Investment Companies*, which provides guidance for determining which entities fall within the scope of the AICPA Audit and Accounting Guide for Investment Companies and requires additional disclosures for certain of those entities. The effective date of SOP 07-1 has been deferred indefinitely by the FASB. Piedmont will continue to assess the provisions and evaluate the financial statement impact of SOP 07-1 on its consolidated financial statements.

**3. Investment in Mezzanine Debt**

On March 19, 2008, Piedmont invested \$45.6 million in mezzanine debt of an entity which is generally secured by a pledge of the equity interest of the entity owning a 46-story, Class A, commercial office building located in downtown Chicago. Piedmont’s interest is subordinate to the mortgage loan secured by the office building as well as subordinate to the interests of two other mezzanine lenders. The note matures on August 9, 2009 (with three one-year extension options exercisable at the borrower’s discretion) and bears interest at a floating rate of LIBOR plus

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1.61%. The purchase of the mezzanine debt resulted in a discount which will be amortized to interest income over the life of the loan using the straight-line method, which materially approximates the effective interest method. Such income, in addition to interest income received through borrower loan repayments, is recognized as interest income in the consolidated financial statements. Piedmont recognized such interest income of \$0.8 million and \$1.7 million for the three and nine months ended September 30, 2008, respectively.

**Table of Contents****4. Impairment of Real Estate Assets**

During the third quarter 2008, Piedmont, in conjunction with its other joint venture partners, reduced its intended holding period for the 20/20 Building, which is owned by Fund XI-XII-REIT Joint Venture. The 20/20 Building was purchased in July 1999 and consists of one, three-story office building located in Leawood, KS totaling approximately 70,000 square feet. Piedmont, through its investment in Fund XI-XII-REIT, owns approximately 57% of the 20/20 Building.

Based on a comparison of the projected undiscounted future cash flows and the net book value of the asset, Piedmont and its joint venture partners determined that the carrying value of the asset was not recoverable, and Piedmont recorded an impairment loss on real estate assets in the amount of approximately \$2.1 million (Piedmont's percentage of the impairment charge) during the three months ended September 30, 2008. The estimated fair value of the asset was determined based upon the present value of discounted cash flows. The impairment charge is recorded with other net operations of the property as equity in loss of unconsolidated joint ventures in the accompanying consolidated statements of income, and as a reduction to the investment in unconsolidated joint ventures in the accompanying consolidated balance sheets.

**5. Dispositions of Real Estate Assets***Discontinued Operations*

The results of operations for the Citigroup Fort Mill Building (sold in March 2007) and the Videojet Technology Building (sold in March 2007) are classified as discontinued operations in the accompanying consolidated statements of income. The details comprising income from discontinued operations are provided below (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
<b>Revenues:</b>				
Rental income	\$	\$ (1)	\$ 10	\$ 1,259
Tenant reimbursements		(210)		(401)
Gain on sale		10		20,680
		(201)	10	21,538
<b>Expenses:</b>				
Property operating costs		(230)		(396)
Depreciation				311
Amortization				41
General and administrative		13		40
		(217)		(4)
<b>Income from discontinued operations</b>	<b>\$</b>	<b>\$ 16</b>	<b>\$ 10</b>	<b>\$ 21,542</b>

**Table of Contents****6. Line of Credit and Notes Payable**

As of September 30, 2008 and December 31, 2007, Piedmont had a line of credit and notes payable outstanding as follows (in thousands):

Facility	Fixed-rate (F) or Variable rate (V)	Rate	Term Debt or Interest Only	Maturity	Amount Outstanding as of	
					September 30, 2008	December 31, 2007
Secured Pooled Facility	F	4.84%	Interest Only	6/14/2014	\$ 350,000	\$ 350,000
Aon Center Chicago Mortgage Notes	F	4.87%	Interest Only	5/1/2014	200,000	200,000
	F	5.70%	Interest Only	5/1/2014	25,000	25,000
\$125.0 Million Fixed-Rate Loan	F	5.50%	Interest Only	4/1/2016	125,000	125,000
35 W. Wacker Building Mortgage Note	F	5.10%	Interest Only	1/1/2014	120,000	120,000
WDC Mortgage Notes	F	5.76%	Interest Only	11/1/2017	140,000	140,000
\$105.0 Million Fixed-Rate Loan	F	5.29%	Interest Only	5/11/2015	105,000	105,000
\$45.0 Million Fixed-Rate Loan	F	5.20%	Interest Only	6/1/2012	45,000	45,000
\$42.5 Million Fixed-Rate Loan	F	5.70%	Interest Only	10/11/2016	42,525	42,525
3100 Clarendon Boulevard Building Mortgage Note	F	6.40%	Interest Only	8/25/2008		33,896
One Brattle Square Building Mortgage Note	F	8.50%	Term Debt	3/11/2028		26,109
\$250 Million Term Loan		3.93% <sup>(2)</sup>	Term Debt	6/28/2010	250,000	
	V <sup>(1)</sup>	LIBOR + 1.50%				
\$500 Million Unsecured Facility	V	3.27% <sup>(3)</sup>	Interest Only	8/31/2011	146,100	89,000
<b>Total indebtedness</b>					<b>\$ 1,548,625</b>	<b>\$ 1,301,530</b>

<sup>(1)</sup> \$250 Million Term Loan has a stated variable rate; however, Piedmont entered into an interest rate swap which effectively fixes the rate on this facility to 4.97% as of September 30, 2008.

<sup>(2)</sup> Represents 30-day LIBOR rate as of September 30, 2008.

<sup>(3)</sup> Rate is equal to the weighted-average interest rate on all outstanding draws as of September 30, 2008. Piedmont may select from multiple interest rate options with each draw, including the prime rate and various length LIBOR locks. All selections are subject to an additional spread over the selected rate based on Piedmont's current credit rating (0.475% as of September 30, 2008).

During the nine months ended September 30, 2008, Piedmont's net borrowings under its \$500 Million Unsecured Facility totaled approximately \$57.1 million, including a draw to repay in full the balance outstanding at maturity of the 3100 Clarendon Boulevard Building Mortgage Note on August 25, 2008. Piedmont made interest payments on all debt facilities totaling approximately \$19.7 million and \$15.0 million for the three months ended September 30, 2008 and 2007, respectively and \$53.6 million and \$46.9 million for the nine months ended September 30, 2008 and 2007, respectively. Piedmont had no capitalized interest for the nine months ended September 30, 2008 or 2007.

*Interest Rate Swap Valuation*

Piedmont's interest rate swap has been designated as a hedge of the variability in expected future cash flows on the \$250 Million Term Loan. Piedmont's objective in using this interest rate derivative is to add stability to interest expense and to manage its exposure to interest rate movements or other identified risks that currently exist. The valuation of this instrument is determined using widely accepted valuation techniques including discounted cash flow analysis on the expected cash flows of this derivative. This analysis reflects the contractual terms of the derivative, including the period to maturity, and uses observable market-based inputs, including interest rate curves and implied volatilities.

To comply with the provisions of SFAS 157, Piedmont incorporates credit valuation adjustments to appropriately reflect both its own nonperformance risk and the respective counterparty's nonperformance risk in the fair value measurement. In adjusting the fair value of its derivative contract for the effect of nonperformance risk, Piedmont has considered the impact of netting and any applicable credit enhancements,

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such as collateral postings, thresholds, mutual puts, and guarantees.

Although Piedmont has determined that the majority of the inputs used to value its derivative falls within Level 2 of the fair value hierarchy, the credit valuation adjustment associated with its derivative utilizes Level 3 inputs, such as estimates of current credit spreads to evaluate the likelihood of default by itself and its counterparty. However, as of September 30, 2008, Piedmont has assessed the significance of the impact of the credit valuation adjustment on the overall valuation of its derivative position and has determined that the credit valuation adjustment is not significant to the overall valuation of its derivative. As a result, Piedmont has determined that its derivative valuation in its entirety is classified in Level 2 of the fair value hierarchy.

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The table below presents Piedmont's liability measured at fair value on a recurring basis as of September 30, 2008, aggregated by the level in the fair value hierarchy within which those measurements fall (in thousands):

	Quoted Prices in Active Markets for Identical Assets and Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at September 30, 2008
<b>Liabilities</b>				
Derivative financial instruments	\$	\$ 1,045	\$	\$ 1,045

**7. Supplemental Disclosures of Noncash Investing and Financing Activities**

Outlined below are significant noncash investing and financing activities for the nine months ended September 30, 2008 and 2007 (in thousands):

	Nine months ended September 30, (in thousands)	
	2008	2007
Acquisition of Piedmont's former advisor in exchange for common stock	\$	\$ 175,000
Transfer of common stock to Piedmont's former advisor in exchange for partnership units	\$	\$ 200
Investment in goodwill funded with other assets	\$	\$ 1,504
Accrued goodwill costs	\$	\$ 65
Liabilities assumed upon acquisition of Piedmont's former advisor	\$	\$ 1,264
Liabilities assumed at property acquisition	\$	\$ 667
Accrued redemptions of common stock	\$ (5,969)	\$ (825)
Accrued capital expenditures and deferred lease costs	\$ 6,191	\$ 3,571
Discounts applied to issuance of common stock	\$ 646	\$ 13,197
Discounts reduced as a result of redemptions and purchases of common stock	\$ 1,690	\$ 269
Redeemable common stock	\$ 79,837	\$ (60,146)

**8. Agreements with Former Advisor Companies**

For the period from January 1, 2007 through April 16, 2007, Piedmont incurred expenses under the following agreements with Piedmont's former advisor and its affiliates. On April 16, 2007, Piedmont closed the transaction to internalize the functions of its former external advisor companies and became a self-managed entity (the "Internalization"). Such agreements were terminated as part of the Internalization. The expenses incurred under the agreements for the periods presented are described below (in thousands):

Agreement	Services Provided	Expense Incurred for the Three Months Ended		Expense Incurred for the Nine Months Ended	
		September 30, 2008	September 30, 2007	September 30, 2008	September 30, 2007
<i>Asset Advisory Agreement</i>	Manage day-to-day operations; administer, promote, operate, maintain, improve, finance, lease, dispose of properties; provide accounting, compliance, other administrative services				\$ 7,046
<i>Property Management Agreement</i>			\$		\$ 1,406

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	Manage properties; coordinate leasing of properties; manage construction activities at certain properties.		
<i>Administrative reimbursements (pursuant to agreements listed above)</i>	Piedmont was required to reimburse each service provider for various expenses incurred in connection with the performance of its duties	\$	\$ 3,048 <sup>(1)</sup>

<sup>(1)</sup> Includes approximately \$795,000 which was reimbursed by tenants pursuant to the respective lease agreements.

**Table of Contents***Agreements with Former Advisor Companies Post Internalization*

During the three and nine months ended September 30, 2008 and 2007, Piedmont incurred expenses and earned revenues under the following agreements with Piedmont's former advisor and its affiliates (in thousands):

Agreement	Services Provided	Fees Incurred / (Revenues Earned) for the Three Months Ended		Fees Incurred / (Revenues Earned) for the Nine Months Ended		Termination Date	Renewal Options
		September 30, 2008	September 30, 2007	September 30, 2008	September 30, 2007		
<i>Property Management</i>	Manage day-to-day	\$ 265	\$ 302	\$ 1,089	\$ 611	April 1, 2009	Automatically renews
<i>Services Piedmont-Owned Properties</i>	operations including accounting					Terminated agreement as it	unless either party gives 60 day notice
<i>Managed by Former Advisor</i>	services for 10 properties					relates to 7 of the 17 properties, effective July 1, 2008	of intent not to renew
<i>Property Management</i>	Manage day-to-day	\$ (726)	\$ (668)	\$ (2,215)	\$ (1,097)	April 16, 2009	Automatically renews
<i>Services Properties</i>	operations including accounting						unless either party
<i>Owned by Real Estate</i>	services for 22						gives 60 day notice
<i>Programs Sponsored by Former Advisor</i>	properties						of intent not to renew
<i>Managed by Piedmont</i>							
<i>Transition Services Agreement</i>	Investor relations support services; transfer agent-related services; investor communication support	\$ 428	\$ 550	\$ 1,528	\$ 1,002	April 15, 2009 Terminated investor communication support portion of agreement effective July 1, 2008	Automatically renews for successive 180-day periods unless otherwise terminated upon 30 days written notice
<i>Headquarters</i>	Office space located at	\$	\$	77	\$ 153	\$ 141	Terminated as of July 1, 2008
<i>Sublease Agreement</i>	6200 The Corners Parkway, Norcross, Ga., along with furniture, fixtures,						

and equipment

<i>Support Services</i>	Information technology	\$ 27	\$ 221	\$ 484	\$ 397	Terminated as of July 1, 2008
<i>Agreement</i>	services					

**9. Commitments and Contingencies**

*Commitments Under Existing Lease Agreements*

Certain lease agreements include provisions that, at the option of the tenant, may obligate Piedmont to provide funding for capital improvements. Under existing lease agreements, the principal tenants at the 35 W. Wacker Building, are entitled to additional landlord-funded tenant improvements, leasing commissions, and building improvements, totaling approximately \$52.6 million as of September 30, 2008.

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### *Contingencies Related to Tenant Audits*

Certain lease agreements include provisions that grant tenants the right to engage independent auditors to audit their annual operating expense reconciliations. Such audits may result in the re-interpretation of language in the lease agreements which could result in the refund of previously recognized tenant reimbursement revenues, resulting in financial loss to Piedmont.

### *Assertion of Legal Action*

*In Re Wells Real Estate Investment Trust, Inc. Securities Litigation, Civil Action No. 1:07-cv-00862-CAP* (Upon motions to dismiss filed by defendants, parts of all seven counts were dismissed by the court. Counts III through VII were dismissed in their entirety. A motion for class certification has been filed and the parties are engaged in discovery.)

On March 12, 2007, a stockholder filed a purported class action and derivative complaint in the United States District Court for the District of Maryland against, among others, Piedmont, Piedmont's previous advisors, and the officers and directors of Piedmont prior to the closing of the Internalization. The complaint attempts to assert class action claims on behalf of those persons who received and were entitled to vote on the proxy statement filed with the SEC on February 26, 2007.

The complaint alleges, among other things, (i) that the consideration to be paid as part of the Internalization is excessive; (ii) violations of Section 14(a), including Rule 14a-9 thereunder, and Section 20(a) of the Exchange Act, based upon allegations that the proxy statement contains false and misleading statements or omits to state material facts; (iii) that the board of directors and the current and previous advisors breached their fiduciary duties to the class and to Piedmont; and (iv) that the proposed Internalization will unjustly enrich certain directors and officers of Piedmont.

The complaint seeks, among other things, (i) certification of the class action; (ii) a judgment declaring the proxy statement false and misleading; (iii) unspecified monetary damages; (iv) to nullify any stockholder approvals obtained during the proxy process; (v) to nullify the merger proposal and the merger agreement; (vi) restitution for disgorgement of profits, benefits, and other compensation for wrongful conduct and fiduciary breaches; (vii) the nomination and election of new independent directors, and the retention of a new financial advisor to assess the advisability of Piedmont's strategic alternatives; and (viii) the payment of reasonable attorneys' fees and experts' fees.

On June 27, 2007, the plaintiff filed an amended complaint, which contains the same counts as the original complaint, described above, with amended factual allegations based primarily on events occurring subsequent to the original complaint and the addition of a Piedmont officer as an individual defendant.

On March 31, 2008, the court granted in part the defendants' motion to dismiss the amended complaint. The court dismissed five of the seven counts of the amended complaint in their entirety. The court dismissed the remaining two counts with the exception of allegations regarding the failure to disclose in Piedmont's proxy statement details of certain expressions of interest in acquiring Piedmont. On April 21, 2008, the plaintiff filed a second amended complaint, which alleges violations of the federal proxy rules based upon allegations that the proxy statement to obtain approval for Internalization omitted details of certain expressions of interest in acquiring Piedmont. The second amended complaint seeks, among other things, unspecified monetary damages, to nullify and rescind Internalization, and to cancel and rescind any stock issued to the defendants as consideration for Internalization. On May 12, 2008, the defendants answered the second amended complaint.

On June 23, 2008, the plaintiff filed a motion for class certification. As of the date of this filing, the time for the defendants to respond to plaintiff's motion for class certification has not yet passed. The parties are presently engaged in discovery.

Piedmont believes that the allegations contained in the complaint are without merit and will continue to vigorously defend this action. Due to the uncertainties inherent in the litigation process, it is not possible to predict the ultimate outcome of this matter at this time; however, as with any litigation, the risk of financial loss does exist.

*In Re Piedmont Office Realty Trust, Inc. Securities Litigation, Civil Action No. 1:07-cv-02660-CAP* (Defendants have filed a motion to dismiss the amended complaint.)

On October 25, 2007, the same stockholder mentioned above filed a second purported class action in the United States District Court for the Northern District of Georgia against Piedmont and its board of directors. The complaint attempts to assert class action claims on behalf of (i) those persons who were entitled to tender their shares pursuant to the tender offer filed with the SEC by Lex-Win Acquisition LLC on May 25, 2007, and (ii) all persons who are entitled to vote on the proxy statement filed with the SEC on October 16, 2007.

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The complaint alleges, among other things, violations of the federal securities laws, including Sections 14(a) and 14(e) of the Exchange Act and Rules 14a-9 and 14e-2(b) promulgated thereunder. In addition, the complaint alleges that defendants have also breached their fiduciary duties owed to the proposed classes.

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On December 26, 2007, the plaintiff filed a motion seeking that the court designate it as lead plaintiff and its counsel as class lead counsel, which the court granted on May 2, 2008.

On May 19, 2008, the lead plaintiff filed an amended complaint which contains the same counts as the original complaint. On June 30, 2008, defendants filed a motion to dismiss the amended complaint. The court has not yet ruled on the motion to dismiss.

Piedmont believes that the allegations contained in the complaint are without merit and will continue to vigorously defend this action. Due to the uncertainties inherent in the litigation process, it is not possible to predict the ultimate outcome of this matter at this time; however, as with any litigation, the risk of financial loss does exist.

*Donald and Donna Goldstein, Derivatively on behalf of Nominal Defendant Piedmont Office Realty Trust, Inc. v. Leo F. Wells, III, et al.* (Defendant's motion to dismiss granted plaintiffs filed a notice to appeal)

On August 24, 2007, two stockholders of Piedmont filed a putative shareholder derivative complaint in the Superior Court of Fulton County, State of Georgia, on behalf of Piedmont against, among others, one of Piedmont's previous advisors, and a number of Piedmont's current and former officers and directors.

The complaint alleges, among other things, (i) that the consideration paid as part of the Internalization of Piedmont's previous advisors was excessive; (ii) that the defendants breached their fiduciary duties to Piedmont; and (iii) that the Internalization transaction unjustly enriched the defendants.

The complaint seeks, among other things, (i) a judgment declaring that the defendants have committed breaches of their fiduciary duties and were unjustly enriched at the expense of Piedmont; (ii) monetary damages equal to the amount by which Piedmont has been damaged by the defendants; (iii) an order awarding Piedmont restitution from the defendants and ordering disgorgement of all profits and benefits obtained by the defendants from their wrongful conduct and fiduciary breaches; (iv) an order directing the defendants to respond in good faith to offers which are in the best interest of Piedmont and its stockholders and to establish a committee of independent directors or an independent third party to evaluate strategic alternatives and potential offers for Piedmont, and to take steps to maximize Piedmont's and the stockholders' value; (v) an order directing the defendants to disclose all material information to Piedmont's stockholders with respect to the Internalization transaction and all offers to purchase Piedmont and to adopt and implement a procedure or process to obtain the highest possible price for the stockholders; (vi) an order rescinding, to the extent already implemented, the Internalization transaction; (vii) the establishment of a constructive trust upon any benefits improperly received by the defendants as a result of their wrongful conduct; and (viii) an award to the plaintiffs of costs and disbursements of the action, including reasonable attorneys' and experts' fees.

On March 13, 2008, the court granted the motion to dismiss this complaint. However, on April 11, 2008, the plaintiffs filed a notice to appeal the court's judgment granting the defendants' motion to dismiss. The appeal is currently pending in the Court of Appeals of Georgia.

### *Other Legal Matters*

Piedmont is from time to time a party to other legal proceedings, which arise in the ordinary course of its business. None of these ordinary course legal proceedings are reasonably likely to have a material adverse effect on results of operations or financial condition.

## **10. Stock-Based Compensation**

### *Deferred Stock Award Grant*

On April 21, 2008, pursuant to the 2007 Omnibus Incentive Plan, Piedmont granted approximately 451,782 shares of common stock as deferred stock awards to its employees, of which 20,695 shares were surrendered immediately to satisfy required minimum tax withholding obligations. Of the shares granted, approximately 112,942 shares (or 25%) vested immediately and the remaining shares, adjusted for any forfeitures, vest ratably on the anniversary date over the following three years. Piedmont estimated the fair value of the awards on the date of grant based on an assumed share price of \$8.70 per share reduced by the present value of dividends expected to be paid on the unvested portion of the shares discounted at the appropriate risk-free interest rate. As of September 30, 2008, 337,977 shares remained unvested.

On May 18, 2007, pursuant to the 2007 Omnibus Incentive Plan, Piedmont granted approximately 764,850 shares of common stock as deferred stock awards to its employees, of which 19,988 shares were surrendered immediately to satisfy required minimum tax withholding obligations.

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Of the shares granted, approximately 191,215 shares (or 25%) vested immediately. On May 18, 2008, approximately 185,952 shares vested, of which 62,678 shares were surrendered immediately to satisfy required minimum tax withholding obligations. The remaining shares, adjusted for any forfeitures, vest ratably on the anniversary date over the next two years. Piedmont estimated the fair value of the awards on the date of grant based on an assumed share price of \$10.00 per share reduced by the present value of dividends expected to be paid on the unvested portion of the shares discounted at the appropriate risk-free interest rate. As of September 30, 2008, 369,770 shares remained unvested.

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During the three months ended September 30, 2008 and 2007, Piedmont recognized approximately \$0.7 million of compensation expense related to restricted stock awards, all of which relates to the amortization of nonvested shares. During the nine months ended September 30, 2008 and 2007, Piedmont recognized approximately \$3.4 million and \$3.0 million of compensation expense, respectively, of which \$2.4 million and \$1.1 million, respectively, relates to the nonvested shares. As of September 30, 2008, approximately \$2.7 million of unrecognized compensation cost related to nonvested share-based compensation remained, which Piedmont will record in its statements of income over a weighted-average vesting period of approximately 2.5 years.

**11. Weighted-Average Common Shares**

There are no adjustments to Net income or Income from continuing operations for the diluted earnings per share computations.

The following table reconciles the denominator for the basic and diluted earnings per share computations shown on the consolidated statements of income (in thousands):

	Three Months Ended September 30, 2008		Nine Months Ended September 30, 2008	
	2008	2007	2008	2007
Weighted-average common shares basic	473,964	488,624	479,733	478,682
Plus incremental weighted-average shares from time-vested conversions:				
Restricted stock awards	393	208	333	104
Weighted-average common shares diluted	474,357	488,832	480,066	478,786

**12. Equity Transactions***Private Equity Purchase*

On August 6, 2008, Piedmont purchased 3,909,701 shares owned collectively by Lex-Win Acquisition LLC and its affiliates (the Sellers) for a purchase price of \$8.31 per share, and on August 21, 2008, Piedmont purchased an additional 750 shares owned by the Sellers for a purchase price of \$8.31 per share. These purchases represent the entire balance of common stock of Piedmont owned by the Sellers. The purchase agreement contained customary representations and warranties by the Sellers, a standstill provision enforceable against the Sellers, and mutual non-disparagement provisions.

*Escrowed Shares Approved to be Released*

Of the original 19,546,302 shares of Piedmont's common stock issued as consideration for the Internalization, 162,706 shares (approximately 0.8%) were placed in escrow. On September 17, 2008, the board of directors of Piedmont approved a resolution to release 130,054 shares of the total 162,706 shares of such common stock to Wells Advisory Services I, LLC (WASI) from the escrow account established at the closing of the Internalization. The release of such shares was subject to a calculation to determine a certain minimum level of projected earnings as a result of our managing properties after the Internalization. This calculation was performed by management, reviewed by an independent third-party advisor, and agreed to by both parties. The remaining 32,652 shares held in escrow will be returned to Piedmont. Further, dividend income received on these shares during the period they were held in escrow will be distributed to WASI or returned to Piedmont pro-rata based on each party's allocated shares.

**13. Subsequent Events***Declaration of Dividend for the Fourth Quarter 2008*

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On November 13, 2008, the board of directors of Piedmont declared dividends for the fourth quarter 2008 in the amount of \$0.1467 (14.67 cents) per share on the outstanding common shares of Piedmont to all stockholders of record of such shares as shown on the books of Piedmont at the close of business on December 15, 2008. Such dividends are to be paid on such date during the month of December 2008 as the President of Piedmont may determine.

### *Suspension of Share Redemption Program*

On November 13, 2008, the board of directors of Piedmont suspended redemptions under the share redemption program effective as of January 1, 2009. This action was taken in response to the current volatile market conditions and the resulting uncertainty as to their impact on asset values and is intended to treat all shareholders equitably. The share redemption program will remain suspended in its entirety until the annual estimation of net asset value of shares of Piedmont is completed on or about March 31, 2009. At that time, the board of directors will determine the terms under which the share redemption program may be reinstated.

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

The following discussion and analysis should be read in conjunction with the accompanying consolidated financial statements and notes thereto of Piedmont Office Realty Trust, Inc. ( Piedmont ). See also Cautionary Note Regarding Forward-Looking Statements preceding Part I, as well as the notes to our consolidated financial statements and Management's Discussion and Analysis of Financial Condition and Results of Operations included in our Annual Report on Form 10-K for the year ended December 31, 2007.

**Liquidity and Capital Resources**

As of September 30, 2008, Piedmont had outstanding borrowings of approximately \$146.1 million on the \$500 Million Unsecured Facility. Along with outstanding letters of credit totaling approximately \$0.4 million, we had approximately \$353.5 million available for future borrowing.

We intend to use cash flows generated from operation of our properties, proceeds from our dividend reinvestment plan, and proceeds from our \$500 Million Unsecured Facility, as our primary sources of immediate and long-term liquidity. In addition, we expect distributions from our existing unconsolidated joint ventures and the potential selective disposal of existing properties to provide additional sources of funds.

We anticipate that our primary future capital requirements will include, but not be limited to, making scheduled debt service payments and funding renovations, expansions, and other significant capital improvements for our existing portfolio of properties. Over the next few years, we anticipate funding significant capital expenditures for the properties currently in our portfolio. These expenditures include specifically identified building improvement projects (including amounts set forth in the Contractual Commitments and Contingencies table below), as well as projected amounts for tenant improvements and leasing commissions related to projected re-leasing, which are subject to change as market and tenant conditions