HIGHWOODS PROPERTIES INC
Form 10-Q
October 28, 2010

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

FORM 10-Q

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

For the quarterly period ended September 30, 2010

HIGHWOODS PROPERTIES, INC.
(Exact name of registrant as specified in its charter)

Maryland (State or other jurisdiction of incorporation or organization)	001-13100 (Commission File Number)	56-1871668 (I.R.S. Employer Identification Number)

HIGHWOODS REALTY LIMITED PARTNERSHIP
(Exact name of registrant as specified in its charter)

North Carolina (State or other jurisdiction of incorporation or organization)	000-21731 (Commission File Number)	56-1869557 (I.R.S. Employer Identification Number)

3100 Smoketree Court, Suite 600
Raleigh, NC 27604
(Address of principal executive offices) (Zip Code)

919-872-4924
(Registrants' telephone number, including area code)

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.

Highwoods Properties, Inc. Yes S No £ Highwoods Realty Limited Partnership Yes S 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).

Highwoods Properties, Inc. Yes S No £ Highwoods Realty Limited Partnership 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 Securities Exchange Act.

Highwoods Properties, Inc.
Large accelerated filer S Accelerated filer £ Non-accelerated filer £ Smaller reporting company £

Highwoods Realty Limited Partnership
Large accelerated filer £ Accelerated filer £ Non-accelerated filer S Smaller reporting company £

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

Highwoods Properties, Inc. Yes £ No S Highwoods Realty Limited Partnership Yes £ No S

The Company had 71,658,232 shares of Common Stock outstanding as of October 21, 2010.

HIGHWOODS PROPERTIES, INC.
HIGHWOODS REALTY LIMITED PARTNERSHIP

QUARTERLY REPORT FOR THE PERIOD ENDED SEPTEMBER 30, 2010

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

We refer to Highwoods Properties, Inc. as the “Company,” Highwoods Realty Limited Partnership as the “Operating Partnership,” the Company’s common stock as “Common Stock” or “Common Shares,” the Company’s preferred stock as “Preferred Stock” or “Preferred Shares,” the Operating Partnership’s common partnership interests as “Common Units,” the Operating Partnership’s preferred partnership interests as “Preferred Units” and in-service properties (excluding rental residential units) to which the Company and/or the Operating Partnership have title and 100.0% ownership rights as the “Wholly Owned Properties.” References to “we” and “our” mean the Company and the Operating Partnership, collectively, unless the context indicates otherwise.

The partnership agreement provides that the Operating Partnership will assume and pay when due, or reimburse the Company for payment of, all costs and expenses relating to the ownership and operations of, or for the benefit of, the Operating Partnership. The partnership agreement further provides that all expenses of the Company are deemed to be incurred for the benefit of the Operating Partnership.

Certain information contained herein is presented as of October 21, 2010, the latest practicable date prior to the filing of this Quarterly Report.

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HIGHWOODS PROPERTIES, INC.

Consolidated Balance Sheets

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

	September 30, 2010	December 31, 2009
Assets:		
Real estate assets, at cost:		
Land	$ 345,531	$ 350,537
Buildings and tenant improvements	2,900,749	2,880,632
Land held for development	104,010	104,148
	3,350,290	3,335,317
Less-accumulated depreciation	(818,347)	(781,073)
Net real estate assets	2,531,943	2,554,244
For-sale residential condominiums	9,576	12,933
Real estate and other assets, net, held for sale	1,249	5,031
Cash and cash equivalents	20,969	23,699
Restricted cash	4,757	6,841
Accounts receivable, net of allowance of $3,157 and $2,810, respectively	22,426	21,069
Mortgages and notes receivable, net of allowance of $950 and $698, respectively	19,942	3,143
Accrued straight-line rents receivable, net of allowance of $2,457 and $2,443, respectively	90,001	82,600
Investment in unconsolidated affiliates	62,456	66,077
Deferred financing and leasing costs, net of accumulated amortization of $55,143 and $52,129, respectively	75,069	73,517
Prepaid expenses and other assets	39,796	37,947
Total Assets	$ 2,878,184	$ 2,887,101
Liabilities, Noncontrolling Interests in the Operating Partnership and Equity:		
Mortgages and notes payable	$ 1,501,624	$ 1,469,155
Accounts payable, accrued expenses and other liabilities	112,738	117,328
Financing obligations	33,625	37,706
Total Liabilities	1,647,987	1,624,189
Commitments and contingencies		
Noncontrolling interests in the Operating Partnership	123,293	129,769
Equity:		
Preferred Stock, $.01 par value, 50,000,000 authorized shares;		
8.625% Series A Cumulative Redeemable Preferred Shares (liquidation preference $1,000 per share), 29,092 shares issued and outstanding	29,092	29,092
8.000% Series B Cumulative Redeemable Preferred Shares (liquidation preference $25 per share), 2,100,000 shares issued and outstanding	52,500	52,500

Common Stock, $.01 par value, 200,000,000 authorized shares; 71,656,232 and 71,285,303 shares issued and outstanding, respectively	717	713
Additional paid-in capital	1,762,968	1,751,398
Distributions in excess of net income available for common stockholders	(740,356)	(701,932)
Accumulated other comprehensive loss	(2,975)	(3,811)
Total Stockholders' Equity	1,101,946	1,127,960
Noncontrolling interests in consolidated affiliates	4,958	5,183
Total Equity	1,106,904	1,133,143
Total Liabilities, Noncontrolling Interests in the Operating Partnership and Equity	$ 2,878,184	$ 2,887,101

See accompanying notes to consolidated financial statements.

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HIGHWOODS PROPERTIES, INC.

Consolidated Statements of Income

(Unaudited and in thousands, except per share amounts)

	Three Months Ended September 30, 2010	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
Rental and other revenues	$ 116,063	$ 113,170	$ 345,456	$ 337,445
Operating expenses:				
Rental property and other expenses	43,505	42,564	123,544	121,743
Depreciation and amortization	34,281	32,367	100,363	97,590
General and administrative	8,882	9,485	24,369	27,286
Total operating expenses	86,668	84,416	248,276	246,619
Interest expense:				
Contractual	22,020	20,001	65,527	60,525
Amortization of deferred financing costs	858	627	2,528	1,978
Financing obligations	460	706	1,330	2,151
	23,338	21,334	69,385	64,654
Other income:				
Interest and other income	1,710	3,324	4,376	6,615
Gain/(loss) on debt extinguishment	(85)	657	(85)	1,287
	1,625	3,981	4,291	7,902
Income from continuing operations before disposition of property, condominiums and investment in unconsolidated affiliates and equity in earnings of unconsolidated affiliates	7,682	11,401	32,086	34,074
Gains on disposition of property	19	34	55	247
Gains on disposition of for-sale residential condominiums	54	187	407	823
Gains on disposition of investment in unconsolidated affiliates	—	—	25,330	—
Equity in earnings of unconsolidated affiliates	1,018	682	2,701	3,844
Income from continuing operations	8,773	12,304	60,579	38,988
Discontinued operations:				
Income from discontinued operations	—	646	411	3,220
Net gains/(losses) on disposition of discontinued operations	—	(377)	(86)	20,639
	—	269	325	23,859
Net income	8,773	12,573	60,904	62,847
Net (income) attributable to noncontrolling interests in the Operating Partnership	(366)	(591)	(2,819)	(3,339)
Net (income)/loss attributable to noncontrolling interests in consolidated affiliates	148	(24)	(281)	(158)
Dividends on Preferred Stock	(1,677)	(1,677)	(5,031)	(5,031)
Net income available for common stockholders	$ 6,878	$ 10,281	$ 52,773	$ 54,319
Earnings per Common Share - basic:				

Income from continuing operations available for common stockholders	$ 0.10	$ 0.15	$ 0.74	$ 0.47
Income from discontinued operations available for common stockholders	—	—	—	0.34
Net income available for common stockholders	$ 0.10	$ 0.15	$ 0.74	$ 0.81
Weighted average Common Shares outstanding - basic	71,631	70,902	71,549	66,912
Earnings per Common Share - diluted:				
Income from continuing operations available for common stockholders	$ 0.10	$ 0.14	$ 0.74	$ 0.47
Income from discontinued operations available for common stockholders	—	—	—	0.34
Net income available for common stockholders	$ 0.10	$ 0.14	$ 0.74	$ 0.81
Weighted average Common Shares outstanding - diluted	75,638	75,072	75,537	71,024
Dividends declared per Common Share	$ 0.425	$ 0.425	$ 1.275	$ 1.275
Net income available for common stockholders:				
Income from continuing operations available for common stockholders	$ 6,878	$ 10,027	$ 52,465	$ 31,851
Income from discontinued operations available for common stockholders	—	254	308	22,468
Net income available for common stockholders	$ 6,878	$ 10,281	$ 52,773	$ 54,319

See accompanying notes to consolidated financial statements.

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HIGHWOODS PROPERTIES, INC.

Consolidated Statements of Equity

Nine Months Ended September 30, 2010 and 2009

(Unaudited and in thousands, except share amounts)

	Number of Common Shares	Common Stock	Series A Cumulative Redeemable Preferred Shares	Series B Cumulative Redeemable Preferred Shares	Additional Paid-In Capital	Accumulated Other Comprehensive Loss	Non-Controlling Interests in Consolidated Affiliates	Distributions in Excess of Net Income Available for Common Stockholders	Total
Balance at December 31, 2009	71,285,303	$ 713	$ 29,092	$ 52,500	$ 1,751,398	$ (3,811)	$ 5,183	$ (701,932)	$ 1,133,143
Issuances of Common Stock, net	112,815	1	—	—	2,075	—	—	—	2,076
Conversion of Common Units to Common Stock	93,971	1	—	—	2,957	—	—	—	2,958
Dividends on Common Stock	—	—	—	—	—	—	—	(91,197)	(91,197)
Dividends on Preferred Stock	—	—	—	—	—	—	—	(5,031)	(5,031)
Adjustment of noncontrolling interests in the Operating Partnership to fair value	—	—	—	—	1,480	—	—	—	1,480
Distributions to noncontrolling interests in consolidated affiliates	—	—	—	—	—	—	(506)	—	(506)
Issuances of restricted stock, net	164,143	—	—	—	—	—	—	—	—
Share-based compensation expense	—	2	—	—	5,058	—	—	—	5,060
Net (income) attributable to noncontrolling interests in the	—	—	—	—	—	—	—	(2,819)	(2,819)

Operating Partnership									
Net (income) attributable to noncontrolling interests in consolidated affiliates	—	—	—	—	—	—	281	(281)	—
Comprehensive income:									
Net income	—	—	—	—	—	—	—	60,904	60,904
Other comprehensive income	—	—	—	—	—	836	—	—	836
Total comprehensive income									61,740
Balance at September 30, 2010	71,656,232	$ 717	$ 29,092	$ 52,500	$ 1,762,968	$ (2,975)	$ 4,958	$ (740,356)	$ 1,106,904

	Number of Common Shares	Common Stock	Series A Cumulative Redeemable Preferred Shares	Series B Cumulative Redeemable Preferred Shares	Additional Paid-In Capital	Accumulated Other Comprehensive Loss	Non-Controlling Interests in Consolidated Affiliates	Distributions in Excess of Net Income Available for Common Stockholders	Total
Balance at December 31, 2008	63,571,705	$ 636	$ 29,092	$ 52,500	$ 1,616,093	$ (4,792)	$ 6,176	$ (639,281)	$ 1,060,424
Issuances of Common Stock, net	7,156,203	72	—	—	147,238	—	—	—	147,310
Conversion of Common Units to Common Stock	101,935	1	—	—	3,240	—	—	—	3,241
Dividends on Common Stock	—	—	—	—	—	—	—	(84,221)	(84,221)
Dividends on Preferred Stock	—	—	—	—	—	—	—	(5,031)	(5,031)
Adjustment of noncontrolling interests in the Operating Partnership to fair value	—	—	—	—	(18,497)	—	—	—	(18,497)
Distributions to noncontrolling interests in consolidated affiliates	—	—	—	—	—	—	(796)	—	(796)

Issuances of restricted stock, net	240,740	—	—	—	—	—	—	—	—
Share-based compensation expense	—	2	—	—	5,202	—	—	—	5,204
Net (income) attributable to noncontrolling interests in the Operating Partnership	—	—	—	—	—	—	—	(3,339)	(3,339)
Net (income) attributable to noncontrolling interests in consolidated affiliates	—	—	—	—	—	—	158	(158)	—
Comprehensive income:									
Net income	—	—	—	—	—	—	—	62,847	62,847
Other comprehensive income	—	—	—	—	—	813	—	—	813
Total comprehensive income									63,660
Balance at September 30, 2009	71,070,583	$ 711	$ 29,092	$ 52,500	$ 1,753,276	$ (3,979)	$ 5,538	$ (669,183)	$ 1,167,955

See accompanying notes to consolidated financial statements.

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HIGHWOODS PROPERTIES, INC.

Consolidated Statements of Cash Flows

(Unaudited and in thousands)

	Nine Months Ended September 30, 2010	2009
Operating activities:		
Net income	$ 60,904	$ 62,847
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	100,728	99,199
Amortization of lease incentives	807	866
Share-based compensation expense	5,060	5,204
Additions to allowance for doubtful accounts	3,605	4,530
Amortization of deferred financing costs	2,528	1,978
Amortization of past cash-flow hedges	262	(229)
(Gain)/loss on debt extinguishment	85	(1,287)
Net (gains)/losses on disposition of property	31	(20,886)
Gains on disposition of for-sale residential condominiums	(407)	(823)
Gains on disposition of investment in unconsolidated affiliates	(25,330)	—
Equity in earnings of unconsolidated affiliates	(2,701)	(3,844)
Changes in financing obligations	103	869
Distributions of earnings from unconsolidated affiliates	2,933	3,076
Changes in operating assets and liabilities:		
Accounts receivable	(4,689)	(534)
Prepaid expenses and other assets	(195)	(1,627)
Accrued straight-line rents receivable	(8,477)	(5,058)
Accounts payable, accrued expenses and other liabilities	7,407	10,548
Net cash provided by operating activities	142,654	154,829
Investing activities:		
Additions to real estate assets and deferred leasing costs	(66,370)	(101,675)
Net proceeds from disposition of real estate assets	6,801	61,926
Net proceeds from disposition of for-sale residential condominiums	3,732	7,940
Proceeds from disposition of investment in unconsolidated affiliates	15,000	—
Distributions of capital from unconsolidated affiliates	1,591	3,257
Repayments of mortgages and notes receivable	231	356
Contributions to unconsolidated affiliates	(907)	(922)
Changes in restricted cash and other investing activities	2,396	(15,506)
Net cash used in investing activities	(37,526)	(44,624)
Financing activities:		
Dividends on Common Stock	(91,197)	(84,221)
Dividends on Preferred Stock	(5,031)	(5,031)
Distributions to noncontrolling interests in the Operating Partnership	(4,857)	(5,168)
Distributions to noncontrolling interests in consolidated affiliates	(506)	(796)
Net proceeds from the issuance of Common Stock	2,076	147,310

Borrowings on revolving credit facility	4,000	128,000
Repayments of revolving credit facility	(4,000)	(291,000)
Borrowings on mortgages and notes payable	10,368	217,215
Repayments of mortgages and notes payable	(18,205)	(185,084)
Additions to deferred financing costs	(506)	(3,118)
Net cash used in financing activities	(107,858)	(81,893)
Net increase/(decrease) in cash and cash equivalents	(2,730)	28,312
Cash and cash equivalents at beginning of the period	23,699	13,757
Cash and cash equivalents at end of the period	$ 20,969	$ 42,069

See accompanying notes to consolidated financial statements.

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HIGHWOODS PROPERTIES, INC.

Consolidated Statements of Cash Flows – Continued

(Unaudited and in thousands)

Supplemental disclosure of cash flow information:

	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
Cash paid for interest, net of amounts capitalized	$ 66,435	$ 64,734

Supplemental disclosure of non-cash investing and financing activities:

	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
Unrealized gains on cash-flow hedges	$ —	$ 591
Conversion of Common Units to Common Stock	$ 2,958	$ 3,241
Change in accrued capital expenditures	$ 890	$ (9,560)
Write-off of fully depreciated real estate assets	$ 34,703	$ 24,991
Write-off of fully amortized deferred financing and leasing costs	$ 11,521	$ 14,592
Unrealized gains/(losses) on marketable securities of non-qualified deferred compensation plan	$ 489	$ (109)
Settlement of financing obligation	$ 4,184	$ —
Adjustment of noncontrolling interests in the Operating Partnership to fair value	$ (1,480)	$ 18,497
Unrealized gain on tax increment financing bond	$ 471	$ 451
Mortgages receivable from seller financing	$ 17,030	$ —
Assumption of mortgages and notes payable	$ 40,306	$ —

See accompanying notes to consolidated financial statements.

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements

September 30, 2010

(tabular dollar amounts in thousands, except per share data)

(Unaudited)

1. Description of Business and Significant Accounting Policies

Description of Business

The Company is a fully-integrated, self-administered and self-managed equity real estate investment trust ("REIT") that operates in the Southeastern and Midwestern United States. The Company conducts virtually all of its activities through the Operating Partnership. At September 30, 2010, the Company and/or the Operating Partnership wholly owned 294 in-service office, industrial and retail properties, comprising 27.1 million square feet; 96 rental residential units; 580 acres of undeveloped land suitable for future development, of which 490 acres are considered core holdings; one 100% pre-leased office property under re-development; one recently developed office property that is in service but not yet stabilized; and 30 for-sale residential condominiums (which are owned through a consolidated, majority-owned joint venture).

The Company is the sole general partner of the Operating Partnership. At September 30, 2010, the Company owned all of the Preferred Units and 71.2 million, or 95.0%, of the Common Units. Limited partners (including one officer and two directors of the Company) own the remaining 3.8 million Common Units. Generally, the Operating Partnership is obligated to redeem each Common Unit at the request of the holder thereof for cash equal to the value of one share of Common Stock, $.01 par value, based on the average of the market price for the 10 trading days immediately preceding the notice date of such redemption provided that the Company, at its option, may elect to acquire any such Common Units presented for redemption for cash or one share of Common Stock. The Common Units owned by the Company are not redeemable. During the nine months ended September 30, 2010, the Company redeemed 93,971 Common Units for a like number of shares of Common Stock, which increased the percentage of Common Units owned by the Company from 94.8% at December 31, 2009 to 95.0% at September 30, 2010.

Basis of Presentation

Our Consolidated Financial Statements are prepared in conformity with accounting principles generally accepted in the United States ("GAAP"). Our Consolidated Statements of Income for the three and nine months ended September 30, 2009 were revised from previously reported amounts to reflect in discontinued operations the operations for those properties sold or held for sale during the 12 months ended September 30, 2010 which required discontinued operations presentation. Prior period amounts related to additions to allowance for doubtful accounts and amortization of lease commissions in our Consolidated Statements of Cash Flows have been reclassified to conform to the current period presentation.

Our Consolidated Financial Statements include the Operating Partnership, wholly owned subsidiaries and those entities in which we have the controlling financial interest. All significant intercompany transactions and accounts have been eliminated. At September 30, 2010 and December 31, 2009, we were not involved with any entities that were determined to be variable interest entities.

The unaudited interim consolidated financial statements and accompanying unaudited consolidated financial information, in the opinion of management, contain all adjustments (including normal recurring accruals) necessary for a fair presentation of our financial position, results of operations and cash flows. We have omitted certain notes and other information from the interim consolidated financial statements presented in this Quarterly Report on Form 10-Q as permitted by SEC rules and regulations. These Consolidated Financial Statements should be read in conjunction with our 2009 Annual Report on Form 10-K.

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

(tabular dollar amounts in thousands, except per share data)

1. Description of Business and Significant Accounting Policies - Continued

Use of Estimates

The preparation of these Consolidated Financial Statements in accordance with GAAP requires us to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

Recently Issued Accounting Standards

Beginning with our 2010 Annual Report on Form 10-K, we will be required to provide enhanced disclosure about our financial receivables, such as our mortgages and notes receivable, and our policy for measuring credit losses related to those receivables.

2. Real Estate Assets

Acquisitions

During the third quarter of 2010, we acquired a 336,000 square foot office property in Memphis, TN for $10.0 million in cash and the assumption of secured debt, which was recorded at fair value of $40.3 million with an implied interest rate of 6.4%. The debt matures in November 2015. We have incurred or expect to incur $0.4 million of acquisition-related expenses and approximately $2.3 million of near-term building improvements. In connection with this acquisition, we recorded $2.8 million of above market lease intangible assets and $7.1 million of in-place lease intangible assets with weighted average amortization periods at the time of acquisition of 7.3 and 5.9 years, respectively.

Dispositions

During the second quarter of 2010, we sold seven office properties in Winston Salem, NC for gross proceeds of $12.9 million. In connection with this disposition, we received cash of $4.5 million and provided seller financing of $8.4 million (recorded at fair value of $8.4 million in mortgages and notes receivable) and committed to lend up to an additional $1.7 million for tenant improvements and lease commissions, of which $0.2 million was funded as of September 30, 2010. The three-year, interest-only first mortgage carries a 6.0% average interest rate. Assuming no default exists, the note can be extended by the buyer for two additional one-year periods, subject to an increase in the interest rate to 7.0% in the fourth year and to 8.0% in the fifth year. We have accounted for this disposition using the installment method, whereby the $0.4 million gain on disposition of property has been deferred and will be recognized when the seller financing is repaid.

During the second quarter of 2010, we also sold six industrial properties in Greensboro, NC for gross proceeds of $12.0 million. In connection with this disposition, we received cash of $3.4 million and provided seller financing of $8.6 million (recorded at fair value of $8.6 million in mortgages and notes receivable) and a limited rent guarantee with maximum exposure to loss of $1.0 million as of September 30, 2010. The three-year, interest-only first mortgage carries a 6.25% average interest rate. Assuming no default exists, the note can be extended by the buyer for two additional one-year periods, subject to an increase in the interest rate to 7.0% in the fourth year and to 7.75% in the fifth year. We currently have concluded that a loss from the rent guarantee is not probable. We have accounted for this disposition using the installment method, whereby the $0.3 million impairment was recognized in net gains/(losses) on disposition of discontinued operations in the second quarter of 2010.

During the first quarter of 2010, we recorded a completed sale in connection with the disposition of an office property in Raleigh, NC in the fourth quarter of 2009 where the buyer's right to compel us to repurchase the property expired. Accordingly, we recognized the $0.2 million gain on disposition of property in the first quarter of 2010.

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

(tabular dollar amounts in thousands, except per share data)

3. Investment in Affiliates

Unconsolidated Affiliates

We have equity interests ranging from 10.0% to 50.0% in various joint ventures with unrelated third parties. The following table sets forth the combined, summarized income statements for our unconsolidated joint ventures:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Income Statements:				
Revenues	$ 26,517	$ 36,152	$ 93,819	$ 112,368
Expenses:				
Rental property and other expenses	12,664	17,805	45,463	54,510
Depreciation and amortization	6,730	9,092	24,108	26,817
Interest expense	6,094	8,743	21,892	26,584
Total expenses	25,488	35,640	91,463	107,911
Income before disposition of property	1,029	512	2,356	4,457
Gains/(losses) on disposition of property	—	(463)	—	2,963
Net income	$ 1,029	$ 49	$ 2,356	$ 7,420
Our share of:				
Net income (1)	$ 1,018	$ 682	$ 2,701	$ 3,844
Depreciation and amortization of real estate assets	$ 2,115	$ 3,352	$ 8,193	$ 9,825
Interest expense	$ 2,190	$ 3,491	$ 8,368	$ 10,611
Gain/(loss) on disposition of property	$ —	$ (199)	$ —	$ 582

(1) Our share of net income differs from our weighted average ownership percentage in the joint ventures' net income due to our purchase accounting and other adjustments related primarily to management and leasing fees.

During the second quarter of 2010, we sold our equity interests in a series of unconsolidated joint ventures relating to properties in Des Moines, IA. The assets in the joint ventures included 2.5 million square feet of office (1.7 million square feet), industrial (788,000 square feet) and retail (45,000 square feet) properties, as well as 418 apartment units. In connection with the closing, we received $15.0 million in cash. We had a negative book basis in certain of the joint ventures, primarily as a result of prior cash distributions to the partners. Accordingly, we recorded gain on disposition of investment in unconsolidated affiliates of $25.3 million in the second quarter of 2010. As of the closing date, the joint ventures had approximately $170 million of secured debt, which was non-recourse to us except (1) in the case of customary exceptions pertaining to matters such as misuse of funds, borrower bankruptcy, unpermitted transfers, environmental conditions and material misrepresentations and (2) approximately $9.0 million of direct and indirect guarantees. We have been released by the applicable lenders from all such direct and indirect guarantees and we have no ongoing lender liability relating to such customary exceptions to non-recourse liability with respect to most, but not all, of the debt. The buyer has agreed to indemnify and hold us harmless from any and all future losses that we suffer as a result of our prior investment in the joint ventures (other than losses directly resulting from our acts or omissions). In the event we are exposed to any such future loss, our financial condition and results of operations would not be adversely affected unless the buyer defaults on its indemnification obligation.

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

(tabular dollar amounts in thousands, except per share data)

3. Investment in Affiliates - Continued

Consolidated Affiliates

We own a majority interest in Plaza Residential, LLC ("Plaza Residential"), a joint venture which was formed to develop and sell 139 for-sale residential condominiums constructed above an office tower developed by us in Raleigh, NC. For-sale residential condominiums in our Consolidated Balance Sheets include 30 and 40 completed, but unsold, condominiums owned by Plaza Residential at September 30, 2010 and December 31, 2009, respectively. We initially record receipts of earnest money deposits in accounts payable, accrued expenses and other liabilities in accordance with the deposit method. We then record completed sales when units close and the remaining net cash is received. During the three months ended September 30, 2010 and 2009, we received $0.6 million and $2.9 million, respectively, in gross proceeds and recorded $0.5 million and $2.7 million, respectively, of cost of goods sold from condominium sales activity. During the nine months ended September 30, 2010 and 2009, we received $4.0 million and $8.4 million, respectively, in gross proceeds and had $3.6 million and $7.6 million, respectively, of cost of goods sold from condominium sales activity.

4. Deferred Financing and Leasing Costs

The following table sets forth total deferred financing and leasing costs, net of accumulated amortization:

	September 30, 2010	December 31, 2009
Deferred financing costs	$ 17,078	$ 16,811
Less accumulated amortization	(6,917)	(4,549)
	10,161	12,262
Deferred leasing costs	113,134	108,835
Less accumulated amortization	(48,226)	(47,580)
	64,908	61,255
Deferred financing and leasing costs, net	$ 75,069	$ 73,517

Amortization of deferred financing and leasing costs were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Amortization of deferred financing costs	$ 858	$ 627	$ 2,528	$ 1,978
Amortization of lease commissions (included in depreciation and amortization)	$ 3,912	$ 3,806	$ 11,495	$ 11,598
Amortization of lease incentives (included in rental and other revenues)	$ 270	$ 318	$ 807	$ 866

The following table sets forth scheduled future amortization for deferred financing and leasing costs:

	Amortization of Deferred Financing Costs	Amortization of Lease Commissions	Amortization of Lease Incentives
September 30, 2010 through December 31, 2010	$ 788	$ 3,855	$ 261
2011	2,680	13,825	982
2012	2,526	11,390	881
2013	897	9,151	683
2014	520	7,015	512
Thereafter	2,750	14,947	1,406
	$ 10,161	$ 60,183	$ 4,725

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

(tabular dollar amounts in thousands, except per share data)

4. Deferred Financing and Leasing Costs - Continued

The weighted average remaining amortization periods for deferred financing and leasing costs were 3.6 years and 6.3 years, respectively, as of September 30, 2010.

5. Mortgages and Notes Payable

The following table sets forth our consolidated mortgages and notes payable:

	September 30, 2010	December 31, 2009
Secured indebtedness	$ 763,107	$ 720,727
Unsecured indebtedness	738,517	748,428
Total mortgages and notes payable	$ 1,501,624	$ 1,469,155

At September 30, 2010, our secured mortgage loans were secured by real estate assets with an aggregate undepreciated book value of $1.2 billion.

Our $400.0 million unsecured revolving credit facility is scheduled to mature on February 21, 2013 and includes an accordion feature that allows for an additional $50.0 million of borrowing capacity subject to additional lender commitments. Assuming we continue to have three publicly announced ratings from the credit rating agencies, the interest rate and facility fee under our revolving credit facility are based on the lower of the two highest publicly announced ratings. Based on our current credit ratings, the interest rate is LIBOR plus 290 basis points and the annual facility fee is 60 basis points. There were no amounts outstanding under our revolving credit facility at September 30, 2010 and October 21, 2010. At September 30, 2010 and October 21, 2010, we had $1.1 million of outstanding letters of credit, which reduces the availability on our revolving credit facility. As a result, the unused capacity of our revolving credit facility at September 30, 2010 and October 21, 2010 was $398.9 million.

Our $70.0 million secured construction facility, of which $52.1 million was outstanding at September 30, 2010, is initially scheduled to mature on December 20, 2010. The outstanding balance increased in the third quarter of 2010 due to the use of proceeds to reduce the balance outstanding under a bank term loan due in March 2012. Assuming no defaults have occurred, we have options to extend the maturity date for two successive one-year periods. During the third quarter of 2010, we submitted our notice to extend the maturity date by one year. Upon payment of the extension fee and assuming no default exists at December 20, 2010, the facility will be extended until December 20, 2011. The interest rate is LIBOR plus 85 basis points. This facility had $17.9 million of availability at September 30, 2010 and October 21, 2010.

We are currently in compliance with all debt covenants and requirements.

6. Derivative Financial Instruments

We had no outstanding interest rate hedge contracts at September 30, 2010 or December 31, 2009. The following table sets forth the effect of our past cash-flow hedges on accumulated other comprehensive loss ("AOCL") and interest expense:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Derivatives Designated as Cash-flow Hedges:				
Unrealized gain recognized in AOCL on derivatives (effective portion):				
Interest rate hedge contracts	$ —	$ 177	$ —	$ 591
(Gain)/loss reclassified out of AOCL into interest expense (effective portion):				
Interest rate hedge contracts	$ (25)	$ (89)	$ 262	$ (229)

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

(tabular dollar amounts in thousands, except per share data)

7. Noncontrolling Interests

Noncontrolling Interests in the Operating Partnership

Noncontrolling interests in the Operating Partnership relate to the ownership of Common Units by various individuals and entities other than the Company. The following table sets forth noncontrolling interests in the Operating Partnership:

	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
Beginning noncontrolling interests in the Operating Partnership	$ 129,769	$ 111,278
Adjustments of noncontrolling interests in the Operating Partnership to fair value	(1,480)	18,497
Conversion of Common Units to Common Stock	(2,958)	(3,241)
Net income attributable to noncontrolling interests in the Operating Partnership	2,819	3,339
Distributions to noncontrolling interests in the Operating Partnership	(4,857)	(5,168)
Total noncontrolling interests in the Operating Partnership	$ 123,293	$ 124,705

The following table sets forth the change in equity from net income available for common stockholders and transfers from noncontrolling interests:

	Three Months Ended September 30, 2010	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
Net income available for common stockholders	$ 6,878	$ 10,281	$ 52,773	$ 54,319
Conversion of Common Units to Common Stock	—	3,052	2,958	3,241
Change in equity from net income available for common stockholders and conversion of Common Units to Common Stock	$ 6,878	$ 13,333	$ 55,731	$ 57,560

Noncontrolling Interests in Consolidated Affiliates

Noncontrolling interests in consolidated affiliates relates to our respective joint venture partners' 50.0% interest in Highwoods-Markel Associates, LLC and both legal and estimated economic interests of 7% in Plaza Residential. Each of our joint venture partners is an unrelated third party.

8. Disclosure About Fair Value of Financial Instruments

The following summarizes the three levels of inputs that we use to measure fair value, as well as the assets, noncontrolling interests in the Operating Partnership and liabilities that we recognize at fair value using those levels of inputs.

Level 1. Quoted prices in active markets for identical assets or liabilities.

Our Level 1 assets are investments in marketable securities which we use to pay benefits under our non-qualified deferred compensation plan. Our Level 1 noncontrolling interests in the Operating Partnership relate to the ownership of Common Units by various individuals and entities other than the Company. Our Level 1 liability is our non-qualified deferred compensation obligation.

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

(tabular dollar amounts in thousands, except per share data)

8. Disclosure About Fair Value of Financial Instruments - Continued

Level 2. Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the related assets or liabilities. We had no Level 2 assets or liabilities at September 30, 2010 and December 31, 2009.

Level 3. Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Our Level 3 assets are our tax increment financing bond, which is not routinely traded but whose fair value is determined using an estimate of projected redemption value based on quoted bid/ask prices for similar unrated municipal bonds, and real estate assets recorded at fair value on a non-recurring basis as a result of our quarterly impairment analysis, which were valued using independent appraisals.

The following tables set forth the assets, noncontrolling interests in the Operating Partnership and liability that we measure at fair value by level within the fair value hierarchy. We determine the level based on the lowest level of substantive input used to determine fair value.

	September 30, 2010	Level 1 Quoted Prices in Active Markets for Identical Assets or Liabilities	Level 3 Significant Unobservable Inputs
Assets:			
Marketable securities of non-qualified deferred compensation plan (in prepaid expenses and other assets)	$ 3,232	$ 3,232	$ —
Tax increment financing bond (in prepaid expenses and other assets)	17,342	—	17,342
Total Assets	$ 20,574	$ 3,232	$ 17,342
Noncontrolling Interests in the Operating Partnership	$ 123,293	$ 123,293	$ —
Liability:			
Non-qualified deferred compensation obligation (in accounts payable, accrued expenses and other liabilities)	$ 3,846	$ 3,846	$ —

	December 31, 2009	Level 1 Quoted Prices in Active Markets for Identical Assets or Liabilities	Level 3 Significant Unobservable Inputs
Assets:			
Marketable securities of non-qualified deferred compensation plan	$ 6,135	$ 6,135	$ —
Tax increment financing bond	16,871	—	16,871
Impaired real estate assets	32,000	—	32,000
Total Assets	$ 55,006	$ 6,135	$ 48,871
Noncontrolling Interests in the Operating Partnership	$ 129,769	$ 129,769	$ —
Liability:			
Non-qualified deferred compensation obligation	$ 6,898	$ 6,898	$ —

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

(tabular dollar amounts in thousands, except per share data)

8. Disclosure About Fair Value of Financial Instruments – Continued

The following table sets forth our Level 3 asset:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Asset:				
Tax Increment Financing Bond				
Beginning balance	$ 17,017	$ 17,660	$ 16,871	$ 17,468
Unrealized gain (in AOCL)	325	259	471	451
Ending balance	$ 17,342	$ 17,919	$ 17,342	$ 17,919

In the fourth quarter of 2007, we acquired a tax increment financing bond associated with a property developed by us. This bond amortizes to maturity in 2020. The estimated fair value at September 30, 2010 was $1.9 million below the outstanding principal due on the bond. If the yield-to-maturity used to fair value this bond was 100 basis points higher, the fair value of the bond would have been $0.8 million lower as of September 30, 2010. If the yield-to-maturity used to fair value this bond was 100 basis points lower, the fair value of the bond would have been $0.8 million higher as of September 30, 2010. Currently, we intend to hold this bond and have concluded that we will not be required to sell this bond before recovery of the bond principal. Payment of the principal and interest for the bond is guaranteed by us and, therefore, we have recorded no credit losses related to the bond in the three and nine months ended September 30, 2010 and 2009. There is no legal right of offset with the liability, which we report as a financing obligation, related to this tax increment financing bond.

The following table sets forth the carrying amounts and fair values of our financial instruments:

	Carrying Amount	Fair Value
September 30, 2010		
Cash and cash equivalents	$ 20,969	$ 20,969
Restricted cash	$ 4,757	$ 4,757
Accounts, mortgages and notes receivable	$ 42,368	$ 42,481
Marketable securities of non-qualified deferred compensation plan	$ 3,232	$ 3,232
Tax increment financing bond	$ 17,342	$ 17,342
Mortgages and notes payable	$ 1,501,624	$ 1,597,621
Financing obligations	$ 33,625	$ 22,861
Non-qualified deferred compensation obligation	$ 3,846	$ 3,846
Noncontrolling interests in the Operating Partnership	$ 123,293	$ 123,293
December 31, 2009		
Cash and cash equivalents	$ 23,699	$ 23,699

Restricted cash	$	6,841	$	6,841
Accounts, mortgages and notes receivable	$	24,212	$	24,212
Marketable securities of non-qualified deferred compensation plan	$	6,135	$	6,135
Tax increment financing bond	$	16,871	$	16,871
Mortgages and notes payable	$	1,469,155	$	1,440,317
Financing obligations	$	37,706	$	31,664
Non-qualified deferred compensation obligation	$	6,898	$	6,898
Noncontrolling interests in the Operating Partnership	$	129,769	$	129,769

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

(tabular dollar amounts in thousands, except per share data)

8. Disclosure About Fair Value of Financial Instruments – Continued

The carrying values of our cash and cash equivalents, restricted cash, accounts receivable, marketable securities of non-qualified deferred compensation plan, tax increment financing bond, non-qualified deferred compensation obligation and noncontrolling interests in the Operating Partnership are equal to or approximate fair value. The fair values of our mortgages and notes receivable, mortgages and notes payable and financing obligations were estimated using the income or market approaches to approximate the price that would be paid in an orderly transaction between market participants on the respective measurement dates.

9. Share-Based Payments

During the nine months ended September 30, 2010, we granted 190,826 stock options at an exercise price equal to the closing market price of a share of our Common Stock on the date of grant. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model, which resulted in a weighted-average grant date fair value per share of $4.96. During the nine months ended September 30, 2010, we also granted 89,635 shares of time-based restricted stock and 78,151 shares of total return-based restricted stock with weighted-average grant date fair values per share of $29.05 and $29.75, respectively. We recorded stock-based compensation expense of $1.6 million each during the three months ended September 30, 2010 and 2009 and $5.1 million and $5.2 million during the nine months ended September 30, 2010 and 2009, respectively. At September 30, 2010, there was $8.4 million of total unrecognized stock-based compensation costs, which will be recognized over a weighted average remaining contractual term of 1.7 years.

10. Comprehensive Income and Accumulated Other Comprehensive Loss

The following table sets forth the components of comprehensive income:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Net income	$ 8,773	$ 12,573	$ 60,904	$ 62,847
Other comprehensive income/(loss):				
Unrealized gain on tax increment financing bond	325	259	471	451
Unrealized gains on cash-flow hedges	—	177	—	591
Amortization of past cash-flow hedges	(25)	(89)	262	(229)
Settlement of past cash-flow hedge from disposition of investment in unconsolidated affiliate	—	—	103	—
Total other comprehensive income	300	347	836	813
Total comprehensive income	$ 9,073	$ 12,920	$ 61,740	$ 63,660

The following table sets forth the components of AOCL:

	September 30, 2010	December 31, 2009
Tax increment financing bond	$ 1,895	$ 2,366
Past cash-flow hedges	1,080	1,445
Total accumulated other comprehensive loss	$ 2,975	$ 3,811

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

(tabular dollar amounts in thousands, except per share data)

11. Discontinued Operations

The following table sets forth our operations which required classification as discontinued operations:

	Three Months Ended September 30, 2010	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
Rental and other revenues	$ —	$ 1,455	$ 1,432	$ 7,837
Operating expenses:				
Rental property and other expenses	—	488	656	3,010
Depreciation and amortization	—	322	365	1,609
Total operating expenses	—	810	1,021	4,619
Other income	—	1	—	2
Income before net gains/(losses) on disposition of discontinued operations	—	646	411	3,220
Net gains/(losses) on disposition of discontinued operations	—	(377)	(86)	20,639
Total discontinued operations	$ —	$ 269	$ 325	$ 23,859

The following table sets forth the major classes of assets and liabilities of the properties classified as held for sale:

	September 30, 2010	December 31, 2009
Assets:		
Land	$ —	$ 867
Buildings and tenant improvements	—	3,876
Land held for development	1,217	1,197
Total real estate assets	1,217	5,940
Less accumulated depreciation	—	(1,484)
Net real estate assets	1,217	4,456
Deferred leasing costs, net	—	209
Accrued straight line rents receivable	—	289
Prepaid expenses and other assets	32	77
Real estate and other assets, net, held for sale	$ 1,249	$ 5,031
Liabilities of real estate and other assets, net, held for sale (1)	$ 12	$ 12

(1) Included in accounts payable, accrued expenses and other liabilities.

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

(tabular dollar amounts in thousands, except per share data)

12. Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per Common Share:

	Three Months Ended September 30,		Nine Months Ended September 30,
	2010	2009	2010