

ARDEN REALTY INC
Form 10-K
March 14, 2005

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Securities and Exchange Commission

Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2004

OR

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

For the transition period from to

Commission File Number 1-12193

ARDEN REALTY, INC.

(Exact name of registrant as specified in its charter)

Maryland
(State or other jurisdiction of
incorporation or organization)

95-4578533
(I.R.S. Employer Identification No.)

11601 Wilshire Boulevard, 4th Floor

Los Angeles, California 90025-1740
(Address and zip code of principal executive offices)

Registrant's telephone number, including area code: (310) 966-2600

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

Title of each class

Name of each exchange on which registered

Common Stock, \$0.01 par value
Preferred Stock Purchase Rights

New York Stock Exchange
New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained to the best of the Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this

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Form 10-K, or any amendment to this Form 10-K. o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes x No o

The aggregate market value of the shares of common stock held by non-affiliates was approximately \$1.9 billion based on the closing price on the New York Stock Exchange for such shares on June 30, 2004.

The number of the Registrant's shares of common stock outstanding was 66,364,703 as of March 10, 2005.

DOCUMENTS INCORPORATED BY REFERENCE

Part III of this report incorporates information by reference from the definitive Proxy Statement for the 2005 Annual Meeting of Stockholders.

ARDEN REALTY, INC.

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PART I

Forward-Looking Statements

This Form 10-K, including the documents incorporated herein by reference, contains forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act pertaining to, among other things, our future results of operations, cash available for distribution, acquisitions, lease renewals, property development, property renovation, capital requirements and general business, industry and economic conditions applicable to us. Also, documents we subsequently file with the SEC and incorporated herein by reference will contain forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements as a result of the risk factors set forth below and the matters set forth or incorporated in this Form 10-K generally. We caution you, however, that this list of factors may not be exhaustive, particularly with respect to future filings.

ITEM 1. Business

(a) GENERAL

The terms Arden Realty, us, we and our as used in this report refer to Arden Realty, Inc. We were incorporated in Maryland in May 1996 and completed our initial public offering in October 1996. Commencing with our taxable year ended December 31, 1996, we have operated and qualified as a real estate investment trust, or REIT, for federal income tax purposes. We are a self-administered and self-managed REIT that owns, manages, leases, develops, renovates and acquires commercial properties located in Southern California. We are the sole general partner of Arden Realty Limited Partnership, or the Operating Partnership, and as of December 31, 2004, we owned approximately 97.5% of the Operating Partnership's common partnership units. We conduct substantially all of our operations through the Operating Partnership and its consolidated subsidiaries.

(b) INDUSTRY SEGMENTS

We are currently involved primarily in one industry segment, the operation of commercial real estate located in Southern California. The financial information contained in this report relates primarily to this industry segment.

(c) DESCRIPTION OF BUSINESS

We are a full-service real estate organization managed by 6 senior executive officers who have experience in the real estate industry ranging from 14 to 35 years and who collectively have an average of 20 years of experience. We perform all property management, construction management, accounting, finance and acquisition and disposition activities and a majority of our leasing transactions for our portfolio with our staff of approximately 300 employees.

As of December 31, 2004, we were Southern California's largest publicly traded office landlord as measured by total net rentable square feet owned. As of December 31, 2004, our portfolio of primarily suburban office properties consisted of 120 properties and 197 buildings containing approximately 18.2 million net rentable square feet and our operating portfolio was 91.2% occupied.

Portfolio Management

We perform all portfolio management activities, including on-site property management, management of all lease negotiations, construction management of tenant improvements or tenant build-outs, property renovations and capital expenditures for our portfolio. We directly manage these activities from approximately 40 management offices located throughout our portfolio. The activities of these management offices are supervised by four regional offices with oversight by our corporate office to ensure consistent application of our operating policies and procedures. Each regional office is strategically located within the Southern California submarkets where our properties are located and is managed by a regional First Vice President who is

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responsible for supervising the day-to-day activities of our management offices. Each regional office is staffed with leasing, property management, building engineering, construction and information systems specialists, referred to as our Regional Service Teams. By maintaining a regionally focused organizational structure led by seasoned managers, we are able to quickly respond to our tenants' needs and market opportunities.

All of our management and regional offices are networked with our corporate office and have access to the Internet and our e-mail, accounting and lease management systems. Our accounting and lease management systems employ the latest technology and allow both corporate and field personnel access to tenant and prospective tenant-related information to enhance responsiveness and communication of marketing and leasing activity for each property.

We currently lease approximately 59% of our portfolio's net rentable space using our in-house staff. We employ outside brokers who are monitored by our Regional Service Teams for the remainder of our net rentable space. Our in-house leasing program allows us to closely monitor rental rates and lease terms for new and renewal leases and reduce third-party leasing commissions.

Business Strategies

Our primary business strategy is to actively manage our portfolio to achieve gains in rental rates and occupancy, control operating expenses and maximize income from ancillary operations and services. When market conditions permit, we may also selectively develop, renovate or acquire new properties in submarkets that add value and fit strategically into our portfolio. We may also sell existing properties and use the net proceeds to repay outstanding indebtedness or place into investments that we believe will generate higher long-term value.

Through our corporate office and regional offices, we implement our business strategies by:

using integrated decision making to provide proactive solutions to the space needs of tenants in the markets where we have extensive real estate expertise and relationships;

emphasizing quality service, tenant satisfaction and retention;

employing intensive property marketing and leasing programs; and

implementing cost control management techniques and systems that capitalize on economies of scale and concentration arising from the size and geographic focus of our portfolio and our technical expertise in reducing energy consumption expenses.

We believe the implementation of these operating practices has been instrumental in maximizing the operating results of our portfolio.

Integrated Decision Making

We use a multidisciplinary approach to our decision making by having our regional management, leasing, construction management, acquisition, disposition and finance teams coordinate their activities to enhance responsiveness to market opportunities and to provide proactive solutions to the space needs of tenants in the submarkets where we have extensive real estate and technical expertise. This integrated approach permits us to analyze the specific requirements of existing and prospective tenants and the economic terms and costs for each transaction on a timely and efficient basis. We are therefore able to commit to leasing, development, acquisition or disposition terms quickly, which facilitates an efficient completion of lease negotiation and tenant build-out, shorter vacancy periods after lease expirations and the timely completion of development, acquisition or disposition transactions.

Quality Service and Tenant Satisfaction

We strive to provide quality service through our multidisciplinary operating approach resulting in timely responses to our tenants' needs. Our seasoned Regional Service Teams interact and resolve issues relating to tenant satisfaction and day-to-day operations. For portfolio-wide operational and administrative functions, our

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corporate office provides support to all regional offices and provides immediate response for critical operational issues. We believe providing quality service leads to enhanced tenant retention.

Proactive Marketing and Leasing

The concentration of many of our properties within particular office submarkets and our relationships with a broad array of businesses and outside brokers enables us to pursue proactive marketing and leasing strategies, to effectively monitor the demand for office space in our existing submarkets, to efficiently identify the office space requirements of existing and prospective tenants and to offer tenants a variety of space alternatives across our portfolio.

Cost Control and Operating Efficiencies

The size and geographic focus of our portfolio provides us with the opportunity to enhance portfolio value by controlling operating costs. We seek to capitalize on the economies of scale and concentration which result from the geographic focus of our portfolio through the ownership and management of multiple properties within particular submarkets and the maintenance of standardized processes and systems for cost control at each of our properties. These cost controls and operating efficiencies allowed us to achieve a 67.3% ratio of property operating results to total property revenues in 2004.

Operating Strategies

Based on our geographic focus in Southern California, experience in the local real estate markets and our evaluation of current market conditions, we believe the following key factors provide us with opportunities to maximize returns:

the broad diversification and balance of the Southern California economy and our tenant base minimizes our dependence on any one industry segment or limited group of tenants;

the relative resiliency of the Southern California real estate market, as measured by lower vacancy rates compared to the national average and a lower decline in rental rates in our key submarkets than the average decreases in rates reported for the nation since the beginning of the office real estate sector downturn in 2001; and

the limited construction of new office properties in the Southern California region due to substantial building construction limitations and a minimal amount of developable land in many key submarkets.

Internal Operating Strategy

We believe that opportunities exist to increase cash flow from our existing portfolio. We intend to pursue this internal growth by:

stabilizing occupancy throughout our portfolio and increasing rental rates, as market conditions permit;

maintaining or increasing the retention rate of expiring leases;

capitalizing on economies of scale and concentration due to the size and geographic focus of our portfolio;

controlling operating expenses through active cost control management techniques and systems; and

sourcing new and innovative revenue streams while providing high quality services to our tenants.

Stabilizing Occupancy and Increasing Rental Rates

Various published reports noted that Southern California achieved approximately 6.7 million square feet of positive net absorption in 2004 with average rental rates increasing approximately 3-4%. Our in-house leasing teams, working with outside leasing brokers, continuously monitor each market to identify strong prospective tenants who are in need of new or additional space. We also strive to be responsive to the needs of existing tenants through our on-site management staff and by providing alternatives within our portfolio to

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accommodate their changing space requirements. We strive to achieve growth in rental revenues by negotiating annual or mid-term increases in rental rates in a majority of our leases.

Retaining Existing Tenants

We also seek to retain our existing tenants when leases expire. Retention of existing tenants reduces the costs of lease rollover by eliminating the down-time required to find a replacement tenant and reducing build-out costs required for new tenants. We believe that we have been successful in attracting and retaining a diverse tenant base by actively managing our properties with an emphasis on tenant satisfaction and retention. During 2004, we retained approximately 64% of our leases that were scheduled to expire.

Capitalizing on Economies of Scale and Concentration

In order to capitalize on economies of scale and concentration arising from the size and geographic focus of our portfolio, each of our Regional Service Teams is responsible for several properties, which spreads administrative and maintenance costs over those properties and reduces per square foot expenses. In addition, contracting in bulk for parking operations, construction materials, building services and supplies on a portfolio-wide basis also reduces our overall operating expenses.

Cost Control Management Techniques and Systems

We plan to continue controlling our operating expenses through active management at all of our properties. We focus on cost control in various areas of our operations. We continuously monitor the operating performance of our properties and employ energy-enhancing purchasing and expense recovery technologies when appropriate. These system enhancements include:

- lighting retrofits;
- replacement of inefficient heating, ventilation and air conditioning systems;
- computer-driven energy management systems that monitor and react to the climatic requirements of individual properties;
- automated and roving security systems that allow us to provide security services to our tenants at a lower cost;
- online competitive bid purchasing of supplies, building materials and construction services;
- enhancement of billing systems, which enables us to more efficiently recover operating expenses from our tenants; and
- on-going preventive maintenance programs to operate our building systems efficiently, thereby reducing operating costs.

Sourcing Additional Revenue While Providing High Quality Services to Tenants

We operate one of the most energy efficient office portfolios in the country. We have invested in energy enhancement programs within our portfolio with the aim of reducing energy consumption, enhancing efficiency and lowering operating costs. We also participate annually in the Environmental Protection Agency's, or the EPA, Energy Star Program. This program involves top commercial real estate landlords throughout the United States and rigorous bench-marking procedures that track individual building energy efficiency. Currently, of the 906 total Energy Star designated office buildings awarded nationally during 2004, 125 were awarded in California; of those, we had 62 EPA Energy Star Certified buildings in our portfolio.

We have formed a taxable REIT subsidiary, Next>edge, to market our expertise in energy solutions and facilities management. Next>edge has begun to assist companies in increasing their energy efficiency and reducing costs by employing the latest technologies and the most energy-efficient operational strategies developed to date. These technologies include lighting, heating, ventilation and air conditioning retrofits, energy management system installations, on-site distributed generation and cogeneration projects and solar energy systems.

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External Operating Strategy

We believe in the diversity and balance of the Southern California economy and commercial real estate market, and we intend to continue to focus our resources primarily in this region. We have assembled a management team that has extensive experience and knowledge in this market which we believe provides us with a competitive advantage in identifying and capitalizing on selective development, renovation and acquisition opportunities.

Subject to capital availability and market conditions, our approach is to seek development, renovation and acquisition opportunities in markets where we have an existing presence and where the following conditions exist:

low vacancy rates;

opportunities for rising rents due to employment growth and population movements;

a minimal amount of developable land; and

significant barriers to entry due to constraints on new development, including strict entitlement processes, height and density restrictions or other governmental requirements.

Competition

We compete with other owners of office properties to attract tenants to our properties, to acquire new properties and to obtain suitable land for development. Ownership of competing properties is currently diversified among many different types, from publicly traded companies and institutional investors, including other REITs, to small enterprises and individual owners. No one owner or group of owners currently dominate or significantly influence the markets in which we operate. See Risk Factors Competition affects occupancy levels, rents and the cost of land which could adversely affect our revenues.

California Electric Utility Deregulation

Problems associated with deregulation of the electric industry in California have resulted in significantly higher costs in some areas over the past few seasons. All of our properties are currently located in areas served by utilities that either produce their own electricity, or that have procured long-term, fixed-rate contracts with commercial electrical providers. While we have no information suggesting that any future service interruptions are expected, we believe that higher utility costs may continue as price increases are allowed by the California Public Utility Commission or other regulatory agencies.

Approximately 26% of our properties and 19% of the total rentable square footage of our portfolio are subject to leases that require our tenants to pay all utility costs and the remainder provide that our tenants will reimburse us for utility costs in excess of a base year amount. See Risk Factors Rising energy costs and power outages in California may have an adverse effect on our operations and revenue.

We are also working with other companies to provide our properties with new applications of distributed generation, or on-site energy systems, such as solar photovoltaic panels, micro-turbine units, natural gas reciprocating engines, fuel cells and other green power alternatives. Lastly, we maintain ongoing communication with our tenants to assist them in ways to lower consumption in their workplace.

Employees

As of December 31, 2004, we had approximately 300 full-time employees that perform all of our property and construction management, accounting, finance, acquisition and disposition activities and a majority of our leasing transactions.

Available Information

We file with the Securities and Exchange Commission, or SEC, our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports, proxy

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statements and registration statements. The public may read and copy any materials we file with the SEC at the SEC's Public Reference Room at 450 Fifth Street, N.W., Washington, D.C. 20549. The public may also obtain public information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. In addition, the SEC maintains an internet site at www.sec.gov that contains reports, proxy and information regarding registrants, including us, that file electronically. This annual report on Form 10-K and other periodic and current reports, and amendments to those reports, filed or furnished with the SEC, are also available, free of charge, by viewing the SEC filings available in the Investor Information section of our website at www.ardenrealty.com as soon as reasonably practicable after we file or furnish them with the SEC.

(d) FOREIGN OPERATIONS

We do not engage in any foreign operations or derive any revenue from foreign sources.

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Our portfolio consists of 120 primarily office properties, containing approximately 18.2 million net rentable square feet that individually range from approximately 12,000 to 600,000 net rentable square feet. Of the 120 properties currently in service in our portfolio, 119, or 99%, are office properties. All of our properties are located in Southern California and most are in suburban areas in close proximity to main thoroughfares. We believe that our properties are located within desirable and established business communities and are well maintained. Our properties offer an array of amenities including high-speed internet access, security, parking, conference facilities, on-site management, food services and health clubs.

Following is a summary of our property portfolio as of December 31, 2004:

| Location | Number of Properties(1) | | Number of Buildings(1) | | Approximate Net Rentable Square Feet(1) | | Property Operating Results(2),(3) | |
|------------------------|-------------------------|------------|------------------------|------------|---|------------|--------------------------------------|------------|
| | Total | % of Total | Total | % of Total | Total | % of Total | For the Year Ended December 31, 2004 | |
| | | | | | | | Total | % of Total |
| | | | | | | | (\$000 s and unaudited) | |
| Los Angeles County | | | | | | | | |
| West(4) | 30 | 25% | 32 | 16% | 5,044,621 | 28% | \$ 107,688 | 39% |
| North | 28 | 23% | 44 | 22% | 3,468,768 | 19% | 44,962 | 16% |
| South | 13 | 11% | 17 | 9% | 2,851,215 | 15% | 37,052 | 14% |
| Subtotal | 71 | 59% | 93 | 47% | 11,364,604 | 62% | 189,702 | 69% |
| Orange County | 20 | 17% | 51 | 26% | 3,255,079 | 18% | 39,602 | 14% |
| San Diego County | 23 | 19% | 35 | 18% | 2,695,678 | 15% | 36,418 | 13% |
| Ventura/ Kern Counties | 6 | 5% | 17 | 9% | 795,299 | 4% | 9,831 | 4% |
| Subtotal | 120 | 100% | 196 | 100% | 18,110,660 | 99% | \$ 275,553 | 100% |
| Renovation Building(5) | | | 1 | | 99,119 | 1% | 5 | |
| Total | 120 | 100% | 197 | 100% | 18,209,779 | 100% | \$ 275,558 | 100% |

(1) Includes one property with approximately 167,000 net rentable square feet held for disposition.

(2) Property Operating Results is a non-GAAP measure of performance. Property Operating Results is used by investors and our management to evaluate and compare the performance of our office properties and to determine trends in earnings and to compute the fair value of our properties as it is not affected by (1) the cost of funds of the property owner, (2) the impact of depreciation and amortization expenses as well as gains or losses from the sale of operating real estate assets that are included in net income computed in accordance with Generally Accepted Accounting Principles, or GAAP, or (3) general and administrative expenses and other specific costs such as permanent impairments to carrying costs. The cost of funds is eliminated from net income because it is specific to the particular financing capabilities and constraints of the owner. The cost of funds is also eliminated because it is dependent on historical interest rates and other costs of capital as well as past decisions made by us regarding the appropriate mix of capital which may have changed or may change in the future. Depreciation and amortization expenses as well as gains or losses from the sale of operating real estate assets are eliminated because they may not accurately represent the actual change in value in our office properties that result from use of the properties or changes in market

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conditions. While certain aspects of real property do decline in value over time in a manner that is reasonably captured by depreciation and amortization, the value of the properties as a whole have historically increased or decreased in value as a result of changes in overall economic conditions instead of from actual use of the property or the passage of time. Gains and losses from the sale of real property vary from property to property and are affected by market conditions at the time of sale which will usually change from period to period. These gains and losses can create distortions when comparing one period to another or when comparing our operating results to the operating results of other real estate companies that have not made similarly timed purchases or sales. We believe that eliminating these costs from net income is useful because the resulting measure captures the actual revenue generated and actual expenses incurred in operating our office properties as well as trends in occupancy rates, rental rates and operating costs.

However, the usefulness of Property Operating Results is limited because it excludes general and administrative costs, interest expense, interest income, depreciation and amortization expense and gains or losses from the sale of properties, changes in value in our real estate properties that result from use or permanent impairment to carrying costs as stipulated by GAAP, the level of capital expenditures and leasing costs necessary to maintain the operating performance of our properties, all of which are significant economic costs. Property Operating Results may fail to capture significant trends in these components of net income which further limits its usefulness.

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Property Operating Results is a measure of the operating performance of our office properties but does not measure our performance as a whole. Property Operating Results is therefore not a substitute for net income as computed in accordance with GAAP. This measure should be analyzed in conjunction with net income computed in accordance with GAAP and discussions elsewhere in Management's Discussion and Analysis of Financial Condition and Results of Operations regarding the components of net income that are eliminated in the calculation of Property Operating Results. Other companies may use different methods for calculating Property Operating Results or similarly entitled measures and, accordingly, our Property Operating Results may not be comparable to similarly entitled measures reported by other companies that do not define the measure exactly as we do.

The following is a reconciliation of Property Operating Results to net income computed in accordance with GAAP (in thousands):

| | Year Ended December 31, | | |
|---|-------------------------|------------------|------------------|
| | 2004 | 2003 | 2002 |
| Net Income | \$ 73,775 | \$ 58,509 | \$ 70,175 |
| Add: | | | |
| General and administrative expense | 19,503 | 16,931 | 12,581 |
| Interest expense | 88,856 | 93,093 | 87,827 |
| Depreciation and amortization | 121,687 | 111,952 | 100,317 |
| Minority interest | 5,255 | 5,375 | 5,816 |
| Interest and other loss | 508 | 401 | |
| Impairment on investment in securities | 2,700 | | |
| Less: | | | |
| Interest and other income | | | (2,063) |
| Gain on sale of discontinued properties | (30,473) | (5,937) | |
| Discontinued operations, net of minority interest | (6,253) | (12,538) | (15,570) |
| Gain on sale of operating properties | | | (1,967) |
| Property Operating Results | <u>\$275,558</u> | <u>\$267,786</u> | <u>\$257,116</u> |

- (3) Excludes the operating results of two properties sold during the first quarter of 2004, one property sold during the third quarter of 2004, nine properties sold during the fourth quarter of 2004 and one property classified as held for disposition. The operating results for these properties are reported as part of discontinued operations in our consolidated statements of income.
- (4) Includes a retail property with approximately 37,000 net rentable square feet.
- (5) Comprised of one building in a business park containing a total of four buildings. After completion of the renovation, the total square footage of this building will expand to 130,000 square feet.

The following is a summary of our occupancy and in-place rents as of December 31, 2004:

| Location | Percent Occupied | Percent Leased | Annualized Base Rent Per Leased Square Foot(1) | |
|----------------------------|------------------|----------------|--|------------------------------|
| | | | Portfolio Total | Full Service Gross Leases(2) |
| Los Angeles County | | | | |
| West | 93.5% | 94.8% | \$27.80 | \$27.81 |
| North | 91.9% | 94.7% | 22.26 | 22.96 |
| South | 89.5% | 91.0% | 19.03 | 20.15 |
| Subtotal/ Weighted Average | <u>92.0%</u> | <u>93.8%</u> | <u>23.96</u> | <u>24.67</u> |
| Orange County | 90.0% | 91.3% | 18.69 | 22.31 |
| San Diego County | 87.8% | 88.5% | 19.87 | 24.26 |
| Ventura/ Kern Counties | 95.0% | 96.1% | 18.84 | 19.61 |

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| | | | | |
|----------------------------|-------|--------|---------|---------|
| Subtotal/ Weighted Average | 91.2% | 92.7% | 22.21 | 24.08 |
| Renovation Building | | 100.0% | 17.40 | |
| Total/ Weighted Average | 90.5% | 92.7% | \$22.18 | \$24.08 |

(1) Based on monthly contractual base rent under existing leases as of December 31, 2004, multiplied by 12 and divided by leased net rentable square feet; for those leases where rent has not yet commenced or which are in a free rent period, the first month in which rent is to be received is used to determine annualized base rent.

(2) Excludes 31 properties and approximately 3.5 million square feet under triple net and modified gross leases.

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The following table summarizes information about the building under renovation as of December 31, 2004:

| Building | Square Feet | Costs Incurred To Date | Estimated Total Cost(1) | Percent Leased | Estimated Construction Completion Date | Estimated Year 1 Stabilized Cash Property Operating Results(2) | Estimated Year 1 Annual Cash Yield | Estimated Year 1 Annual GAAP Yield(3) |
|--------------------------|--------------------|-------------------------------|--------------------------------|-----------------------|---|---|---|--|
| | | (in thousands) | (in thousands) | | | (in thousands) | | |
| 22745 Savi Ranch Parkway | 130,000 | \$ 7,659 | \$9,705 | 100% | 1st Qtr 2005 | \$ 1,881 | 9.6% | 11.2% |

- (1) Estimated total cost includes capital expenditures, tenant improvements, leasing commissions and carrying costs during renovation.
- (2) We consider stabilized Cash Property Operating Results to be the rental revenues from the property less the operating expenses of the property on a cash basis before deducting financing costs (interest and principal payments) after the property is at least 95% leased. Property Operating Results are discussed in greater detail in Note (2) to the Existing Portfolio summary table above.
- (3) Estimated Year 1 Annual GAAP Yield includes an adjustment for straight-line rents.
This renovation was completed on February 15, 2005.

In addition to the renovation building above, we have preliminary architectural designs completed for an additional 475,000 net rentable square feet of office space at the Howard Hughes Center in Los Angeles, California. We also have construction entitlements at the Howard Hughes Center for up to 600 hotel rooms. Build-to-suit projects consist of properties constructed to the tenant's specifications in return for the tenant's long-term commitment to the property. We do not intend to commence construction on any additional build-to-suit or multi-tenant projects at the Howard Hughes Center until development plans and budgets are finalized with terms allowing us to achieve yields commensurate with the project's development risk.

In addition to our development at the Howard Hughes Center, we have completed preliminary designs and are marketing an approximately 170,000 net rentable square foot build-to-suit office building at our Long Beach Airport Business Park. We also have a 5-acre developable land parcel in Torrance, California that we intend to market for a build-to-suit building. We currently do not intend to commence construction on these projects until build-to-suit tenant leases are signed with terms allowing us to achieve yields commensurate with the project's development risk.

We expect to finance our development/renovation activities over the next 24 months through net cash provided by operating activities, proceeds from asset sales, proceeds from our lines of credit or other secured borrowings.

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The following table summarizes our disposition activity during 2004:

| Property | County | Submarket | Date of Sale | Property Type | Square Feet | Gross Sales Price |
|-----------------------------|---------------|-----------------------|---------------------|----------------------|--------------------|--------------------------|
| | | | | | | (\$000 s) |
| Tower Plaza Retail | Riverside | Temecula | February 4, 2004 | Retail | 133,481 | \$ 17,050 |
| Univision 5999 Center Drive | Los Angeles | Culver City/Fox Hills | March 16, 2004 | Office | 161,650 | 52,500 |
| 10251 Vista Sorrento | San Diego | Sorrento Mesa | August 24, 2004 | Office | 69,386 | 9,250 |
| Waples Tech Center | San Diego | Sorrento Mesa | December 29, 2004 | Office | 28,119 | (A) |
| Morehouse Center | San Diego | Sorrento Mesa | December 29, 2004 | Office | 181,207 | (A) |
| 91 Freeway Center | Los Angeles | Artesia | December 29, 2004 | Office | 93,277 | (A) |
| Norwalk | Los Angeles | Norwalk | December 29, 2004 | Office | 122,175 | (A) |
| 1501 Hughes Way | Los Angeles | Suburban Long Beach | December 29, 2004 | Office | 77,060 | (A) |
| 3901 Via Oro | Los Angeles | Suburban Long Beach | December 29, 2004 | Office | 53,195 | (A) |
| Glendale Corporate Center | Los Angeles | Glendale | December 29, 2004 | Office | 108,209 | (A) |
| Whittier | Los Angeles | Whittier | December 29, 2004 | Office | 135,415 | (A) |
| South Bay Tech | Los Angeles | 190th Corridor | December 29, 2004 | Office | 104,815 | (A) |
| Sub-total | | | | | 1,267,989 | 78,800 |
| (A) Portfolio sale | | | | | 1,267,989 | 126,000 |
| | | | | | 1,267,989 | \$204,800 |

Acquisitions

The following table summarizes our acquisition activity during 2004:

| Property | County | Submarket | Date of Purchase | Property Type | Square Feet | Gross Purchase Price |
|-------------------------|---------------|------------------|-------------------------|----------------------|--------------------|-----------------------------|
| | | | | | | (\$000 s) |
| Homestore | Los Angeles | Westlake Village | October 4, 2004 | Office | 137,762 | \$32,300 |
| Warner Corporate Center | Los Angeles | Woodland Hills | October 11, 2004 | Office | 253,000 | 64,500 |

390,762

\$96,800

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The following table presents specific information regarding our 120 properties as of December 31, 2004:

| Property Name | Major Area | Submarket | Year(s) Built/ Renovated | Approximate Net Rentable Square Feet | Percentage of Total Portfolio Net Rentable Square Feet | Percent Leased | Annualized Base Rent (\$000s) | Number of Leases | Annualized Base Rent per Leased Net Rentable Square Feet(1) |
|-----------------------------|-----------------------------|------------------------|-----------------------------|--|---|-------------------|-------------------------------------|---------------------|--|
| Los Angeles County | | | | | | | | | |
| <i>Los Angeles West</i> | | | | | | | | | |
| 145 South Fairfax | Hollywood/Wilshire Corridor | Miracle Mile | 1984 | 54,398 | 0.3% | 95.5% | \$ 1,032 | 13 | \$ 19.86 |
| 6100 Wilshire | Hollywood/Wilshire Corridor | Miracle Mile | 1986 | 202,675 | 1.1 | 100.0 | 5,051 | 57 | 24.43 |
| 120 S. Spalding | West Los Angeles | Beverly Hills Triangle | 1984 | 64,877 | 0.4 | 97.5 | 2,700 | 15 | 42.67 |
| 8383 Wilshire | West Los Angeles | Beverly Hills | 1971/93 | 424,588 | 2.3 | 91.7 | 10,100 | 134 | 25.93 |
| 9100 Wilshire | West Los Angeles | Beverly Hills | 1971/90 | 328,697 | 1.8 | 92.7 | 8,300 | 76 | 27.25 |
| 9665 Wilshire | West Los Angeles | Beverly Hills Triangle | 1972/92-93 | 159,645 | 0.9 | 100.0 | 6,140 | 24 | 38.34 |
| Beverly Atrium | West Los Angeles | Beverly Hills | 1989 | 59,582 | 0.3 | 96.6 | 1,718 | 15 | 29.85 |
| Wilshire Pacific Plaza | West Los Angeles | Brentwood | 1976/87 | 101,229 | 0.6 | 99.6 | 2,561 | 43 | 25.39 |
| World Savings Center(2) | West Los Angeles | Brentwood | 1983 | 473,581 | 2.6 | 86.4 | 12,440 | 54 | 30.41 |
| 10350 Santa Monica | West Los Angeles | West Los Angeles | 1979 | 42,696 | 0.2 | 92.5 | 902 | 17 | 22.84 |
| 10351 Santa Monica | West Los Angeles | West Los Angeles | 1984 | 96,899 | 0.5 | 87.3 | 1,998 | 14 | 23.63 |
| Century Park Center | West Los Angeles | West Los Angeles | 1972/94 | 235,178 | 1.3 | 100.0 | 5,606 | 98 | 23.33 |
| 400 Corporate Pointe | West Los Angeles | Culver City/Fox Hills | 1987 | 165,487 | 0.9 | 85.9 | 2,732 | 19 | 19.23 |
| 600 Corporate Pointe | West Los Angeles | Culver City/Fox Hills | 1989 | 275,113 | 1.5 | 95.1 | 5,523 | 19 | 21.10 |
| 6060 Center Drive | West Los Angeles | Culver City/Fox Hills | 1999 | 256,665 | 1.4 | 99.1 | 8,280 | 8 | 32.55 |
| 6080 Center Drive | West Los Angeles | Culver City/Fox Hills | 2001 | 286,568 | 1.6 | 93.2 | 9,643 | 15 | 36.11 |
| 6100 Center Drive | West Los Angeles | Culver City/Fox Hills | 2002 | 284,798 | 1.6 | 99.4 | 7,278 | 24 | 25.72 |
| Bristol Plaza | West Los Angeles | Culver City/Fox Hills | 1982 | 84,033 | 0.5 | 95.3 | 1,640 | 28 | 20.47 |
| Howard Hughes Spectrum Club | West Los Angeles | Culver City/Fox Hills | 1993 | 36,959 | 0.2 | 100.0 | 967 | 1 | 26.16 |
| Howard Hughes Tower | West Los Angeles | Culver City/Fox Hills | 1987 | 316,014 | 1.7 | 87.0 | 7,541 | 33 | 27.44 |
| Northpoint | West Los Angeles | Culver City/Fox Hills | 1991 | 105,145 | 0.6 | 94.1 | 2,638 | 7 | 26.67 |
| 1919 Santa Monica | West Los Angeles | Santa Monica | 1991 | 43,766 | 0.2 | 85.2 | 947 | 7 | 25.41 |
| 2001 Wilshire Blvd. | West Los Angeles | Santa Monica | 1980 | 99,565 | 0.5 | 100.0 | 2,805 | 23 | 27.47 |
| 2730 Wilshire | West Los Angeles | Santa Monica | 1985 | 55,531 | 0.3 | 100.0 | 1,553 | 26 | 27.57 |
| 2800 28th Street | West Los Angeles | Santa Monica | 1979 | 106,481 | 0.6 | 95.9 | 2,456 | 42 | 24.06 |
| 10780 Santa Monica | West Los Angeles | West Los Angeles | 1984 | 93,211 | 0.5 | 97.0 | 2,193 | 33 | 24.26 |
| 1950 Sawtelle | West Los Angeles | West Los Angeles | 1988/95 | 104,171 | 0.6 | 98.0 | 2,367 | 42 | 23.17 |
| 11075 Santa Monica | West Los Angeles | West Los Angeles | 1983 | 35,996 | 0.2 | 99.1 | 877 | 8 | 24.57 |

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| | | | | | | | | | |
|------------------|------------------|------------------------------|-----------|---------|-----|------|--------|----|-------|
| Westwood Center | West Los Angeles | West Los Angeles Westwood | 1965/2000 | 314,366 | 1.7 | 99.6 | 11,366 | 45 | 36.30 |
| Westwood Terrace | West Los Angeles | West Los Angeles | 1988 | 136,707 | 0.8 | 98.3 | 3,549 | 22 | 26.41 |

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| Property Name | Major Area | Submarket | Year(s) Built/ Renovated | Approximate Net Rentable Square Feet | Percentage of Total Portfolio Net Rentable Square Feet | Percent Leased | Annualized Base Rent (\$000s) | Number of Leases | Annualized Base Rent per Leased Net Rentable Square Feet(1) |
|--|---------------------|----------------------------|-----------------------------|--------------------------------------|--|----------------|-------------------------------|------------------|---|
| Subtotal/Weighted Average Los Angeles West | | | | | | | | | |
| | | | | 5,044,621 | 27.7% | 94.8% | \$ 132,903 | 962 | \$ 27.80 |
| <i>Los Angeles North</i> | | | | | | | | | |
| 303 Glenoaks | Glendale/Tri-Cities | Burbank | 1983/96 | 177,898 | 1.0% | 99.4% | \$ 4,028 | 28 | \$ 22.78 |
| 333 N. Glenoaks | Glendale/Tri-Cities | Burbank | 1978 | 82,939 | 0.5 | 98.0 | 1,921 | 17 | 23.62 |
| 601 S. Glenoaks | Glendale/Tri-Cities | Burbank | 1990 | 74,745 | 0.4 | 87.4 | 1,206 | 18 | 18.45 |
| <i>Burbank</i> | | | | | | | | | |
| Executive Plaza | Glendale/Tri-Cities | Burbank | 1983 | 63,320 | 0.3 | 99.0 | 1,437 | 19 | 22.92 |
| <i>425 West Broadway</i> | | | | | | | | | |
| 535 N. Brand Blvd. | Glendale/Tri-Cities | Glendale | 1984 | 72,317 | 0.4 | 94.9 | 1,456 | 14 | 21.21 |
| 5161 Lankershim | Glendale/Tri-Cities | Glendale North | 1973/92/99 | 109,104 | 0.6 | 96.6 | 2,233 | 44 | 21.19 |
| 70 South Lake | Glendale/Tri-Cities | Hollywood | 1985/97 | 180,940 | 1.0 | 99.4 | 3,964 | 9 | 22.05 |
| 150 East Colorado Boulevard | Glendale/Tri-Cities | Pasadena | 1982/94 | 101,236 | 0.5 | 99.9 | 2,627 | 19 | 25.97 |
| <i>299 N. Euclid</i> | | | | | | | | | |
| Calabasas Commerce Center | Glendale/Tri-Cities | Pasadena | 1979/97 | 61,657 | 0.3 | 100.0 | 1,447 | 20 | 23.47 |
| Calabasas Tech | Glendale/Tri-Cities | Pasadena | 1983 | 74,573 | 0.4 | 100.0 | 1,890 | 4 | 25.30 |
| <i>San Fernando Valley</i> | | | | | | | | | |
| 16000 Ventura | San Fernando Valley | Calabasas | 1990 | 126,771 | 0.7 | 100.0 | 2,323 | 12 | 18.32 |
| 15250 Ventura | San Fernando Valley | Calabasas | 1990/2001 | 283,692 | 1.5 | 90.3 | 4,837 | 17 | 18.89 |
| | San Fernando Valley | Encino | 1980/96 | 175,275 | 1.0 | 93.2 | 3,628 | 45 | 22.21 |
| | San Fernando Valley | Sherman Oaks | 1970/90-91 | 112,142 | 0.6 | 93.1 | 2,438 | 41 | 23.35 |
| <i>Noble Professional Center</i> | | | | | | | | | |
| Sunset Pointe Plaza | San Fernando Valley | Sherman Oaks | 1985/93 | 52,599 | 0.3 | 92.8 | 1,129 | 18 | 23.11 |
| Tourney Pointe | San Fernando Valley | Valencia | 1988 | 59,186 | 0.3 | 99.7 | 1,500 | 27 | 25.42 |
| Homestore | San Fernando Valley | Valencia | 1985/98-2000 | 219,673 | 1.2 | 92.1 | 4,196 | 38 | 20.74 |
| Westlake 5601 Lindero | San Fernando Valley | Westlake Village | 2000 | 137,762 | 0.8 | 100.0 | 3,036 | 1 | 22.04 |
| Clarendon Crest | San Fernando Valley | Westlake Village | 1989 | 106,144 | 0.6 | 95.3 | 1,894 | 5 | 18.73 |
| Warner Corporate Center | San Fernando Valley | Woodland Hills | 1990 | 43,222 | 0.2 | 97.9 | 887 | 18 | 20.95 |
| Woodland Hills | San Fernando Valley | Woodland Hills | 1988 | 253,000 | 1.4 | 98.9 | 6,433 | 34 | 25.71 |
| | San Fernando Valley | Woodland Hills | 1972/95 | 229,616 | 1.3 | 93.0 | 4,874 | 73 | 22.82 |
| <i>Los Angeles Corporate Center</i> | | | | | | | | | |
| Conejo Business Center | San Gabriel Valley | Monterey Park | 1984/86 | 389,615 | 2.1 | 90.6 | 7,552 | 45 | 21.40 |
| | Ventura | Newbury Park/Thousand Oaks | 1991 | 69,425 | 0.4 | 92.9 | 1,375 | 29 | 21.32 |
| | Ventura | Oaks | 1998 | 61,000 | 0.3 | 97.3 | 1,564 | 10 | 26.36 |

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| | | | | | | | | | |
|----------------------------|-------------------|----------------------------|---------|-----------|-------|--------|-----------|-----|----------|
| Hillside Corporate Center | | Newbury Park/Thousand Oaks | | | | | | | |
| Marin Corporate Center | Ventura | Newbury Park/Thousand Oaks | 1986 | 51,776 | 0.3 | 64.9 | 778 | 27 | 23.14 |
| Westlake Gardens | Ventura | Westlake Village | 1998 | 50,267 | 0.3 | 94.0 | 1,288 | 19 | 27.27 |
| Westlake Gardens II | Ventura | Westlake Village | 1999 | 48,874 | 0.3 | 93.1 | 1,229 | 4 | 27.02 |
| Subtotal/ Weighted Average | Los Angeles North | | | 3,468,768 | 19.0% | 94.7% | \$ 73,170 | 655 | \$ 22.26 |
| <i>Los Angeles</i> | | | | | | | | | |
| <i>South</i> | | | | | | | | | |
| <i>South Bay</i> | | | | | | | | | |
| Centre | South Bay | 190th Corridor | 1984 | 204,197 | 1.1% | 100.0% | \$ 4,150 | 36 | \$ 20.30 |
| Pacific Gateway | South Bay | 190th Corridor | 1982/90 | 225,805 | 1.2 | 97.4 | 4,617 | 40 | 20.99 |
| Gateway Towers | South Bay | 190th Corridor | 1984/86 | 433,545 | 2.4 | 95.3 | 9,448 | 74 | 22.88 |

Huntington Beach Orange County
Plaza County 1984/96

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| Property Name | Major Area | Submarket | Year(s) Built/ Renovated | Approximate Net Rentable Square Feet | Percentage of Total Portfolio Net Rentable Square Feet | Percent Leased | Annualized Base Rent (\$000s) | Number of Leases | Annualized Base Rent per Leased Net Rentable Square Feet(1) |
|--|---------------------|--------------------------|-----------------------------|--|---|-------------------|-------------------------------------|---------------------|---|
| Huntington Commerce Center | Orange County | West County | 1987 | 69,749 | 0.4 | 98.4 | 638 | 23 | 9.29 |
| Subtotal/ Weighted Average Orange County | | | | 3,255,079 | 17.9% | 91.3% | \$ 55,518 | 470 | \$ 18.69 |
| San Diego County | | | | | | | | | |
| Carlsbad Corporate Center | San Diego County | Carlsbad | 1996 | 129,000 | 0.7% | 100.0% | \$ 445 | 1 | \$ 3.45 |
| Carmel Valley Center | San Diego County | Del Mar Heights | 1987/89 | 109,518 | 0.6 | 93.8 | 3,410 | 17 | 33.20 |
| 701 B Street(2) | San Diego County | Downtown | 1982/96 | 548,310 | 3.0 | 87.3 | 11,023 | 70 | 23.04 |
| 5120 Shoreham | San Diego County | Governor Park | 1984 | 37,813 | 0.2 | 100.0 | 842 | 7 | 22.24 |
| Governor Executive Centre | San Diego County | Governor Park | 1988 | 52,828 | 0.3 | 85.1 | 1,175 | 10 | 26.12 |
| Governor Executive Centre II | San Diego County | Governor Park | 1989 | 101,433 | 0.6 | 100.0 | 3,006 | 17 | 29.64 |
| Governor Park Plaza | San Diego County | Governor Park | 1986 | 104,441 | 0.6 | 94.0 | 2,485 | 19 | 25.31 |
| 10180 Scripps Ranch | San Diego County | Scripps Ranch | 1978/96 | 43,560 | 0.2 | 0 | 0 | 0 | 0 |
| Activity Business Center | San Diego County | Miramar | 1987 | 167,170 | 0.9 | 72.3 | 1,652 | 41 | 13.66 |
| Balboa Corporate Center | San Diego County | Kearney Mesa | 1990 | 70,987 | 0.4 | 75.8 | 777 | 2 | 14.44 |
| Panorama Corporate Center | San Diego County | Kearney Mesa | 1991 | 130,396 | 0.7 | 99.6 | 2,392 | 3 | 18.42 |
| Ruffin Corporate Center | San Diego County | Kearney Mesa | 1990 | 45,059 | 0.2 | 100.0 | 378 | 1 | 8.40 |
| Skypark Office Plaza | San Diego County | Kearney Mesa | 1986 | 203,946 | 1.1 | 96.9 | 4,423 | 24 | 22.39 |
| Crossroads | San Diego County | Mission Valley Rancho | 1979 | 134,477 | 0.7 | 65.8 | 2,093 | 8 | 23.64 |
| Poway Industrial | San Diego County | Bernardo/Poway Rancho | 1991/96 | 112,000 | 0.6 | 100.0 | 672 | 1 | 6.00 |
| Bernardo Regency | San Diego County | Bernardo/Poway Rancho | 1986 | 48,052 | 0.3 | 93.3 | 1,145 | 16 | 25.54 |
| Carmel View Office Plaza | San Diego County | Bernardo/Poway Rancho | 1985 | 77,672 | 0.4 | 84.1 | 1,497 | 16 | 22.92 |
| Cymer Technology Center | San Diego County | Bernardo/Poway Rancho | 1986 | 155,612 | 0.9 | 100.0 | 1,923 | 2 | 12.36 |
| Foremost Professional Plaza | San Diego County | Bernardo/Poway Rancho | 1992 | 60,311 | 0.3 | 73.6 | 1,113 | 29 | 25.06 |
| Via Frontera | San Diego County | Bernardo/Poway Rancho | 1982/97 | 77,920 | 0.4 | 100.0 | 914 | 6 | 11.60 |
| Westridge | San Diego County | Sorrento Mesa | 1984/96 | 48,955 | 0.3 | 82.4 | 551 | 3 | 13.65 |
| Torreyana Science Park | San Diego County | Torrey Pines | 1980/97 1984 | 81,204 155,014 | 0.5 0.9 | 100.0 87.5 | 2,008 3,493 | 1 23 | 24.72 25.75 |

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| Genesee Executive Plaza | San Diego County | University Towne Centre | | | | | | |
|---|---------------------|----------------------------|-----------|-------|-------|----------|-----|---------|
| Subtotal/ Weighted Average San Diego County | | | 2,695,678 | 14.8% | 88.5% | \$47,417 | 317 | \$19.87 |

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| Property Name | Submarket | Location | Year(s) Built/ Renovated | Approximate Net Rentable Square Feet | Percentage of Total Portfolio Net Rentable Square Feet | Percent Leased | Annualized Base Rent (\$000s) | Number of Leases | Annualized Base Rent per Leased Net Rentable Square Feet(1) |
|--|------------------|-----------------|-------------------------------------|---|---|-----------------------|--------------------------------------|-------------------------|--|
| Ventura & Kern Counties | | | | | | | | | |
| 4900 California | Kern County | Bakersfield | 1983 | 155,791 | 0.9% | 95.6% | \$ 2,385 | 23 | \$ 16.01 |
| Parkway Center I | Kern County | Bakersfield | 1992/95 | 61,289 | 0.3 | 90.8 | 1,038 | 11 | 18.64 |
| Camarillo | | | | | | | | | |
| Business Park | Ventura | Camarillo | 1984/97 | 154,298 | 0.8 | 97.5 | 3,134 | 29 | 20.83 |
| 1000 Town Center | Ventura | Oxnard | 1989 | 108,508 | 0.6 | 99.8 | 2,379 | 10 | 21.96 |
| Solar Drive | | | | | | | | | |
| Business Center | Ventura | Oxnard | 1982 | 138,341 | 0.8 | 98.0 | 2,494 | 36 | 18.39 |
| Center Promenade | Ventura | Ventura | 1988 | 177,072 | 1.0 | 93.4 | 2,969 | 61 | 17.96 |
| Subtotal/ Weighted Average Ventura & Kern Counties | | | | 795,299 | 4.4% | 96.1% | \$ 14,399 | 170 | \$ 18.84 |
| Renovation Building | | | | | | | | | |
| Savi Tech | | | | | | | | | |
| Center(3) | Orange County | North County | 1989 | 99,119 | 0.5% | 100.0% | \$ 2,262 | 1 | \$ 17.40 |
| Portfolio Total/ Weighted Average | | | | 18,209,779 | 100.0% | 92.7% | \$ 375,040 | 3,024 | \$ 22.18 |

(1) Calculated as monthly contractual base rent under existing leases as of December 31, 2004, multiplied by 12 and divided by leased net rentable square feet, for those leases where rent has not yet commenced or which are in a free rent period, the first month in which rent is to be received is used to determine annualized base rent.

(2) We lease the land underlying these properties or their parking structures pursuant to long term ground leases.

(3) Comprised of one building in a business park containing a total of four buildings. After completion of the renovation, the total square footage of this building will expand to 130,000 square feet. The annualized base rent and the annualized base rent per leased net rentable square feet amounts are calculated based on the expanded square footage of 130,000 square feet.

Table of Contents*Tenant Information*

As of December 31, 2004, we had approximately 3,000 tenants with no one tenant representing more than 2.2% of the aggregate annualized base rent of our properties and only 2 tenants individually representing more than 1.0% of our aggregate annualized base rent. Our properties are leased to local, national and international companies engaged in a variety of businesses including financial services, entertainment, health care services, accounting, law, education, publishing and local, state and federal government entities.

Our leases are typically structured for terms of three to ten years. Leases typically contain provisions permitting tenants to renew expiring leases at prevailing market rates. Approximately 81% of our total rentable square footage is under full service gross leases under which tenants typically pay for all real estate taxes and operating expenses above those for an established base year or expense stop. Our remaining square footage is under triple net and modified gross leases. Triple net and modified gross leases are those where tenants pay not only base rent, but also some or all of real estate taxes and operating expenses of the leased property. Tenants generally reimburse us the full direct cost, without regard to a base year or expense stop, for use of lighting, heating and air conditioning during non-business hours, and for on-site monthly employee and visitor parking. We are generally responsible for structural repairs to our buildings.

The following table presents information as of December 31, 2004 derived from our ten largest tenants based on the percentage of aggregate portfolio annualized base rent:

| Tenant | Number of Locations | Weighted Average Lease Term Remaining in Months | Percentage of Aggregate Portfolio Leased Square Feet | Percentage of Aggregate Portfolio Annualized Base Rent(1) | Net Rentable Square Feet | Annualized Base Rent (in thousands) |
|-------------------------------------|---------------------|---|--|---|--------------------------|-------------------------------------|
| Vivendi Universal | 2 | 64 | 1.38% | 2.14% | 231,681 | \$ 7,980 |
| State of California | 18 | 51 | 1.63 | 1.61 | 274,065 | 5,992 |
| University of Phoenix | 6 | 52 | 0.99 | 1.00 | 166,195 | 3,733 |
| Ceridian Corporation | 2 | 64 | 0.91 | 0.99 | 152,612 | 3,706 |
| Atlantic Richfield | 1 | 21 | 0.86 | 0.93 | 143,885 | 3,465 |
| Pepperdine University | 1 | 167 | 0.68 | 0.87 | 113,488 | 3,251 |
| Homestore.com, Inc. | 1 | 37 | 0.82 | 0.82 | 137,762 | 3,036 |
| Walt Disney Pictures and Television | 1 | 43 | 0.76 | 0.78 | 128,258 | 2,894 |
| Haight, Brown & Bonesteel, LLP | 2 | 77 | 0.38 | 0.73 | 63,262 | 2,736 |
| Westfield Corporation | 1 | 100 | 0.58 | 0.73 | 96,876 | 2,725 |
| Total/ Weighted Average(2) | 35 | 63 | 8.99% | 10.60% | 1,508,084 | \$39,518 |

(1) Annualized base rent is calculated as monthly contractual base rent under existing leases as of December 31, 2004, multiplied by 12; for those leases where rent has not yet commenced or which are in a free rent period, the first month in which rent is to be received is used to determine annualized base rent.

(2) The weighted average calculation is based on net rentable square footage leased by each tenant.

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The following table presents the diversification of the tenants occupying space in our portfolio by industry as of December 31, 2004:

| North American Industrial Classification System Description (NAICS) | NAICS Code | Occupied Square Feet | Percentage of Total Occupied Portfolio |
|--|------------|----------------------|--|
| Professional, Scientific, and Technical Services | 541 | 4,278,468 | 25.91% |
| Finance and Insurance | 521-525 | 2,838,317 | 17.19 |
| Information | 511-519 | 1,625,403 | 9.84 |
| Manufacturing | 311-339 | 1,282,143 | 7.77 |
| Health Care and Social Assistance | 621-624 | 1,107,178 | 6.71 |
| Educational Services | 611 | 750,882 | 4.55 |
| Administrative and Support and Waste Management and Remediation Services | 561-562 | 742,831 | 4.50 |
| Real Estate, Rental and Leasing | 531-533 | 709,020 | 4.29 |
| Public Administration | 921-928 | 638,857 | 3.87 |
| Wholesale Trade | 423-425 | 564,150 | 3.42 |
| Construction | 236-238 | 334,098 | 2.02 |
| Transportation and Warehousing | 481-493 | 319,070 | 1.93 |
| Other Services (except Public Administration) | 811-814 | 295,987 | 1.79 |
| Arts, Entertainment, and Recreation | 711-713 | 287,027 | 1.74 |
| Accommodation and Food Services | 721-722 | 180,608 | 1.09 |
| Retail Trade | 441-454 | 112,738 | 0.68 |
| Mining | 211-213 | 41,291 | 0.25 |
| Management of Companies and Enterprises | 551 | 34,410 | 0.21 |
| Utilities | 221 | 8,975 | 0.05 |
| Agriculture, Forestry, Fishing and Hunting | 111-115 | 6,261 | 0.04 |
| Other Uncategorized | | 352,346 | 2.15 |
| Total Square Feet Occupied | | 16,510,060 | 100.00% |

Lease Distribution

The following table presents information relating to the distribution of the leases for our 120 properties, based on leased net rentable square feet, as of December 31, 2004:

| Square Feet Under Lease | Number of Leases | Percent of All Leases | Total Leased Square Feet | Percent of Aggregate Portfolio Leased Square Feet | Annualized Base Rent of Leases(1) (000 \$) | Avg. Base Rent per Leased Square Foot | Percent of Aggregate Portfolio Annualized Base Rent |
|--------------------------------|------------------|-----------------------|--------------------------|---|---|---------------------------------------|---|
| 2,500 and under | 1,490 | 49.29% | 2,114,663 | 12.60% | \$ 50,567 | \$23.91 | 12.42% |
| 2,501 - 5,000 | 704 | 23.29 | 2,447,176 | 14.58 | 60,844 | 24.86 | 14.95 |
| 5,001 - 7,500 | 299 | 9.89 | 1,813,171 | 10.80 | 46,939 | 25.89 | 11.53 |
| 7,501 - 10,000 | 164 | 5.43 | 1,432,241 | 8.54 | 36,027 | 25.15 | 8.85 |
| 10,001 - 20,000 | 241 | 7.97 | 3,405,929 | 20.30 | 85,663 | 25.15 | 21.04 |
| 20,001 - 40,000 | 78 | 2.58 | 2,118,322 | 12.62 | 51,036 | 24.09 | 12.54 |
| 40,001 and over | 47 | 1.55 | 3,451,173 | 20.56 | 76,002 | 22.02 | 18.67 |
| Total/ Weighted Average | 3,023 | 100.00% | 16,782,675 | 100.00% | \$407,078 | \$24.26 | 100.00% |

(1) Base rent is determined as of the date of lease expiration, including all fixed contractual base rent increases; increases tied to indices such as the Consumer Price Index are not included.

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The following table presents a summary schedule of the total lease expirations for our 120 properties for leases in place at December 31, 2004. This table assumes that none of the tenants exercise renewal options or termination rights, if any, at or prior to the scheduled expirations:

| Year of Lease Expiration | Number of Leases Expiring | Square Footage of Expiring Leases | Percentage of Aggregate Leased Square Feet | Annualized Base Rent of Expiring Leases(1) (\$000s) | Average Annualized Base Rent per Square Foot of Expiring Leases | Percentage of Aggregate Portfolio Annualized Base Rent |
|---------------------------------|----------------------------------|--|---|--|--|---|
| Month-to-Month | 113 | 499,517 | 2.98% | \$ 8,878 | \$17.77 | 2.18% |
| Q1 2005 | 136 | 465,009 | 2.77 | 9,421 | 20.26 | 2.31 |
| Q2 2005 | 160 | 623,578 | 3.72 | 13,792 | 22.12 | 3.39 |
| Q3 2005 | 167 | 624,148 | 3.72 | 14,522 | 23.27 | 3.57 |
| Q4 2005 | 188 | 802,859 | 4.78 | 17,347 | 21.61 | 4.26 |
| 2005 Sub-Total(2) | 651 | 2,515,594 | 14.99 | 55,082 | 21.90 | 13.53 |
| 2006 | 596 | 2,513,849 | 14.98 | 59,551 | 23.69 | 14.63 |
| 2007 | 529 | 2,416,185 | 14.40 | 56,854 | 23.53 | 13.97 |
| 2008 | 392 | 2,355,397 | 14.03 | 58,662 | 24.91 | 14.41 |
| 2009 | 344 | 2,139,029 | 12.74 | 51,137 | 23.91 | 12.56 |
| 2010 | 159 | 1,615,217 | 9.62 | 39,338 | 24.35 | 9.66 |
| 2011 | 53 | 704,942 | 4.20 | 22,102 | 31.35 | 5.43 |
| 2012 | 54 | 855,313 | 5.10 | 20,291 | 23.72 | 4.98 |
| 2013 | 34 | 411,142 | 2.45 | 12,195 | 29.66 | 3.00 |
| 2014+ | 98 | 756,490 | 4.51 | 22,988 | 30.39 | 5.65 |
| Total/ Weighted Average | 3,023 | 16,782,675 | 100.00% | \$407,078 | \$24.26 | 100.00% |

(1) Base rent is determined as of the date of lease expiration, including all fixed contractual base rent increases; increases tied to indices such as the Consumer Price Index are not included.

(2) Excludes month-to-month leases.

ITEM 3. Legal Proceedings

We are presently subject to various lawsuits, claims and proceedings arising in the ordinary course of business none of which if determined unfavorably to us is expected to have a material adverse effect on our cash flows, financial condition or results of operations during the year ended December 31, 2004.

ITEM 4. Submission of Matters to a Vote of Security Holders

No matters were submitted to a vote of our stockholders during the fourth quarter of the year ended December 31, 2004.

Table of Contents**PART II****ITEM 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities**

Our common stock is traded on the New York Stock Exchange, or NYSE, under the symbol ARI. On March 10, 2005, the last reported sales price per share of common stock on the NYSE was \$35.41 and there were approximately 226 registered holders of record of our common stock. The table below sets forth the quarterly high and low closing sales price per share of our common stock as reported on the NYSE and the cash dividends per share we declared with respect to each period.

| | High | Low | Per Share Common Stock Dividends Declared |
|----------------|-------------|------------|--|
| 2003 | | | |
| First Quarter | \$23.69 | \$20.18 | \$0.505 |
| Second Quarter | \$26.23 | \$22.68 | \$0.505 |
| Third Quarter | \$27.92 | \$26.15 | \$0.505 |
| Fourth Quarter | \$30.34 | \$27.49 | \$0.505 |
| 2004 | | | |
| First Quarter | \$32.75 | \$29.30 | \$0.505 |
| Second Quarter | \$32.86 | \$26.89 | \$0.505 |
| Third Quarter | \$33.15 | \$29.54 | \$0.505 |
| Fourth Quarter | \$37.72 | \$32.66 | \$0.505 |

We pay quarterly cash dividends to common stockholders at the discretion of our Board of Directors. The amount of each quarterly cash dividend depends on our funds from operations, financial condition, capital requirements and annual distribution requirements under the REIT provisions of the Internal Revenue Code and such other factors our Board of Directors deem relevant.

Table of Contents**ITEM 6. Selected Financial Data**

You should read the following consolidated financial and operating data for Arden Realty together with our Management's Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements included elsewhere in this Form 10-K.

| | Year Ended December 31, | | | | |
|--|--|------------|------------|------------|------------|
| | 2004 | 2003 | 2002 | 2001 | 2000 |
| | (in thousands, except ratio and per share amounts) | | | | |
| Operating Data: | | | | | |
| Property revenues | \$ 409,193 | \$ 393,765 | \$ 374,135 | \$ 382,839 | \$ 351,924 |
| Interest and other (loss) income | (508) | (401) | 2,063 | 2,135 | 3,290 |
| Property operating expenses | (133,635) | (125,979) | (117,019) | (110,421) | (100,574) |
| General and administrative expense | (19,503) | (16,931) | (12,581) | (11,496) | (9,103) |
| Depreciation and amortization | (121,687) | (111,952) | (100,317) | (92,613) | (78,672) |
| Interest expense | (88,856) | (93,093) | (87,827) | (85,949) | (78,495) |
| Income from continuing operations before gain on sale of operating properties, impairment on investment in securities, and minority interest | 45,004 | 45,409 | 58,454 | 84,495 | 88,370 |
| Gain on sale of operating properties(1) | | | 1,967 | 4,591 | 2,132 |
| Income from continuing operations before impairment on investment securities and minority interest | 45,004 | 45,409 | 60,421 | 89,086 | 90,502 |
| Impairment on investment in securities | (2,700) | | | | |
| Minority interest | (5,255) | (5,375) | (5,816) | (7,046) | (7,158) |
| Income from continuing operations | 37,049 | 40,034 | 54,605 | 82,040 | 83,344 |
| Discontinued operations, net of minority interest | 6,253 | 12,538 | 15,570 | 15,719 | 13,366 |
| Gain on sale of discontinued properties | 30,473 | 5,937 | | | |
| Net income | \$ 73,775 | \$ 58,509 | \$ 70,175 | \$ 97,759 | \$ 96,710 |
| Basic net income per common share: | | | | | |
| Income from continuing operations | \$ 0.57 | \$ 0.63 | \$ 0.85 | \$ 1.28 | \$ 1.32 |
| Income from discontinued operations | 0.56 | 0.29 | 0.24 | 0.25 | 0.21 |
| Net income per common share-basic | \$ 1.13 | \$ 0.92 | \$ 1.09 | \$ 1.53 | \$ 1.53 |
| Weighted average number of common shares-basic | 65,372 | 63,553 | 64,151 | 63,754 | 63,408 |
| Diluted net income per common share: | | | | | |
| Income from continuing operations | \$ 0.56 | \$ 0.63 | \$ 0.85 | \$ 1.28 | \$ 1.31 |
| Income from discontinued operations | 0.56 | 0.29 | 0.24 | 0.25 | 0.21 |

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| | | | | | |
|---|--------------|--------------|--------------|--------------|--------------|
| Net income per common share-diluted | \$ 1.12 | \$ 0.92 | \$ 1.09 | \$ 1.53 | \$ 1.52 |
| Weighted average number of common shares- diluted | \$ 65,740 | \$ 63,815 | \$ 64,351 | \$ 64,014 | \$ 63,598 |
| Cash dividends declared per common share | \$ 2.02 | \$ 2.02 | \$ 2.02 | \$ 1.96 | \$ 1.86 |
| Other Data: | | | | | |
| Cash provided by operating activities | \$ 184,907 | \$ 181,482 | \$ 199,922 | \$ 204,667 | \$ 192,152 |
| Cash used in investing activities | \$ (11,241) | \$ (20,355) | \$ (213,002) | \$ (115,854) | \$ (216,024) |
| Cash (used in) provided by financing activities | \$ (165,333) | \$ (160,483) | \$ (19,898) | \$ (57,204) | \$ 22,248 |
| Funds from Operations(2) | \$ 171,777 | \$ 174,458 | \$ 181,549 | \$ 198,240 | \$ 185,146 |

Selected financial data continues on next page.

Table of Contents**Year Ended December 31,**

| | 2004 | 2003 | 2002 | 2001 | 2000 |
|-------------------------------|--------------|--------------|--------------|--------------|--------------|
| Balance Sheet Data: | | | | | |
| Net investment in real estate | \$ 2,551,981 | \$ 2,646,699 | \$ 2,741,624 | \$ 2,622,980 | \$ 2,603,566 |
| Total assets | \$ 2,659,997 | \$ 2,741,433 | \$ 2,832,409 | \$ 2,761,443 | \$ 2,705,597 |
| Total indebtedness | \$ 1,326,084 | \$ 1,349,781 | \$ 1,402,304 | \$ 1,251,483 | \$ 1,177,769 |
| Other liabilities(3) | \$ 83,713 | \$ 76,638 | \$ 76,350 | \$ 62,685 | \$ 56,885 |
| Minority interests | \$ 20,414 | \$ 72,194 | \$ 74,571 | \$ 78,661 | \$ 86,176 |
| Total stockholders equity | \$ 1,196,292 | \$ 1,210,285 | \$ 1,247,377 | \$ 1,337,206 | \$ 1,355,171 |

- (1) Beginning with the adoption of the Statement of Financial Accounting Standard No. 144 in 2002, the operating results and gains and losses of real estate properties classified as held for disposition are included in discontinued operations.
- (2) We believe that funds from operations, or FFO, is a useful supplemental measure of our operating performance. We compute FFO in accordance with standards established by the White Paper on FFO approved by the Board of Governors of the National Association of Real Estate Investment Trusts, or NAREIT, in April 2002. The white paper defines FFO as net income or loss computed in accordance with generally accepted accounting principles, or GAAP, excluding extraordinary items, as defined by GAAP, and gains and losses from sales of depreciable operating property plus real estate-related depreciation and amortization and after adjustments for unconsolidated partnerships and joint ventures.

We believe that FFO, by excluding depreciation costs, the gains or losses from the sale of operating real estate properties and extraordinary items as defined by GAAP, provides an additional perspective on our operating results. However, because these items have real economic effect, FFO is a limited measure of performance.

FFO captures trends in occupancy rates, rental rates and operating costs. FFO excludes depreciation and amortization costs and it does not capture the changes in value in our properties that result from use or changes in market conditions or the level of capital expenditures and leasing costs necessary to maintain the operating performance of our properties, all of which are significant economic costs. Therefore, its ability to measure performance is limited.

Because FFO excludes significant economic components of net income determined in accordance with GAAP, FFO should be used as an adjunct to net income and not as an alternative to net income. FFO should also not be used as an indicator of our financial performance, or as a substitute for cash flow from operating activities determined in accordance with GAAP or as a measure of our liquidity. FFO is not by itself indicative of funds available to fund our cash needs, including our ability to pay dividends or service our debt. Therefore, FFO only provides investors with an additional performance measure that when combined with measures computed in accordance with GAAP such as net income, cash flow from operating activities, investing activities and financing activities provides investors with an indication of our ability to service debt and to fund acquisitions and other expenditures.

FFO is used by investors to compare our performance with other REITs. Other REITs may use different methodologies for calculating FFO and, accordingly, our FFO may not be comparable to other REITs. See a reconciliation of FFO to Net income in Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations of this report.

- (3) Excludes dividends payable.

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ITEM 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations*

Overview

The following discussion should be read in conjunction with Item 6, Selected Financial Data, and our historical consolidated financial statements and related notes thereto included elsewhere in this Form 10-K.

We are a self-administered and self-managed real estate investment trust that owns, manages, leases, develops, renovates and acquires commercial properties located in Southern California. We are a full-service real estate organization managed by 6 senior executive officers who have experience in the real estate industry ranging from 14 to 35 years and who collectively have an average of 20 years of experience. We perform all property management, construction management, accounting, finance, acquisition and disposition activities and a majority of our leasing transactions with our staff of approximately 300 employees.

As of December 31, 2004, we were Southern California's largest publicly traded office landlord as measured by total net rentable square feet owned. As of that date, our portfolio consisted of 120 primarily suburban office properties and 197 buildings containing approximately 18.2 million net rentable square feet. As of December 31, 2004, our operating portfolio was 91.2% occupied.

Our primary business strategy is to actively manage our portfolio to achieve gains in rental rates and occupancy, control operating expenses and maximize income from ancillary operations and services. When market conditions permit, we may also selectively develop or acquire new properties that add value and fit strategically into our portfolio. We may also sell existing properties and use the net proceeds to repay outstanding indebtedness or place into investments that we believe will generate higher long-term value.

Critical Accounting Policies

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses for the reporting periods. Certain accounting policies are considered to be critical accounting estimates, as they require management to make assumptions about matters that are highly uncertain at the time the estimate is made and changes in the accounting estimate are reasonably likely to occur from period to period. Management believes the following critical accounting policies reflect the Company's more significant judgments and estimates used in the preparation of the consolidated financial statements. For a summary of all the Company's significant accounting policies see note 2 to the Company's consolidated financial statements included elsewhere in this report. We periodically evaluate our estimates and assumptions used in the preparation of our financial statements including our reported operating results. Because over 97% of our assets as of December 31, 2004 and 2003, respectively, consists of investments in real estate and amounts due from tenants, our primary evaluations consist of recoverability of amounts invested in real estate properties and collectability of amounts due from tenants.

Revenue Recognition

We recognize minimum rent, including rental abatements and contractual fixed increases attributable to operating leases, on a straight-line basis over the term of the related lease. The amount by which straight-line rental income differs from cash rents billed under the lease is included in deferred rents.

Allowance for Rents and Other Receivables

We periodically evaluate the collectability of amounts due from particular tenants based on a variety of factors including the tenant's payment history, our observation of space utilization, periodic discussions with the tenants regarding the tenant's short and long-term business plan for the space under contract, the overall financial health of the business and/or parent company, available financial and other information regarding the tenant or its parent company and the amount of lease security on hand. Based on these factors, unless collection is reasonably assured, we fully reserve amounts due that are in excess of the lease security we hold. All of our allowances are tenant specific.

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As of December 31, 2004 and 2003 we had a total of \$5.7 million and \$6.3 million in our allowance for doubtful accounts and other reserves, respectively, representing approximately 10% and 12% of the total rent and deferred rent balance outstanding at each respective balance sheet date. Including security deposits and existing letters of credit, as of December 31, 2004 and 2003, we had a total of \$39.3 million and \$33.5 million of total lease security available, respectively. For the years ended December 31, 2004, 2003 and 2002 our bad debt expense related to losses for uncollected rents, deferred rents, tenants reimbursements and other uncollectible charges were approximately 0.3%, 0.6% and 1.4% of total gross revenue, respectively, for each of those years. Our allowances have historically proved to be adequate; however, due to the uncertainty inherent in the tenant specific evaluation process, our allowance for doubtful accounts may not prove to be sufficient in all future periods.

Commercial Properties

Impairment of Assets

The recoverability of amounts invested in real estate properties is highly dependent on the assumptions we use. For properties we intend to hold and operate, we recognize a write-down to estimated fair value whenever a property's estimated undiscounted future cash flows are less than its depreciated cost. For properties we intend to sell, we recognize a write-down to estimated fair value whenever a property's estimated sales price less costs to sell are less than its depreciated costs.

We determine fair value of our properties using methods similar to those used by independent appraisers, including comparison of carrying costs on a per square foot basis to sales price on a per square foot basis on recently transacted properties that are similar in quality and location and also by comparing carrying costs to acquisition offers from prospective buyers. Based on our assessment, no write-downs to estimated fair value were necessary as of December 31, 2004 and 2003.

Due to the availability of comparable sales information in most of our sub-markets, historically our fair value estimates have proven to be accurate. However, our estimates may vary from actual values, especially for real estate assets located in sub-markets where quoted per square foot market prices for comparable properties may not be readily available or real estate assets that become impaired due to non-recurring circumstances such as previously unknown environmental issues or casualty losses that result in damages in excess of our insurance coverage amount.

Property Acquisitions

The amounts paid for properties acquired are allocated between the tangible and intangible assets. Tangible assets include land, building and tenant improvements. Intangible assets include the value of in place leases. To arrive at the value of in place leases, we compare estimates of current market rents to the in place rents. We also make assumptions regarding the amount of time that currently occupied space would remain vacant if we had to replace the existing tenants under current market conditions. We also reduce the value of each lease using a discount rate that we deem to be commensurate with each tenant's credit profile. The assumptions we use are based on available market information, from independent sources and our own market knowledge and experience.

The fair market value that we assign to acquired leases is amortized over the remaining lease terms. The tangible assets assigned to building improvements are depreciated over a much longer period of time, normally forty years. Consequently, the assumptions we use in this allocation have a significant impact on the operating results that we will report in future periods. We cannot guarantee that the initial assumptions that we use to any property's purchase price will prove to be accurate. We also would not revise these estimates in future periods if our initial amounts were proven to be inaccurate.

Qualification as a REIT

Since our taxable year ended December 31, 1996, we have been organized and operated, and intend to continue to operate, so as to qualify for taxation as a REIT under the Internal Revenue Code. Our qualification and taxation as a REIT depends on our ability to meet, through actual annual operating results,

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asset diversification, distribution levels and diversity of stock ownership, numerous requirements established under highly technical and complex Internal Revenue Code provisions subject to interpretation.

If we failed to qualify as a REIT in any taxable year, we would be subject to federal income tax, including any applicable alternative minimum tax, on our taxable income at regular corporate rates. Moreover, unless entitled to relief under specific statutory provisions, we also would be disqualified as a REIT for the four taxable years following the year during which qualification was lost. For additional information see Risk Factors We may suffer adverse tax consequences and be unable to attract capital if we fail to qualify as a REIT, and Our operating partnership intends to qualify as a partnership, but we cannot guarantee that it will qualify, elsewhere in this Form 10-K.

Off-Balance Sheet Arrangements

There are no off-balance sheet transactions, arrangements or obligations (including contingent obligations) that have, or are reasonably likely to have a current or future material effect on our financial condition, changes in the financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

Table of Contents*Results Of Operations*

Our financial position and operating results are primarily comprised of our portfolio of properties and income derived from those properties. Therefore, the comparability of financial data from period to period will be affected by the timing of significant property development, acquisitions and dispositions.

Comparison of the year ended December 31, 2004 to the year ended December 31, 2003

(in thousands, except number of properties and percentages)

| | Year Ended December 31, | | Change | Percent Change | |
|---|--|------------------|------------------|-------------------|--------------|
| | 2004 | 2003 | | | |
| Revenue from rental operations: | | | | | |
| Scheduled cash rents | \$ 351,465 | \$ 339,009 | \$ 12,456 | 4% | |
| Straight-line rents | 2,020 | 915 | 1,105 | 121 | |
| Tenant reimbursements | 20,129 | 23,355 | (3,226) | (14) | |
| Parking, net of expense | 23,816 | 21,635 | 2,181 | 10 | |
| Other rental operations | 11,763 | 8,851 | 2,912 | 33 | |
| | <u>409,193</u> | <u>393,765</u> | <u>15,428</u> | <u>4</u> | |
| Property expenses: | | | | | |
| Repairs and maintenance | 44,281 | 40,738 | 3,543 | 9 | |
| Utilities | 32,835 | 32,497 | 338 | 1 | |
| Real estate taxes | 30,569 | 28,156 | 2,413 | 9 | |
| Insurance | 7,506 | 7,909 | (403) | (5) | |
| Ground rent | 746 | 961 | (215) | (22) | |
| Administrative | 17,698 | 15,718 | 1,980 | 13 | |
| | <u>133,635</u> | <u>125,979</u> | <u>7,656</u> | <u>6</u> | |
| Property operating results(1) | 275,558 | 267,786 | 7,772 | 3 | |
| General and administrative | 19,503 | 16,931 | 2,572 | 15 | |
| Interest | 88,856 | 93,093 | (4,237) | (5) | |
| Depreciation and amortization | 121,687 | 111,952 | 9,735 | 9 | |
| Interest and other loss | 508 | 401 | 107 | 27 | |
| | <u>Income from continuing operations before gain on sale of properties and minority interest</u> | <u>\$ 45,004</u> | <u>\$ 45,409</u> | <u>\$ (405)</u> | <u>(1)%</u> |
| | <u>Discontinued operations, net of minority interest</u> | <u>\$ 6,253</u> | <u>\$ 12,538</u> | <u>\$ (6,285)</u> | <u>(50)%</u> |
| Number of properties: | | | | | |
| Acquired during period | 2 | 1 | | | |
| Completed and placed in service during period | 1 | | | | |
| Disposed of during period | (12) | (8) | | | |
| Owned at end of period | 120 | 129 | | | |
| Net rentable square feet: | | | | | |
| Acquired during period | 391 | 101 | | | |
| Completed and placed in service during period | 283 | | | | |
| Expansion space placed in service | 168 | | | | |
| Disposed of during period | (1,268) | (598) | | | |

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| | | | | |
|------------------------------------|-------------------|-------------------|-----------------|----------|
| Owned at end of period | 18,210 | 18,636 | | |
| Same Property Portfolio(2): | | | | |
| Revenue from rental operations | \$ 397,842 | \$ 394,449 | \$ 3,393 | 1% |
| Property expenses | 129,822 | 125,953 | 3,869 | 3 |
| | <u>\$ 268,020</u> | <u>\$ 268,496</u> | <u>\$ (476)</u> | <u>%</u> |
| Straight-line rents | \$ 315 | \$ 592 | | |
| Number of properties | 116 | | | |
| Number of buildings | 192 | | | |
| Average occupancy | 90.0% | 89.3% | | |
| Net rentable square feet | 17,334 | | | |

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(1) The components outlined above comprise our Property Operating Results. Property Operating Results is a non-GAAP measure of performance. Property Operating Results is used by investors and our management to evaluate and compare the performance of our office properties and to determine trends in earnings. Property Operating Results is also employed by investors as one of the components used to estimate the value of our properties. Property Operating Results is used for the purposes noted above because it is not affected by (1) the cost of funds of the property owner, (2) the impact of depreciation and amortization expense as well as gains or losses from the sale of operating real estate assets that are included in net income computed in accordance with Generally Accepted Accounting Principles, or GAAP or (3) general and administrative expenses and other specific costs such as permanent impairments to carrying costs. The cost of funds is eliminated from net income because it is specific to the particular financing capabilities and constraints of the owner. The cost of funds is also eliminated because it is dependent on historical interest rates and other costs of capital as well as past decisions made by us regarding the appropriate mix of capital, which may have changed or may change in the future. Depreciation and amortization expenses as well as gains or losses from the sale of operating real estate assets are eliminated because they may not accurately represent the actual change in value in our office properties that result from use of the properties or changes in market conditions. While certain aspects of real property do decline in value over time in a manner that is reasonably captured by depreciation and amortization, the value of the properties as a whole have historically increased or decreased in value as a result of changes in overall economic conditions as well as the actual use of the property or the passage of time. Gains and losses from the sale of real property vary from property to property and are affected by market conditions at the time of sale which will usually change from period to period. These gains and losses can create distortions when comparing one period to another or when comparing our operating results to the operating results of other real estate companies that have not made similarly timed purchases and subsequent sales. General and administrative expenses and other owner specific costs such as impairment losses are eliminated because these costs are also in large part specific to the ownership structure and timing of purchases of the owner. We believe that eliminating these costs from net income is useful because the resulting measure captures the actual revenue generated and actual expenses incurred in operating our office properties as well as trends in occupancy rates, rental rates and operating costs.

However, the usefulness of Property Operating Results is limited because it excludes general and administrative costs, interest expense, interest income, depreciation and amortization expense and gains or losses from the sale of properties, changes in value in our real estate properties that result from use or permanent impairment to carrying costs as stipulated by GAAP, the level of capital expenditures and leasing costs necessary to maintain the operating performance of our properties, all of which are significant economic costs. Property Operating Results may fail to capture significant trends in these components of net income which further limits its usefulness.

Property Operating Results is a measure of the operating performance of our office properties but does not measure our performance as a whole. Property Operating Results is therefore not a substitute for net income as computed in accordance with GAAP. This measure should be analyzed in conjunction with net income computed in accordance with GAAP and discussions elsewhere in Management's Discussion and Analysis of Financial Condition and Results of Operations regarding the components of net income that are eliminated in the calculation of Property Operating Results. Other companies may use different methods for calculating Property Operating Results or similarly entitled measures and, accordingly, our Property Operating Results may not be comparable to similarly entitled measures reported by other companies that do not define the measure exactly as we do.

The following is a reconciliation of Property Operating Results to net income computed in accordance with GAAP (in thousands):

| | Year Ended December 31, | | |
|---|--------------------------------|------------------|------------------|
| | 2004 | 2003 | 2002 |
| Net Income | \$ 73,775 | \$ 58,509 | \$ 70,175 |
| Add: | | | |
| General and administrative expense | 19,503 | 16,931 | 12,581 |
| Interest expense | 88,856 | 93,093 | 87,827 |
| Depreciation and amortization | 121,687 | 111,952 | 100,317 |
| Minority interest | 5,255 | 5,375 | 5,816 |
| Interest and other loss | 508 | 401 | |
| Impairment on investment in securities | 2,700 | | |
| Less: | | | |
| Interest and other income | | | (2,063) |
| Gain on sale of discontinued properties | (30,473) | (5,937) | |
| Discontinued operations, net of minority interest | (6,253) | (12,538) | (15,570) |
| Gain on sale of operating properties | | | (1,967) |
| Property Operating Results | <u>\$275,558</u> | <u>\$267,786</u> | <u>\$257,116</u> |



- (2) Consists of non-development/renovation properties classified as part of continuing and discontinued operations that were owned for the entirety of the periods presented.

Variances for Results of Operations

Our Property Operating Results for the year ended December 31, 2004 compared to 2003 were primarily affected by our acquisitions and development activities since January 1, 2003.

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As a result of these changes within our portfolio of properties since January 1, 2003, we do not believe the Property Operating Results presented above are comparable from period to period. Therefore, in the table above, we have also presented the Property Operating Results for our same property portfolio.

Revenue from Rental Operations

Revenue from rental operations increased approximately \$15.4 million, or 4%, for the year ended December 31, 2004 compared to 2003. This increase was primarily due to our December 2003 acquisition of a 101,000 square foot office property in San Diego County in December of 2003, revenues from our 6100 Center Drive development property which was placed in service during the second quarter of 2004, two office properties acquired in Los Angeles County in October of 2004 totaling approximately 391,000 square feet, an 0.8% point overall occupancy gain in 2004.

Revenue from rental operations for the same store portfolio increased by approximately \$3.4 million, or 1%, in 2004 as compared to 2003. The increase was due to an approximate \$2.9 million increase in scheduled cash rents, a \$2.9 million increase in other rental operations and a \$1.6 million increase in parking income, all of which were partially offset by an approximate \$3.7 million decrease in tenant reimbursements. The increase in scheduled cash rents was primarily attributable to scheduled rent increases in existing leases and by the 0.7% increase in average occupancy for these properties. Other rental operations increased primarily due to higher lease termination fees in 2004 and lower bad debt expense as a result of a reduced level of defaults in 2004. Parking income increased in 2004 primarily due to an increase in occupancy in 2004 and higher special event parking. Tenant reimbursements decreased primarily due to the resetting of base years for new leases in 2004.

Property Expenses

Property expenses increased approximately \$7.7 million, or 6%, for the year ended December 31, 2004 compared to 2003. This increase was partially due to our acquisition and development activities, gains in occupancy and increases in operating expenses for the same property portfolio described below.

Property expenses for the same store portfolio increased by approximately \$3.9 million, or 3%, in 2004 as compared to 2003. The increase was primarily due to an approximate \$2.9 million increase in repairs and maintenance, a \$1.6 million increase in real estate taxes and a \$1.3 million increase in property administrative expenses, all of which were partially offset by a \$1.2 million decrease in utilities expense and a \$0.5 million decrease in insurance expense. The increase in repairs and maintenance expense was primarily due to higher costs for contracted services and the timing of certain projects. The increase in real estate taxes was primarily due to the timing of reassessments and property tax refunds received in 2003 as well as new property tax measures implemented in Los Angeles County. The increase in property administrative expense was primarily due to higher employee compensation costs and higher property legal expenses. The decrease in utilities expense was primarily due to lower than anticipated usage in 2004 as a result of a mild summer, partially offset by an increase in occupancy. The decrease in insurance expense was primarily due to lower premiums on a new insurance policy which began in March 2004.

General and Administrative

General and administrative expenses increased approximately \$2.6 million in 2004 as compared to 2003. This increase was primarily related to higher personnel costs associated with annual merit increases, non-cash compensation expense associated with restricted stock grants issued in 2004 and 2003 and Section 404 implementation costs in 2004.

Interest Expense

Interest expense decreased approximately \$4.2 million, or 5%, in 2004 as compared to 2003. This decrease was primarily due to a lower cost of debt in 2004 due to the refinancing of a \$175 million, 7.52% secured loan with proceeds from property dispositions and from the issuance of \$200 million, 5.20% (5.45% effective rate) unsecured senior notes in August 2004, partially offset by lower capitalized interest in 2004. Capitalized interest was lower in 2004 as we stopped capitalizing interest on our 6100 Center Drive development property in May 2003.

Table of Contents**Depreciation and Amortization**

Depreciation and amortization expense increased by approximately \$9.7 million, or 9%, in 2004 as compared to 2003. The increase was primarily due to depreciation related to a property acquired in December 2003, two properties acquired in October 2004, a development property placed in service in the second quarter of 2004 and depreciation related to capital expenditures, tenant improvements and leasing commissions placed in service in 2003 and 2004.

Discontinued Operations

Financial Accounting Standards No. 144, (SFAS 144), requires, among other things, that the operating results of real estate properties classified as held for disposition subsequent to January 1, 2002 be included in discontinued operations in the statements of income for all periods presented.

The results of operations for the properties disposed of or held for disposition during the years ended December 31, 2004 and 2003 are as follows (in thousands, except number of properties):

| | Year Ended December 31, | | Change | Percent Change |
|---|----------------------------|-----------|------------|-------------------|
| | 2004 | 2003 | | |
| Discontinued Operations: | | | | |
| Revenues | \$20,533 | \$33,794 | \$(13,261) | (39)% |
| Property operating expenses | 7,781 | 11,711 | (3,930) | (34) |
| | 12,752 | 22,083 | (9,331) | (42) |
| Depreciation and amortization | 4,895 | 8,372 | (3,477) | (42) |
| Interest expense | 659 | 674 | (15) | (2) |
| Interest and other income | (2) | (2) | (2) | 100 |
| Minority interest | 947 | 499 | 448 | 90 |
| Discontinued operations, net of minority interest | \$ 6,253 | \$ 12,538 | \$ (6,285) | (50)% |
| Gain on sale of discontinued properties | \$30,473 | \$ 5,937 | \$ 24,536 | 413% |
| Properties sold | 12 | 8 | | |
| Properties held for disposition at end of period | 1 | 2 | | |

Table of Contents**Comparison of the year ended December 31, 2003 to the year ended December 31, 2002**

(in thousands, except number of properties and percentages)

| | Year Ended December 31, | | Change | Percent Change |
|---|-------------------------|-------------------|-------------------|-------------------|
| | 2003 | 2002 | | |
| Revenue from rental operations: | | | | |
| Scheduled cash rents | \$ 339,009 | \$ 320,505 | \$ 18,504 | 6% |
| Straight-line rents | 915 | 4,629 | (3,714) | (80) |
| Tenant reimbursements | 23,355 | 21,161 | 2,194 | 10 |
| Parking, net of expense | 21,635 | 20,350 | 1,285 | 6 |
| Other rental operations | 8,851 | 7,490 | 1,361 | 18 |
| | <u> </u> | <u> </u> | <u> </u> | <u> </u> |
| Total revenue from rental operations | 393,765 | 374,135 | 19,630 | 5 |
| | <u> </u> | <u> </u> | <u> </u> | <u> </u> |
| Property expenses: | | | | |
| Repairs and maintenance | 40,738 | 35,294 | 5,444 | 15 |
| Utilities | 32,497 | 32,338 | 159 | 0 |
| Real estate taxes | 28,156 | 27,290 | 866 | 3 |
| Insurance | 7,909 | 7,291 | 618 | 8 |
| Ground rent | 961 | 895 | 66 | 7 |
| Administrative | 15,718 | 13,911 | 1,807 | 13 |
| | <u> </u> | <u> </u> | <u> </u> | <u> </u> |
| Total property expenses | 125,979 | 117,019 | 8,960 | 8 |
| | <u> </u> | <u> </u> | <u> </u> | <u> </u> |
| Property operating results(1) | 267,786 | 257,116 | 10,670 | 4 |
| General and administrative | 16,931 | 12,581 | 4,350 | 35 |
| Interest | 93,093 | 87,827 | 5,266 | 6 |
| Depreciation and amortization | 111,952 | 100,317 | 11,635 | 12 |
| Interest and other loss (income) | 401 | (2,063) | (2,464) | (119) |
| | <u> </u> | <u> </u> | <u> </u> | <u> </u> |
| Income from continuing operations before gain on sale of properties and minority interest | \$ 45,409 | \$ 58,454 | \$ (13,045) | (22)% |
| | <u> </u> | <u> </u> | <u> </u> | <u> </u> |
| Discontinued operations, net of minority interest | \$ 12,538 | \$ 15,570 | \$ (3,032) | (19)% |
| | <u> </u> | <u> </u> | <u> </u> | <u> </u> |
| Number of properties: | | | | |
| Acquired during period | 1 | 5 | | |
| Completed and placed in service during period | | 1 | | |
| Disposed of during period | (8) | (3) | | |
| Owned at end of period | 129(2) | 136 | | |
| Net rentable square feet: | | | | |
| Acquired during period | 101 | 803 | | |
| Completed and placed in service during period | | 287 | | |
| Disposed of during period | (597) | (205) | | |
| Owned at end of period | 18,636(2) | 19,132 | | |
| Same Store Portfolio(3): | | | | |
| Revenue from rental operations | \$ 391,960 | \$ 386,826 | \$ 5,134 | 1% |
| Property expenses | 126,041 | 121,112 | 4,929 | 4 |
| | <u> </u> | <u> </u> | <u> </u> | <u> </u> |
| | \$ 265,919 | \$ 265,714 | \$ 205 | % |
| | <u> </u> | <u> </u> | <u> </u> | <u> </u> |
| Straight-line rents | \$ 721 | \$ 4,312 | | |

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| | | |
|--------------------------|--------|--------|
| Number of properties | 122 | 122 |
| Average occupancy | 90.2% | 91.3% |
| Net rentable square feet | 17,444 | 17,444 |

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- (1) The components outlined above comprise our Property Operating Results. Property Operating Results is a non-GAAP measure of performance. Property Operating Results is used by investors and our management to evaluate and compare the performance of our office properties and to determine trends in earnings. Property Operating Results is also employed by investors as one of the components used to estimate the value of our properties. Property Operating Results is used for the purposes noted above because it is not affected by (1) the cost of funds of the property owner, (2) the impact of depreciation and amortization expense as well as gains or losses from the sale of operating real estate assets that are included in net income computed in accordance with Generally Accepted Accounting Principles, or GAAP or (3) general and administrative expenses and other specific costs such as permanent impairments to carrying costs. The cost of funds is eliminated from net income because it is specific to the particular financing capabilities and constraints of the owner. The cost of funds is also eliminated because it is dependent on historical interest rates and other costs of capital as well as past decisions made by us regarding the appropriate mix of capital, which may have changed or may change in the future. Depreciation and amortization expenses as well as gains or losses from the sale of operating real estate assets are eliminated because they may not accurately represent the actual change in value in our office properties that result from use of the properties or changes in market conditions. While certain aspects of real property do decline in value over time in a manner that is reasonably captured by depreciation and amortization, the value of the properties as a whole have historically increased or decreased in value as a result of changes in overall economic conditions as well as the actual use of the property or the passage of time. Gains and losses from the sale of real property vary from property to property and are affected by market conditions at the time of sale which will usually change from period to period. These gains and losses can create distortions when comparing one period to another or when comparing our operating results to the operating results of other real estate companies that have not made similarly timed purchases and subsequent sales. General and administrative expenses and other owner specific costs such as impairment losses are eliminated because these costs are also in large part specific to the ownership structure and timing of purchases of the owner. We believe that eliminating these costs from net income is useful because the resulting measure captures the actual revenue generated and actual expenses incurred in operating our office properties as well as trends in occupancy rates, rental rates and operating costs.

However, the usefulness of Property Operating Results is limited because it excludes general and administrative costs, interest expense, interest income, depreciation and amortization expense and gains or losses from the sale of properties, changes in value in our real estate properties that result from use or permanent impairment to carrying costs as stipulated by GAAP, the level of capital expenditures and leasing costs necessary to maintain the operating performance of our properties, all of which are significant economic costs. Property Operating Results may fail to capture significant trends in these components of net income which further limits its usefulness.

Property Operating Results is a measure of the operating performance of our office properties but does not measure our performance as a whole. Property Operating Results is therefore not a substitute for net income as computed in accordance with GAAP. This measure should be analyzed in conjunction with net income computed in accordance with GAAP and discussions elsewhere in Management's Discussion and Analysis of Financial Condition and Results of Operations regarding the components of net income that are eliminated in the calculation of Property Operating Results. Other companies may use different methods for calculating Property Operating Results or similarly entitled measures and, accordingly, our Property Operating Results may not be comparable to similarly entitled measures reported by other companies that do not define the measure exactly as we do.

The following is a reconciliation of Property Operating Results to net income computed in accordance with GAAP (in thousands):

| | 2003 | 2002 | 2001 |
|---|------------------|------------------|------------------|
| Net Income | \$ 58,509 | \$ 70,175 | \$ 97,759 |
| Add: | | | |
| General and administrative expense | 16,931 | 12,581 | 11,496 |
| Interest expense | 93,093 | 87,827 | 85,949 |
| Depreciation and amortization | 111,952 | 100,317 | 92,613 |
| Interest and other loss | 401 | | |
| Minority interest | 5,375 | 5,816 | 7,046 |
| Less: | | | |
| Interest and other income | | (2,063) | (2,135) |
| Discontinued operations, net of minority interest | (12,538) | (15,570) | (15,719) |
| Gain on sale of discontinued properties | (5,937) | | |
| Gain on sale of operating properties | | (1,967) | (4,591) |
| Property Operating Results | <u>\$267,786</u> | <u>\$257,116</u> | <u>\$272,418</u> |

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- (2) Excludes one development property containing approximately 283,000 net rentable square feet under lease-up.
- (3) Consists of non-development/renovation properties classified as part of continuing and discontinued operations that were owned for the entirety of the periods presented.

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Variations for Results of Operations

Our Property Operating Results for the year ended December 31, 2003 compared to 2002 were primarily affected by our acquisitions and development activities since January 1, 2002.

As a result of these changes within our portfolio of properties since January 1, 2002, we do not believe the Property Operating Results presented above are comparable from period to period. Therefore, in the table above, we have also presented the Property Operating Results for our same property portfolio.

Revenue from Rental Operations

Revenue from rental operations increased approximately \$19.6 million, or 5%, for the year ended December 31, 2003 compared to 2002. This increase was primarily due to our August 2002 acquisitions of a 430,00 square foot office property in Los Angeles County and four office properties in San Diego County totaling approximately 370,000 square feet and a December 2003 acquisition of a 101,000 square foot office property in San Diego County and the placement in service of our 6080 Center Drive development property in December of 2002.

Revenue from rental operations for the same store portfolio increased by approximately \$5.1 million, or 1%, in 2003 as compared to 2002. The increase was due to an approximate \$6.0 million increase in scheduled cash rents, a \$2.3 million increase in tenant reimbursements and a \$0.9 million increase in parking income, all of which were partially offset by an approximate \$3.6 million decrease in straight-line rents and a \$0.5 million decrease in other rental operations. The increase in scheduled cash rents was primarily attributable to scheduled rent increases in existing leases that were partially offset by the 1.1% decrease in average occupancy for these properties. Tenant reimbursement increased primarily due to recovery billings for higher operating expenses in 2003 as discussed below. Parking income increased primarily due to an increase in demand for monthly parking in 2003 in some of our buildings. Straight-line rents decreased primarily due to the decline in occupancy and the scheduled reversal of straight-line rents for certain older leases. Other rental operations decreased primarily due to decreases in lease termination settlements in 2003.

Property Expenses

Property expenses increased approximately \$9.0 million, or 8%, for the year ended December 31, 2003 compared to 2002. This increase was partially due our acquisition and development activities described above.

Property expenses for the same store portfolio increased by approximately \$4.9 million, or 4%, in 2003 as compared to 2002. The increase was primarily due to an approximate \$3.6 million increase in repairs and maintenance, a \$1.6 million increase in property administrative expenses and a \$0.4 million increase in insurance expense, partially offset by a \$0.8 million decrease in real estate taxes. The increase in repairs and maintenance expense was primarily due to higher contractual costs for janitorial and other contract services as well as the timing of certain projects. The increase in property administrative expense was primarily due to higher employee compensation costs, higher property legal expenses and costs associated with training programs implemented in 2003. The increase in insurance expense was due to increases in industry-wide rates and premiums related to a \$100 million terrorism insurance policy entered into in the second quarter of 2002. Real estate taxes decreased due to the timing of final reassessments of some properties in 2002.

General and Administrative

General and administrative expenses increased approximately \$4.4 million or, 35% in 2003 as compared to 2002. This increase was primarily due to employee compensation costs, including employee separation costs in the current year and non-cash compensation costs associated with annual restricted stock grants issued in 2003 as well as higher corporate governance costs in 2003.

Interest Expense

Interest expense increased approximately \$5.3 million, or 6%, in 2003 as compared to 2002. This increase was primarily due to an increase in borrowings in the last half of 2002 for property acquisitions, lower interest capitalized in 2003 and costs associated with interest rate swaps entered into at the end of 2002 to fix

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approximately \$175 million of floating rate debt. Capitalized interest in 2003 was lower as we ceased capitalizing interest on our 6100 Center Drive property in May 2003.

Depreciation and Amortization

Depreciation and amortization expense increased by approximately \$11.6 million, or 12%, in 2003 as compared to 2002. The increase was primarily due to depreciation related to five properties acquired in August 2002, the placement in service of our 6080 Center Drive development property in the fourth quarter of 2002 and depreciation related to capital expenditures, tenant improvements and leasing commissions placed in service in 2002 and 2003.

Interest and Other Loss (Income)

Interest and other loss (income) decreased by approximately \$2.5 million, or 119%, in 2003 as compared to 2002, primarily due to the repayment by the borrower of a \$13.7 million mortgage note receivable in the fourth quarter of 2002 and the reclassification of the operating results for Next>edge, our taxable REIT subsidiary that provides energy consulting services, into interest and other income for the years ended December 31, 2003 and 2002.

Discontinued Operations

SFAS 144, effective January 1, 2002, requires, among other things, that the operating results of real estate properties classified as held for disposition subsequent to January 1, 2002 be included in discontinued operations in the statements of income for all periods presented.

The results of operations for the properties disposed of or held for disposition during the years ended December 31, 2003 and 2002 are as follows (in thousands, except number of properties):

| | Year Ended December 31, | | Change | Percent Change |
|---|----------------------------|-----------|-----------|-------------------|
| | 2003 | 2002 | | |
| Discontinued Operations: | | | | |
| Revenues | \$ 33,794 | \$ 41,978 | \$(8,184) | (19)% |
| Property operating expenses | 11,711 | 14,199 | (2,488) | (18) |
| | 22,083 | 27,779 | (5,696) | (21) |
| Depreciation and amortization | 8,372 | 11,100 | (2,728) | (25) |
| Interest expense | 674 | 689 | (15) | (2) |
| Minority interest | 499 | 420 | 79 | 19 |
| Discontinued operations, net of minority interest | \$ 12,538 | \$ 15,570 | \$(3,032) | (19)% |
| Gain on sale of discontinued properties | \$ 5,937 | \$ | \$ 5,937 | 100% |
| Properties sold | 8 | 3 | | |
| Properties held for disposition at end of period | 2 | 1 | | |

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Liquidity and Capital Resources

Cash Flows

Cash provided by operating activities increased by approximately \$3.4 million to \$184.9 million in 2004 as compared to \$181.5 million in 2003. This increase was primarily due to lower financing costs in 2004 as a result of a \$175 million 7.52% loan and a \$50 million, 8.675% preferred equity issuance that were refinanced at lower carrying costs. In addition, our cash flow from operations was affected by the timing of our acquisitions and dispositions in 2004. Although during 2004 we had net property sales, \$126 million of our \$204.8 million in dispositions occurred in December of 2004.

Cash used in investing activities decreased by approximately \$9.2 million to \$11.2 million in 2004 as compared to \$20.4 million in 2003. The decrease was primarily due to higher net selling activities in 2004. In 2004, our cash flow used in investing activities was also affected by a higher level of tenant improvement and leasing commission expenditures as a result of approximately 485,000 square feet of additional leasing completed in 2004 over 2003.

Cash used in financing activities increased by approximately \$4.8 million to \$165.3 million in 2004 as compared to \$160.5 million in 2003. This increase was primarily due to higher net debt repayments in 2004 with proceeds generated from our capital recycling program.

Cash Balances and Available Borrowings

As of December 31, 2004, we had approximately \$27.8 million in cash and cash equivalents, including \$14.8 million in restricted cash. Restricted cash consisted of \$9.7 million in interest bearing cash deposits required by four of our mortgage loans and \$5.1 million in cash impound accounts for real estate taxes and insurance as required by several of our mortgage loans.

Through our Operating Partnership, we have access to a total of \$330 million under two unsecured lines of credit. As of December 31, 2004, \$121.5 million was outstanding and \$208.5 million was available under these unsecured lines of credit.

Capital Recycling Program

Under our capital recycling program, we evaluate our existing portfolio of properties and current market opportunities to determine if the sale or purchase of properties would improve the overall quality or return on invested capital of our existing portfolio. Proceeds from sales of properties may be used to pay down our borrowings until we identify attractive properties to purchase, renovate or develop. During 2004, we sold twelve properties totaling approximately 1.3 million square feet for approximately \$204.8 million in gross sales proceeds. In October 2004, we acquired two office properties consisting of approximately 391,000 square feet for approximately \$96.8 million. For additional information regarding the properties acquired and sold, see the accompanying notes to our financial statements elsewhere in this report.

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Following is a summary of scheduled principal payments for our total outstanding indebtedness as of December 31, 2004 (in thousands):

| Year | Amount |
|------------|---------------------|
| 2005 | \$ 216,871 |
| 2006 | 251,101 |
| 2007 | 158,035 |
| 2008 | 230,726 |
| 2009 | 112,291 |
| 2010 | 150,307 |
| 2011 | 200,538 |
| 2012 | 768 |
| 2013 | 845 |
| 2014 | 914 |
| Thereafter | 3,688 |
| Total | <u>\$ 1,326,084</u> |

Following is other information related to our indebtedness as of December 31, 2004 (in thousands, except percentage and interest rate data):

Unsecured and Secured Debt:

| | Balance | Percent | Weighted Average Interest Rate(1) | Weighted Average Maturity (in years) |
|----------------|---------------------|-------------|--------------------------------------|---|
| | (000 s) | | | |
| Unsecured Debt | \$ 943,445 | 71% | 6.79% | 3.2 |
| Secured Debt | 382,639 | 29 | 7.16 | 3.8 |
| Total Debt | <u>\$ 1,326,084</u> | <u>100%</u> | <u>6.90</u> | <u>3.4</u> |

Floating and Fixed Rate Debt:

| | Balance | Percent | Weighted Average Interest Rate(1) | Weighted Average Maturity (in years) |
|-----------------------|---------------------|-------------|--------------------------------------|---|
| | (000 s) | | | |
| Floating Rate Debt(2) | \$ 171,500 | 13% | 5.88% | 2.1 |
| Fixed Debt(3) | 1,154,584 | 87 | 7.05 | 3.5 |
| Total Debt | <u>\$ 1,326,084</u> | <u>100%</u> | <u>6.90%</u> | <u>3.4</u> |

(1) Includes amortization of prepaid financing costs.

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(2) Includes \$100 million of fixed rate debt that has been converted to floating rate through interest rate hedge agreements.

(3) Includes \$175 million of floating rate debt that has been fixed through interest rate hedge agreements.

Interest Incurred:

| | Year Ended December 31, | | |
|----------------------------|-------------------------|----------|----------|
| | 2004 | 2003 | 2002 |
| Total interest incurred(1) | \$90,451 | \$96,263 | \$94,162 |
| Amount capitalized | (936) | (2,496) | (5,646) |
| | \$89,515 | \$93,767 | \$88,516 |
| | \$89,515 | \$93,767 | \$88,516 |

(1) Includes interest expense for a property currently classified as held for disposition .

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Consolidated Income Available for Debt Service and Compliance with Principal Financial Covenants

Consolidated Income Available for Debt Service is a non-GAAP measurement of our performance and liquidity. Consolidated Income Available for Debt Service is presented below because this data is used by investors and our management as a supplemental measure to (a) evaluate our operating performance and compare it to other real estate companies, (b) determine trends in earnings, (c) determine our ability to service debt and (d) determine our ability to fund future capital expenditure requirements. As discussed more fully below, Consolidated Income Available for Debt Service is also used in several financial covenants we are required to satisfy each quarter under the terms of our principal debt agreements.

Consolidated Income Available for Debt Service permits investors and management to view income from our operations on an unleveraged basis before the effects of non-cash depreciation and amortization expense. By excluding interest expense, Consolidated Income Available for Debt Service measures our operating performance independent of our capital structure and indebtedness and, therefore, allows for a more meaningful comparison of our operating performance between quarters as well as annual periods and to compare our operating performance to that of other companies, and to more readily identify and evaluate trends in earnings.

The usefulness of Consolidated Income Available for Debt Service is limited because it does not reflect interest expense, taxes, gains or losses on sales of property, losses on valuations of derivatives, asset impairment losses, cumulative effect of a change in accounting principle, extraordinary items as defined by GAAP and depreciation and amortization costs. These costs have been or may in the future be incurred by us, each of which affects or could effect our operating performance and ability to finance our investments at competitive borrowing costs, successfully maintain our REIT status, and acquire and dispose of real estate properties at favorable prices to us. Some of these costs also reflect changes in value in our properties that result from use or changes in market conditions and the level of capital expenditures and leasing costs necessary to maintain the operating performance of our properties. Due to the significance of the net income components excluded from Consolidated Income Available for Debt Service, this measure should not be considered an alternative to (and should be considered in conjunction with) net income, cash flow from operations, and other performance or liquidity measures prescribed by GAAP. This measure should also be analyzed in conjunction with discussions elsewhere in Management's Discussion and Analysis of Financial Condition and Results of Operations regarding the items eliminated in the calculation of Consolidated Income Available for Debt Service.

The reader is cautioned that Consolidated Income Available for Debt Service, as calculated by us, may not be comparable to similar measures reported by other companies (under names such as or similar to Consolidated Income Available for Debt Service, EBITDA or adjusted EBITDA) that do not define this measure exactly the same as we do.

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We calculate Consolidated Income Available for Debt Service as follows:

| | Year Ended December 31, | | | | |
|--|-------------------------|-------------------|-------------------|-------------------|-------------------|
| | 2004 | 2003 | 2002 | 2001 | 2000 |
| Net cash provided by operating activities | \$ 184,907 | \$ 181,482 | \$ 199,922 | \$ 204,667 | \$ 192,152 |
| Add: | | | | | |
| Interest expense | 88,856 | 93,093 | 87,827 | 85,949 | 78,495 |
| Interest expense from discontinued operations | 659 | 674 | 689 | (1,754) | (89) |
| Gain on repayment on mortgage note receivable | | | 750 | | |
| Less: | | | | | |
| Amortization of loan costs and fees | (3,801) | (3,972) | (3,807) | (3,568) | (3,568) |
| Straight-line rent | (1,841) | (1,732) | (5,465) | (9,208) | (8,077) |
| Changes in operating assets and liabilities: | | | | | |
| Rent and other receivables | 2,265 | 771 | (6,768) | (3,775) | 1,080 |
| Deferred rent | 1,015 | 557 | 4,657 | 7,401 | 7,656 |
| Prepaid financing costs, expenses and other assets | 4,783 | 1,494 | 2,997 | 4,366 | 7,480 |
| Accounts payable and accrued expenses | (3,338) | 2,365 | (9,729) | (4,388) | (11,359) |
| Security deposits | (3,285) | (1,676) | (962) | (213) | (3,397) |
| Consolidated Income Available for Debt Service | <u>\$ 270,220</u> | <u>\$ 273,056</u> | <u>\$ 270,111</u> | <u>\$ 279,477</u> | <u>\$ 260,373</u> |

| | Year Ended December 31, | | | | |
|--|-------------------------|-------------------|-------------------|-------------------|-------------------|
| | 2004 | 2003 | 2002 | 2001 | 2000 |
| Net Income | \$ 73,775 | \$ 58,509 | \$ 70,175 | \$ 97,759 | \$ 96,710 |
| Add: | | | | | |
| Interest expense | 88,856 | 93,093 | 87,827 | 85,949 | 78,495 |
| Interest expense from discontinued operations | 659 | 674 | 689 | (1,754) | (89) |
| Depreciation and amortization | 121,687 | 111,952 | 100,317 | 92,613 | 78,672 |
| Minority interest | 5,255 | 5,375 | 5,816 | 7,046 | 7,158 |
| Minority interest from discontinued operations | 947 | 499 | 420 | 519 | 455 |
| Amortization of deferred compensation | 3,760 | 2,251 | 1,199 | 1,938 | 586 |
| Depreciation from discontinued operations | 4,895 | 8,372 | 11,100 | 9,206 | 8,595 |
| Impairment on investment in securities | 2,700 | | | | |
| Less: | | | | | |
| Gain on sale of discontinued properties | (30,473) | (5,937) | | | |
| Gain on sale of operating properties | | | (1,967) | (4,591) | (2,132) |
| Straight-line rent | (1,841) | (1,732) | (5,465) | (9,208) | (8,077) |
| Consolidated Income Available for Debt Service | <u>\$ 270,220</u> | <u>\$ 273,056</u> | <u>\$ 270,111</u> | <u>\$ 279,477</u> | <u>\$ 260,373</u> |



Consolidated Income Available for Debt Service is also presented because it is used in ratios contained in the principal financial covenants of the Indenture governing our publicly traded senior unsecured notes and our Credit Agreement with a syndicate of banks led by Wells Fargo. As of December 31, 2004, our senior unsecured notes represented approximately 53% of our total outstanding debt and amounts outstanding under our Wells Fargo unsecured line of credit represented approximately 9% of our total outstanding debt. The Consolidated Income Available for Debt Service ratios and the other ratios reported below are part of financial covenants we are required to satisfy each fiscal quarter. We believe information about these ratios is useful to

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(1) confirm that we are in compliance with the financial covenants of our principal loan agreements, (2) evaluate our ability to service our debt, (3) evaluate our ability to fund future capital expenditures, and (4) compare our ratios to other real estate companies, including other REITs, that present the same ratios.

If we were to fail to satisfy these financial covenants, we would be in default under the terms of the Indenture for the senior unsecured notes and/or the Wells Fargo Credit Agreement. A default under those agreements could accelerate the obligation to repay such debt and could cause us to be in default under our other debt agreements. Depending on the circumstances surrounding such acceleration, we might not be able to repay the debt on terms that are favorable to us, or at all, which could have a material adverse affect on our financial condition and our ability to raise capital in the future.

The reader is cautioned that these ratios, as calculated by us, may not be comparable to similarly entitled ratios reported by other companies that do not calculate these ratios exactly the same as we do. These ratios should not be considered as alternatives to the ratio of earnings to fixed charges.

The following table summarizes the principal ratios contained in the financial covenants of our senior unsecured notes and Wells Fargo unsecured line of credit as of December 31, 2004 (in thousands, except percentage and covenant ratio data):

| | |
|---|--------------------|
| Net investment in real estate | \$2,551,981 |
| Cash and cash equivalents | 13,040 |
| Restricted cash | 14,788 |
| Accumulated depreciation and amortization | 488,808 |
| Total Assets | \$3,068,617 |
| | |
| Total unencumbered assets | \$2,097,592 |
| | |
| Mortgage loans payable(1) | \$ 382,639 |
| Unsecured lines of credit | 121,500 |
| Unsecured term loan | 125,000 |
| Unsecured senior notes, net of discount | 696,945 |
| Total Outstanding Debt | \$1,326,084 |
| | |
| Consolidated Income Available for Debt Service(2) | \$ 270,220 |
| | |
| Interest incurred(2) | \$ 90,451 |
| Loan fee amortization(2) | (3,332) |
| Debt Service(2) | \$ 87,119 |

| Senior Unsecured Notes Covenant Ratios | Test | Actual |
|---|-------------------|---------------|
| Ratio of Consolidated Income Available for Debt Service to Debt Service | Greater than 1.5 | 3.1 |
| Total Outstanding Debt/ Total Assets | Less than 60% | 43% |
| Secured Debt/ Total Assets | Less than 40% | 12% |
| Unencumbered Assets/ Unsecured Debt | Greater than 150% | 222% |
| | | |
| Wells Fargo Unsecured Line of Credit Covenant Ratios | Test | Actual |

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| | | |
|--|-------------------|-----|
| Ratio of Consolidated Income Available for Debt Service to interest expense(3) | Greater than 2.0 | 3.0 |
| Ratio of Consolidated Income Available for Debt Service to fixed charges(4) | Greater than 1.75 | 2.2 |

- (1) Represents 9 secured loans that are secured by 53 properties in our portfolio.
- (2) Represents amounts for the most recent four consecutive quarters. Loan fee amortization excludes discount amortization on senior unsecured notes.
- (3) Interest expense consists of interest expense plus capitalized interest and less amortization of loan fees and discounts.
- (4) Fixed charges consist of interest costs, whether expensed or capitalized, principal payments on all debt, an amount equal to \$0.3125 per quarter multiplied by the weighted average gross leasable square feet of the portfolio at the end of the period and preferred unit distributions.

Table of Contents*Future Capital Resources*

Depending on market conditions, we may sell assets over the next twelve to twenty-four months and it is difficult to predict the actual period and amount of these potential asset sales. At the time of any such sales, depending on market conditions, sales proceeds may be placed into investments that we believe will generate higher long-term value, which may include development or redevelopment of office buildings, acquisitions of existing buildings or repurchases of our common stock. In addition, we expect to use a portion of any proceeds to pay down portions of our debt in order to maintain our conservative leverage and coverage ratios.

We expect to continue meeting our short-term liquidity and capital requirements generally through net cash provided by operating activities, proceeds from our lines of credit or from asset sales. We believe that the net cash provided by operating activities, sales proceeds and short-term borrowings, if necessary, will continue to be sufficient to pay any distributions necessary to enable us to continue qualifying as a REIT. We also believe the foregoing sources of liquidity will be sufficient to fund our short-term liquidity needs over the next twelve months, including recurring non-revenue enhancing capital expenditures, tenant improvements and leasing commissions.

We expect to meet our long-term liquidity and capital requirements such as scheduled principal repayments, development costs, property acquisitions, if any, and other non-recurring capital expenditures through net cash provided by operations, refinancing of existing indebtedness, proceeds from asset sales and/or the issuance of long-term debt and equity securities.

Recurring non-revenue enhancing capital expenditures represent building improvements and leasing costs required to maintain current revenue. Recurring capital expenditures do not include immediate building improvements that were taken into consideration when underwriting the purchase of a building or which are being incurred to bring a building up to our operating standards or to reach stabilization. We consider a property to be stabilized when the property is at least 95% leased. Recurring capital expenditures consist primarily of replacement components such as new elevators, roof replacements and upgrade requirements required by new safety codes such as new fire-life-emergency systems.

Non-recurring capital expenditures represent improvement costs incurred to improve a property to our operating standards or reach stabilization. These costs are normally taken into consideration during the underwriting process for a given property's acquisition. Non-recurring capital expenditures include improvements such as new building expansion and renovation costs.

We capitalize both recurring capital expenditures and non-recurring capital expenditures due to the probable benefit derived in future years from both non-recurring as well as recurring capital expenditures.

Contractual Obligations

As of December 31, 2004, we were subject to significant contractual payment obligations as described in the table below.

| | Payments Due by Period | | | | | | |
|-------------------------------|------------------------|-----------|-----------|-----------|-----------|-----------|------------|
| | Total | 2005 | 2006 | 2007 | 2008 | 2009 | Thereafter |
| | (in thousands) | | | | | | |
| Contractual Obligations: | | | | | | | |
| Long-term debt | | | | | | | |
| Mortgage debt | \$ 382,639 | \$ 7,436 | \$ 15,140 | \$ 8,710 | \$231,109 | \$112,674 | \$ 7,570 |
| Unsecured senior notes(1) | 700,000 | 200,000 | | 150,000 | | | 350,000 |
| Unsecured term loan | 125,000 | | 125,000 | | | | |
| Unsecured line of credit | 121,500 | 10,000 | 111,500 | | | | |
| Ground leases | 118,306 | 1,815 | 1,840 | 1,865 | 1,865 | 1,865 | 109,056 |
| Operating leases | 18,340 | 2,020 | 2,020 | 2,020 | 2,020 | 2,020 | 8,240 |
| Capital commitments | 26,498 | 26,498 | | | | | |
| Total Contractual Obligations | \$1,492,283 | \$247,769 | \$255,500 | \$162,595 | \$234,994 | \$116,559 | \$474,866 |

(1) Excludes amortization of discount on unsecured senior notes.

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The following table reflects the calculation of our funds from operations for the years ended December 31, 2004, 2003, 2002, 2001 and 2000 (in thousands, except percentages):

| | Year Ended December 31, | | | | |
|--|-------------------------|------------|------------|------------|------------|
| | 2004 | 2003 | 2002 | 2001 | 2000 |
| (in thousands, except ratio and per share amounts) | | | | | |
| Funds from Operations(1) | | | | | |
| Net income | \$ 73,775 | \$ 58,509 | \$ 70,175 | \$ 97,759 | \$ 96,710 |
| Depreciation and minority interest from discontinued operations | 5,842 | 8,871 | 11,520 | 9,725 | 9,050 |
| Gain on sale of discontinued properties | (30,473) | (5,937) | | | |
| Depreciation and amortization | 121,687 | 111,952 | 100,317 | 92,613 | 78,672 |
| Gain on sale of operating properties | | | (1,967) | (4,591) | (2,132) |
| Minority interest | 4,180(2) | 5,375 | 5,816 | 7,046 | 7,158 |
| Income allocated to Preferred Operating Partnership Units | (3,234)(2) | (4,312) | (4,312) | (4,312) | (4,312) |
| Funds from Operations(3) | 171,777 | 174,458 | 181,549 | 198,240 | 185,146 |
| Arden Realty's percentage share(4) | 97.5% | 97.4% | 97.3% | 96.8% | 96.7% |
| Arden Realty's share of Funds from Operations | \$ 167,483 | \$ 169,922 | \$ 176,647 | \$ 191,896 | \$ 179,036 |
| Weighted average common shares and operating partnership units outstanding Diluted | 67,415 | 65,513 | 66,098 | 66,132 | 65,759 |

- (1) We believe that funds from operations, or FFO, is a useful supplemental measure of our operating performance. We compute FFO in accordance with standards established by the White Paper on FFO approved by the Board of Governors of the National Association of Real Estate Investment Trusts, or NAREIT, in April 2002. The White Paper defines FFO as net income or loss computed in accordance with generally accepted accounting principles, or GAAP, excluding extraordinary items, as defined by GAAP, and gains and losses from sales of depreciable operating property plus real estate-related depreciation and amortization and after adjustments for unconsolidated partnerships and joint ventures.

We believe that FFO, by excluding depreciation costs, the gains or losses from the sale of operating real estate properties and the extraordinary items as defined by GAAP, provides an additional perspective on our operating results. However, because these excluded items have a real economic effect, FFO is a limited measure of performance.

FFO captures trends in occupancy rates, rental rates and operating costs. FFO excludes depreciation and amortization costs and it does not capture the changes in value in our properties that result from use or changes in market conditions or the level of capital expenditures and leasing costs necessary to maintain the operating performance of our properties, all of which are significant economic costs. Therefore, its ability to measure performance is limited.

Because FFO excludes significant economic components of net income determined in accordance with GAAP, FFO should be used as an adjunct to net income and not as an alternative to net income. FFO should also not be used as an indicator of our financial performance, or as a substitute for cash flow from operating activities determined in accordance with GAAP or as a measure of our liquidity. FFO is not by itself indicative of funds available to fund our cash needs, including our ability to pay dividends or service our debt. Therefore, FFO only provides investors with an additional performance measure that when combined with measures computed in accordance with GAAP such as net

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income, cash flow from operating activities, investing activities and financing activities provides investors with an indication of our ability to service debt and to fund acquisitions and other expenditures.

FFO is used by investors to compare our performance with other REITs. Other REITs may use different methods for calculating FFO and, accordingly, our FFO may not be comparable to other REITs.

- (2) Excludes approximately \$1.1 million of original issuance costs expensed in conjunction with the redemption of our Preferred Operating Partnership Units on September 28, 2004.
- (3) Includes approximately \$3.8 million, \$2.2 million, \$1.2 million, \$1.9 million and \$586,000 in non-cash compensation expense for the years ended December 31, 2004, 2003, 2002, 2001 and 2000, respectively.
- (4) Represents Arden Realty's weighted average ownership percentage during the respective twelve month period.

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Current Economic Climate

Our short and long-term liquidity, ability to refinance existing indebtedness, ability to issue long-term debt and equity securities at favorable rates and our dividend policy are significantly impacted by the operating results of our properties, all of which are located in Southern California. Our ability to lease available space and increase rates when leases expire is largely dependent on the demand for office space in the markets where our properties are located.

The timing and extent of future changes in the national and local economy and their effects on our properties and results of operations are difficult to accurately predict. It is possible, however, that these national and regional issues may more directly affect us and our operating results in the future, making it more difficult for us to lease and renew available space, to increase or maintain rental rates as leases expire and to collect amounts due from our tenants. For additional information, see Risk Factors Lack of non-farm job growth in Southern California or a deterioration of the local and national economy will adversely affect our operating results, The financial condition and solvency of our tenants may reduce our cash flow, and Rising energy costs and power outages in California may have an adverse effect on our operations and revenue.

ITEM 7A. *Quantitative and Qualitative Disclosure About Market Risk*

Market risk is the exposure or loss resulting from changes in interest rates, foreign currency exchange rates, commodity prices and equity prices. The primary market risk to which we are exposed is interest rate risk, which is sensitive to many factors, including governmental monetary and tax policies, domestic and international economic and political considerations and other factors that are beyond our control.

In order to modify and manage the interest characteristics of our outstanding debt and limit the effects of interest rates on our operations, we may use a variety of financial instruments, including interest rate hedges, caps, floors and other interest rate exchange contracts. The use of these types of instruments to hedge our exposure to changes in interest rates carries additional risks such as counter-party credit risk and legal enforceability of hedging contracts. We do not enter into any transactions for speculative or trading purposes. During 2004, we entered into \$300 million of forward-starting interest rate hedge agreements effectively fixing the 10-year Treasury Rate at approximately 4.37% for borrowings that are anticipated to occur in 2005 to refinance some of our scheduled debt maturities. In October and November of 2003, we also entered into reverse interest rate hedge agreements to float \$100 million of the fixed interest rate associated with the 7.00% senior unsecured notes due in November 2007. Under these reverse hedges, we will receive interest at a fixed rate of 7.00% and pay interest at a variable rate averaging the six-month LIBOR in arrears plus 3.10%.

Some of our future earnings, cash flows and fair values relating to financial instruments are dependent upon prevailing market rates of interest, such as LIBOR. Based on interest rates and outstanding balances as of December 31, 2004, a 1% increase in interest rates on our \$171.5 million of floating rate debt, including \$100 million in fixed rate debt swapped to floating through interest rate hedges, would decrease annual future earnings and cash flows by approximately \$1.7 million and would not have an impact on the fair value of the floating rate debt. A 1% decrease in interest rates on our \$171.5 million of floating rate debt would increase annual future earnings and cash flows by approximately \$1.7 million and would not have an impact on the fair value of the floating rate debt. The weighted average interest rate on our floating debt as of December 31, 2004 was 5.88%.

Our fixed rate debt, including \$175.0 million in floating rate debt swapped to fixed through interest rate hedges, totaled \$1,154.6 million as of December 31, 2004 with a weighted average interest rate of 7.05% and a total fair value of approximately \$1,177.0 million. A 1% decrease in interest rates on our \$1,154.6 million of fixed rate debt would increase its fair value by approximately \$36.3 million and would not have an impact on annual future earnings and cash flows. A 1% increase in interest rates on our \$1,154.6 million of fixed rate debt would decrease its fair value by approximately \$34.4 million and would not have an impact of annual future earnings and cash flows.

These amounts are determined by considering the impact of hypothetical interest rates on our borrowing cost. These analyses do not consider the effects of the reduced level of overall economic activity that could exist in that environment. Further, in the event of a change of this magnitude, we would consider taking

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actions to further mitigate our exposure to any such change. Due to the uncertainty of the specific actions that would be taken and their possible effects, however, this sensitivity analysis assumes no changes in our capital structure.

RISK FACTORS

In addition to the other information contained or incorporated by reference in this Form 10-K, readers should carefully consider the following risk factors.

Real Estate Investment Risks

An inability to retain tenants or rent space upon lease expirations may adversely affect our revenues and our ability to service our debt.

Through 2009, 2,625 leases, including month-to-month leases, comprising approximately 74% of our leased net rentable square footage and approximately 71% of our annualized base rents at December 31, 2004 are scheduled to expire as follows:

| Year | Number of Leases Expiring | Percentage of Aggregate Portfolio Leased Square Feet | Percentage of Aggregate Portfolio Annualized Base Rent |
|------|------------------------------|---|---|
| 2005 | 764 | 18.0% | 15.7% |
| 2006 | 596 | 15.0% | 14.6% |
| 2007 | 529 | 14.4% | 14.0% |
| 2008 | 392 | 14.0% | 14.4% |
| 2009 | 344 | 12.8% | 12.6% |

If we are unable to promptly renew or relet leases for all or a substantial portion of this space, or if the rent upon renewal or reletting are significantly lower than expected, our cash flow and business could be adversely affected which would limit our ability to service our debt.

Lack of non-farm job growth in Southern California or a deterioration of the local and national economy will adversely affect our operating results.

All of our properties are located in Southern California. In 2004, the Southern California economy experienced a 0.8% increase in job growth representing approximately 55,000 non-farm jobs. We believe non-farm job growth to be a leading indicator of office demand for the region. During 2005, a total of approximately 3.0 million square feet of occupied space, representing approximately 18.0% of our total net rentable space, including month-to-month leases, will expire. Negative non-farm job growth in our submarkets or a deterioration of the local and/or national economy may result in a decline in occupancy and rental rates and may cause tenant concessions to increase and would most likely negatively affect our operating performance and property values.

Competition affects occupancy levels, rents and cost of land which could adversely affect our revenues.

Many office properties compete with our properties in attracting tenants to lease space. Some of the competing properties may be newer, better located or owned by parties better capitalized than we are. Although ownership of these competing properties is currently diversified among many different types of owners, from publicly traded companies and institutional investors to small enterprises and individual owners, and no one or group of owners currently dominate or significantly influence the market, consolidation of owners could create efficiencies and marketing advantages for the consolidated group that could adversely affect us. These competitive advantages, the number of competitors and the number of competitive commercial properties in a particular area could have a material adverse effect on the rents we can charge, our ability to lease space in our existing properties or at newly acquired or developed properties and the prices we have to pay for developable land.

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The financial condition and solvency of our tenants may reduce our cash flow.

Tenants may experience a downturn in their business which may cause them to miss rental payments when due or to seek the protection of bankruptcy laws, which could result in rejection and termination of their leases or a delay in recovering possession of their premises. Although we have not experienced material losses from tenant bankruptcies, we cannot assure you that tenants will not file for bankruptcy protection in the future or, if any tenants file, that they will affirm their leases and continue to make rental payments in a timely manner.

Because real estate investments are illiquid, we may not be able to sell properties when appropriate.

Equity real estate investments are relatively illiquid. That illiquidity may tend to limit our ability to sell properties promptly in response to changes in economic or other conditions. In addition, the Internal Revenue Code of 1986, as amended, may under specified circumstances impose a 100% prohibited transaction tax on the profits derived from our sale of properties held for fewer than four years, which could affect our ability to sell our properties.

Rising energy costs and power outages in California may have an adverse effect on our operations and revenue.

Problems associated with deregulation of the electric industry in California have resulted in significantly higher costs in some areas. All of our properties are currently located in areas served by utilities that either produce their own electricity, or that have procured long-term, fixed rate contracts with commercial electrical providers. While we have no information suggesting that any future service interruptions are expected, we believe that higher utility costs may continue as price increases are allowed by the California Public Utility Commission or other regulatory agencies.

Approximately 26% of our buildings and 19% of the total rentable square footage of our portfolio are subject to leases that require our tenants to pay all utility costs. The remainder of our leases provide that tenants will reimburse us for utility costs in excess of a base year amount.

Although we have not experienced any material losses resulting from electric deregulation, it is possible that some or all of our tenants will not fulfill their lease obligations and reimburse us for their share of any significant electric rate increases and that we will not be able to retain or replace our tenants if energy problems in California continue.

Increases in taxes and regulatory compliance costs may reduce our revenue.

Except for our triple net leases, we may not be able to pass all real estate tax increases through to some or all of our tenants. Therefore, any tax increases may adversely affect our cash flow and our ability to pay or refinance our debt obligations. Our properties are also subject to various federal, California and local regulatory requirements, such as requirements of the Americans with Disabilities Act, and California and local fire and life safety requirements. Failure to comply with these requirements could result in the imposition of fines by governmental authorities or awards of damages to private litigants. We believe that our properties are currently in substantial compliance with these regulatory requirements. We cannot assure you, however, that these requirements will not be changed or that new requirements will not be imposed that would require significant unanticipated expenditures by us and could have an adverse effect on our cash flow, the amounts available for distributions and on our business.

We may acquire properties through partnerships or joint ventures with third parties that could result in financial dependency and management conflicts.

We may participate with other entities in property ownership through joint ventures or partnerships in the future. Depending on the characteristics and business objectives of the joint venture or partnership, we may

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not have voting control over the joint venture or partnership. Partnership or joint venture investments may, under certain circumstances, involve risks not otherwise present, including:

our partners or co-venturers might become bankrupt;

our partners or co-venturers might at any time have economic or other business interests or goals which are inconsistent with our business interests or goals; and

our partners or co-venturers may be in a position to take action contrary to our instructions or requests contrary to our policies or objectives.

Neither the partnership agreement of our Operating Partnership nor our governing documents prevent us from participating in joint ventures with our affiliates. Because a joint venture with an affiliate may not be negotiated in a traditional arm's length transaction, terms of the joint venture may not be as favorable to us as we could obtain if we entered into a joint venture with an outside third party.

We may not be able to successfully integrate or finance our acquisitions.

As we acquire additional properties, we will be subject to risks associated with managing new properties, including building systems not operating as expected, delay in or failure to lease vacant space and tenants failing to renew leases as they expire. In addition, our ability to manage our growth effectively will require us to successfully integrate our new acquisitions into our existing accounting systems and property management structure. We cannot assure you that we will be able to succeed with that integration or effectively manage additional properties or that newly acquired properties will perform as expected. Changing market conditions, including competition from other purchasers of suburban office properties, may diminish our opportunities for attractive additional acquisitions. Moreover, acquisition costs of a property may exceed original estimates, possibly making the property uneconomical.

Our acquisitions and renovations may not perform as expected.

Although we currently have no plans to significantly expand or renovate our properties, we may do so in the future. Expansion and renovation projects may inconvenience and displace existing tenants, require us to engage in time consuming up-front planning and engineering activities and expend capital, and require us to obtain various government and other approvals, the receipt of which cannot be assured. While our policies with respect to expansion and renovation activities are intended to limit some of the risks otherwise associated with these activities, we will nevertheless incur risks, including expenditures of funds on, and devotion of our time to, projects that may not be completed.

Our development activities may be more expensive than anticipated and may not yield our anticipated results.

We have preliminary architectural designs completed for an additional 475,000 net rentable square feet at the Howard Hughes Center in Los Angeles, California and have completed preliminary designs on a build-to-suit office building at our Long Beach Airport Business Park. We have entitlements for up to 600 hotel rooms at the Howard Hughes Center. We also have a 5-acre developable land parcel in Torrance, California that we are also marketing for a build-to-suit building. We do not intend to commence construction on any of these projects until development plans and budgets are finalized and build-to-suit tenant leases are signed with terms allowing us to achieve yields commensurate with each project's development risk. We also intend to review, from time to time, other opportunities for developing and constructing office buildings and other commercial properties in accordance with our development and underwriting policies.

We expect to finance our development activities over the next 24 months through net cash provided by operating activities, proceeds from asset sales, proceeds from our lines of credit or other secured borrowings.

Risks associated with our development activities may include:

abandonment of development opportunities due to a lack of financing or other reasons;

construction costs of a property exceeding original estimates, possibly making the property uneconomical;

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occupancy rates and rents at a newly completed property may not be sufficient to make the property profitable;

construction and lease-up may not be completed on schedule, resulting in increased debt service expense and construction costs; and

development activities would also be subject to risks relating to the inability to obtain, or delays in obtaining, all necessary zoning, land-use, building, occupancy and other required governmental permits and authorizations.

We are not subject to any limit on the amount or percentage of our assets that may be invested in any single property or any single geographic area.

Our governing documents do not restrict the amount or percentage of our assets that we may invest in a single property or geographic area. All of our properties are currently in Southern California and we have no immediate plans to invest outside of Southern California. Although the overall Southern California economy is diverse and well balanced, the geographic concentration of our portfolio may make us more susceptible to changes affecting the Southern California economy and real estate markets or damages from regional events such as earthquakes.

We may not be able to expand into new markets successfully.

While our business is currently limited to the Southern California market, it is possible that we will in the future expand our business to new geographic markets. We will not initially possess the same level of familiarity with new markets outside of Southern California, which could adversely affect our ability to manage, lease, develop or acquire properties in new localities.

Financing Risks

Our amount of debt could limit our operational flexibility or otherwise adversely affect our financial condition.

As of December 31, 2004, we had total debt of approximately \$1.3 billion, consisting of approximately \$382.6 million in secured debt and approximately \$943.4 million of unsecured debt. See Management's Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources.

Our indebtedness could:

require us to dedicate a substantial portion of our cash flow to pay our debt, thereby reducing the availability of our cash flow to fund distributions, working capital, capital expenditures, acquisition and development activity and other business purposes;

make it more difficult for us to satisfy our debt obligations;

limit our ability to refinance our debt and obtain additional debt financing; and

increase our vulnerability to general adverse economic and real estate industry conditions and limit our flexibility in planning for, or reacting to, changes in our business and the real estate industry.

Despite current indebtedness levels, we may still be able to incur substantially more debt in the future, which would increase the risks associated with our substantial leverage. Neither the partnership agreement of our Operating Partnership nor our governing documents limit the amount or the percentage of indebtedness that we may incur. We may borrow up to a maximum of \$330 million under our two lines of credit. As of December 31, 2004, we had the ability to borrow an additional \$208.5 million under these two lines of credit. If new debt is added to our current debt levels, the related risks that we now face could intensify and could increase the risk of default on our indebtedness.

Scheduled debt payments could adversely affect our financial condition.

Our cash flow could be insufficient to meet required payments of principal and interest when due. In addition, we may not be able to refinance existing indebtedness, which in virtually all cases requires substantial principal payments at maturity, and, if we can refinance, the terms of the refinancing might not be as favorable

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as the terms of our existing indebtedness. As of March 10, 2005, approximately \$102.4 million of principal will be coming due over the next eighteen months. If principal payments cannot be refinanced, extended or paid with proceeds of other capital transactions, such as new equity capital, our cash flow will not be sufficient in all years to repay all maturing debt and continue to service and repay our debt obligations.

Rises in interest rates could adversely affect our financial condition.

An increase in prevailing interest rates would have an immediate effect on the interest rates charged on our variable rate debt which rise and fall upon changes in interest rates. At December 31, 2004, approximately 13% of our debt was variable rate debt. Increases in interest rates would also impact the refinancing of our fixed rate debt. If interest rates are higher when our fixed debt becomes due, we may be forced to borrow at the higher rates. If prevailing interest rates or other factors result in higher interest rates, the increased interest expense would adversely affect our cash flow and our ability to service our debt. As a protection against rising interest rates, we may enter into agreements such as interest rate hedges, caps, floors and other interest rate exchange contracts. These agreements, however, increase our risks as to the other parties to the agreements not performing or that the agreements could be unenforceable. During 2004, we entered into \$300 million of forward-starting interest rate hedge agreements effectively fixing the 10-year Treasury Rate at approximately 4.37% for borrowings that are anticipated to occur in 2005 to refinance some of our scheduled debt maturities. In October and November of 2003, we also entered into reverse interest rate hedge agreements to float \$100 million of the fixed interest rate associated with the 7.00% senior unsecured notes due in November 2007. Under these reverse hedges, we will receive interest at a fixed rate of 7.00% and pay interest at a variable rate averaging the six-month LIBOR in arrears plus 3.10%.

Many of our properties are subject to mortgage financing which could result in foreclosure if we are unable to pay or refinance the mortgages when due.

We currently have outstanding four mortgage financings totaling approximately \$365.3 million that are secured by 49 of our properties. The properties in each of these financings are fully cross-collateralized and cross-defaulted. To the extent two or more mortgages are cross-defaulted, a default in one mortgage will trigger a default in the other mortgages. The cross-defaults can give the lender a number of remedies depending on the circumstances such as the right to increase the interest rate, demand additional collateral, accelerate the maturity date of the mortgages or foreclose on and sell the properties. To the extent two or more mortgages are cross-collateralized, a default in one mortgage will allow the mortgage lender to foreclose upon and sell the properties that are not the primary collateral for the loan in default. Four additional properties are subject to single property mortgages totaling approximately \$17.3 million at December 31, 2004. If we are unable to meet our obligations under these mortgages, we could be forced to pay higher interest rates or provide additional collateral or the properties subject to the mortgages could be foreclosed upon and sold, which could have a material adverse effect on us and our ability to pay or refinance our debt obligations.

Tax Risks

Our desire to qualify as a REIT restricts our ability to accumulate cash that might be used in future periods to make debt payments or to fund future growth.

In order to qualify as a REIT and avoid federal income tax liability, we must distribute to our stockholders at least 90% of our net taxable income, excluding net capital gain, and to avoid income taxation, our distributions must not be less than 100% of our net taxable income, including capital gains. To avoid excise tax liability, our distributions to our stockholders for the year must exceed the sum of 85% of its ordinary income, 95% of its capital gain net income, and any undistributed taxable income from prior years. As a result of these distribution requirements, we do not expect to accumulate significant amounts of cash. Accordingly, these distributions could significantly reduce the cash available to us in subsequent periods to make payments on our debt obligations and to fund future growth.

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Our Operating Partnership intends to qualify as a partnership, but we cannot guarantee that it will qualify.

Our Operating Partnership intends to qualify as a partnership for federal income tax purposes. However, if the Operating Partnership were a publicly traded partnership, it would be treated as a corporation instead of a partnership for federal income tax purposes unless at least 90% of its income is qualifying income as defined in the Internal Revenue Code. The income requirements applicable to REITs and the definition of qualifying income for purposes of this 90% test are similar in most respects. Qualifying income for the 90% test generally includes passive income, such as specified types of real property rents, dividends and interest. We believe that the Operating Partnership would meet this 90% test, but we cannot guarantee that it would. If the Operating Partnership were to be taxed as a corporation, it would incur substantial tax liabilities and we would fail to qualify as a REIT for federal income tax purposes.

We may suffer adverse tax consequences and be unable to attract capital if we fail to qualify as a REIT.

We believe that since our taxable year ended December 31, 1996, we have been organized and operated, and intend to continue to operate, so as to qualify for taxation as a REIT under the Internal Revenue Code. Although we believe that we have been and will continue to be organized and have operated and will continue to operate so as to qualify for taxation as a REIT, we cannot assure you that we have been or will continue to be organized or operated in a manner so as to qualify or remain so qualified. For us to qualify as a REIT, we must satisfy numerous requirements established under highly technical and complex Internal Revenue Code provisions for which there are only limited judicial and administrative interpretations and tests regarding various factual matters and circumstances not entirely within our control. The complexity of these provisions and of the applicable Treasury Regulations that have been promulgated under the Internal Revenue Code is greater in the case of a REIT, like us, that holds its assets through an investment in a partnership. No assurance can be given that legislation, new regulations, administrative interpretations or court decisions will not significantly change the tax laws with respect to our qualification as a REIT or the federal income tax consequences of qualification. We are, however, not aware of any pending legislation that would adversely affect our ability to qualify as a REIT. Our qualification and taxation as a REIT depends on our ability to meet, through actual annual operating results, asset diversification, distribution levels and diversity of stock ownership, the various qualification tests imposed under the Internal Revenue Code, the results of which have not been and will not be reviewed by our tax counsel.

If we failed to qualify as a REIT in any taxable year, we would be subject to federal income tax, including any applicable alternative minimum tax, on our taxable income at regular corporate rates. Moreover, unless entitled to relief under specific statutory provisions, we also would be disqualified as a REIT for the four taxable years following the year during which qualification was lost. If we were disqualified as a REIT, our ability to raise additional capital could be significantly impaired. This could reduce the funds we would have available to pay distributions to our stockholders and to service our debt.

Even if we qualify for and maintain our REIT status, we will be subject to certain federal, state and local taxes on our income and property. For example, if we have net income from a prohibited transaction, specifically sales or other taxable dispositions of property held primarily for sale to customers in the ordinary course of business, that income will be subject to a 100% tax.

Other Risks

We are subject to agreements and policies that may deter change in control offers that might be attractive to our stockholders.

Certain provisions of our charter and bylaws may delay, defer or prevent a third party from making offers to acquire us or assume control over us. For example, such provisions may:

deter tender offers for our common stock, which offers may be attractive to the stockholders; and

deter purchases of large blocks of common stock, thereby limiting the opportunity for stockholders to receive a premium for their common stock over then-prevailing market prices.

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Our charter contains a provision designed to prevent a concentration of ownership among our stockholders that would cause us to fail to qualify as a REIT. Under the Internal Revenue Code, not more than 50% in value of our outstanding shares of common stock may be owned, actually or constructively, by five or fewer individuals, including specific kinds of entities, at any time during the last half of our taxable year. In addition, if we, or an owner of 10% or more of our common stock, actually or constructively owns 10% or more of a tenant of ours, or a tenant of any partnership in which we are a partner, the rent received by us from that tenant will not be qualifying income for purposes of the REIT gross income tests. In order to protect us against the risk of losing REIT status, the ownership limit included in our charter limits actual or constructive ownership of our outstanding shares of common stock by any single stockholder to 9.0%, by value or by number of shares, whichever is more restrictive, of the then outstanding shares of common stock. Actual or constructive ownership of shares of common stock in excess of the ownership limit will cause the violative transfer or ownership to be void with respect to the transferee or owner as to that number of shares in excess of the ownership limit and such shares will be automatically transferred to a trust for the exclusive benefit of one or more qualified charitable organizations. That transferee or owner will have no right to vote such shares or be entitled to dividends or other distributions with respect to such shares.

Although our Board of Directors presently has no intention of doing so, except as described below, our Board of Directors could waive this restriction with respect to a particular stockholder if it were satisfied, based upon the advice of counsel or a ruling from the Internal Revenue Service, that ownership by such stockholder in excess of the ownership limit would not jeopardize our status as a REIT and our Board of Directors otherwise decided such action would be in our best interests. Our Board of Directors has waived our ownership limit with respect to Mr. Ziman, our Chairman and CEO, and certain family members and affiliates and has permitted these parties to actually and constructively own up to 13.0% of the outstanding shares of common stock.

Our charter authorizes our Board of Directors to cause us to issue authorized but unissued shares of common stock or preferred stock and to reclassify any unissued shares of common stock or classify any unissued and reclassify any previously classified but unissued shares of preferred stock and, with respect to the preferred stock, to set the preferences, rights and other terms of such classified or unclassified shares. Although our Board of Directors has no such intention at the present time, it could establish a series of preferred stock that could, depending on the terms of such series, delay, defer or prevent a transaction or a change in control that might involve a premium price for the common stock or otherwise be in the best interest of our stockholders.

Our Board of Directors is divided into three classes of directors. Directors of each class are chosen for three-year terms upon the expiration of their current terms and each year one class of directors will be elected by the stockholders. The staggered terms of directors may reduce the possibility of a tender offer or an attempt to change control even though a tender offer or change in control might be in the best interest of our stockholders.

Losses in excess of our insurance coverage or uninsured losses could adversely affect our cash flow.

We carry comprehensive liability, fire, extended coverage, terrorism and rental loss insurance policies which currently cover all of our properties with specifications and insured limits that we believe are adequate and appropriate under the circumstances. Some losses, however, are generally not insured against because it is not economically feasible to do so. Should an uninsured loss or a loss in excess of insured limits occur, we could lose our capital invested in the property, as well as the anticipated future revenue from the property and, in the case of debt which is recourse to us, we would remain obligated for any mortgage debt or other financial obligations related to the property. Any loss would adversely affect our cash flow with respect to the property subject to the loss. Moreover, we would generally be liable for any unsatisfied obligations other than non-recourse obligations with respect to the property subject to the loss.

Lack of availability of insurance coverage for biological, chemical or nuclear terrorist attacks could adversely affect our financial condition.

Our current terrorism insurance policy, which has been extended to March 2006 subject to the continuation of the Terrorism Risk Insurance Act of 2002 (TRIA), specifically excludes biological, chemical

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or nuclear terrorist acts. We have been notified by our insurance broker that in the aftermath of the September 11th attacks, insurance carriers will continue to exclude these types of attacks from terrorism insurance policies or offer coverage for biological, chemical or nuclear attacks coverages at prohibitive costs. Although we did not derive more than 3.6% of our 2004 net operating income from any one of the properties in our portfolio, a biological, chemical or nuclear terrorist attack damaging several of our properties or negatively impacting the financial condition of our tenants could materially deteriorate our operating results and overall financial condition.

An earthquake could adversely affect our business.

All of our properties are located in Southern California which is a high risk geographical area for earthquakes. Depending upon its magnitude, an earthquake could severely damage our properties which would adversely affect our business. We maintain earthquake insurance for our properties and the resulting business interruption. We cannot assure you that our insurance will be sufficient if there is a major earthquake.

Our properties may be subject to environmental liabilities.

Under federal, state and local environmental laws, a current or previous owner or operator of real estate may be required to investigate and clean up hazardous or toxic substances or petroleum product releases at the property and may be held liable to a governmental entity or to third parties for property damage and for investigation and clean-up costs in connection with the contamination. These laws typically impose clean-up responsibility and liability without regard to whether the owner knew of or caused the presence of the contaminants, and the liability under these laws has been interpreted to be joint and several unless the harm is divisible and there is a reasonable basis for allocation of responsibility. These costs may be substantial, and the presence of these substances, or the failure to remediate the contamination on the property, may adversely affect the owner's ability to sell or rent the property or to borrow against the property. Finally, third parties may have claims against the owner of the site based on damages and costs resulting from environmental contamination emanating from that site.

Specific federal, state and local laws, regulations and ordinances govern the removal, encapsulation or disturbance of asbestos-containing materials when those materials are in poor condition or in the event of construction, remodeling, renovation or demolition of a building. These laws may impose liability for release of asbestos-containing material and may provide for third parties to seek recovery from owners or operators of real properties for personal injury associated with asbestos-containing materials. In connection with the ownership and operation of our properties, we may be potentially liable for those costs.

In the past few years, independent environmental consultants have conducted or updated Phase I environmental assessments and other environmental investigations as appropriate at some of our properties. The environmental site assessments and investigations have identified 35 properties in our portfolio, representing approximately 35% of the total rentable square feet in the portfolio, affected by environmental concerns. These environmental concerns include properties that may be impacted by known or suspected (a) contamination caused by third party sources or (b) soil and/or groundwater contamination which has been remediated, and (c) those containing underground storage tanks or asbestos.

Of these properties, two are believed to be affected by contamination caused by third party sources and also house an underground storage tank, two contain friable asbestos, twenty-three contain non-friable asbestos, and eight house underground storage tanks only. The properties affected by contamination are primarily affected by petroleum and solvent substances, and in each case a third party has indemnified us for any and all problems associated with this contamination. With regard to those properties affected by asbestos, asbestos does not pose a health hazard if it is not disturbed in such a way to cause an airborne release of asbestos. Asbestos is friable when it can be crumbled, pulverized or reduced to powder by hand pressure, and non-friable when hand pressure cannot release encapsulated asbestos fibers. Friable asbestos is more likely to be released into the air than non-friable asbestos. We manage all asbestos in ways that minimize its potential to become airborne or otherwise threaten human health. Regarding underground storage tanks, subsurface leakage of the materials contained within the tank constitutes the primary risk posed by these devices. There are no known UST-related violations or outstanding compliance issues with regulatory agencies. We have also

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implemented a program to ensure appropriate double-wall construction, testing protocols, placement of tanks within bermed areas, and the installation of leak and spill detection equipment at relevant sites.

Environmental site assessments and investigations completed to date have not, however, revealed any environmental liability that we believe would have a material adverse effect on our business, assets or results of operations taken as a whole, nor are we aware of any material environmental liability. Nevertheless, it is possible that our environmental site assessments do not reveal all environmental liabilities or that there are material environmental liabilities of which we are unaware.

We believe that our properties are in compliance in all material respects with all federal, state and local laws regarding hazardous or toxic substances or petroleum products, except as noted above. We have not been notified by any governmental authority, and are not otherwise aware, of any material noncompliance, liability or claim relating to hazardous or toxic substances or petroleum products in connection with any of our present properties, other than as noted above. It is possible that future laws will impose material environmental liabilities on us and that the current environmental condition of our properties will be affected by tenants, by the condition of land or operations in the vicinity of our properties, such as the presence of underground storage tanks, or by third parties unrelated to us.

We may incur increased costs as a result of enacted and proposed changes in laws and regulations.

Enacted and proposed changes in the law and regulations affecting public companies, including the provisions of the Sarbanes-Oxley Act of 2002 and rules proposed by the SEC and by the New York Stock Exchange has resulted in significant increased compliance costs to us as we evaluate the implications of any new rules and comply to their requirements. The new rules could make it more difficult or more costly for us to obtain certain types of insurance, including director and officer liability insurance, and we may be forced to accept reduced policy limits and coverage or incur substantially higher costs to obtain the same or similar coverage. The impact of these events could also make it more difficult for us to attract and retain qualified persons to serve on our board of directors, our board committees or as executive officers. The compliance with and the provisions of the Sarbanes-Oxley Act in future years will result in significant continuing costs to us.

ITEM 8. Financial Statements and Supplementary Data

The financial statements and supplementary data required by Regulation S-X are included in this Report on Form 10-K commencing on page F-1.

The Board of Directors and Shareholders of Arden Realty, Inc.

We have audited management's assessment, included in the accompanying Management's Report on Internal Control over Financial Reporting, that Arden Realty, Inc. maintained effective internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Arden Realty, Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company;

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(2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

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

In our opinion, management's assessment that Arden Realty, Inc. maintained effective internal control over financial reporting as of December 31, 2004, is fairly stated, in all material respects, based on the COSO criteria. Also, in our opinion, Arden Realty, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2004, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets as of December 31, 2004 and 2003 and the related consolidated statements of income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2004 of Arden Realty, Inc. and our report dated March 10, 2005 expressed an unqualified opinion thereon.

Ernst & Young LLP

Los Angeles, California
March 10, 2005

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ITEM 9. *Changes in and Disagreements with Accountants on Accounting and Financial Disclosure*

None.

**ITEM 9A. *Controls and Procedures*
Evaluation of Disclosure Controls and Procedures**

We have established disclosure controls and procedures that are designed to ensure that information required to be disclosed by Arden Realty, Inc., including its consolidated entities, in its reports under the Securities and Exchange Act of 1934, as amended (the "Act") is recorded, processed, summarized and reported, within the time periods specified in the U.S. Securities and Exchange Commission's rules and forms and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As of and for the year ended December 31, 2004, we carried out an evaluation, under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on the foregoing, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective.

Management's Report on Internal Control Over Financial Reporting

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

Management is responsible for establishing and maintaining adequate internal control over financial reporting. Arden Realty, Inc.'s internal control over financial reporting is supported by written policies and procedures and by an appropriate segregation of responsibilities and duties. Arden Realty, Inc. has used the criteria set forth in the *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission to assess its internal control over financial reporting. Based upon this assessment, management concluded that internal control over financial reporting is operating effectively as of December 31, 2004. Ernst & Young LLP has audited Arden Realty, Inc.'s financial statements and has issued an attestation report on management's assessment of internal control over financial reporting.

Submitted on March 10, 2005

ITEM 9B. *Other Information*

None.

Table of Contents**PART III**

The information required by Part III is incorporated by reference from our definitive proxy statement for our 2005 Annual Meeting of Stockholders.

ITEM 10. Directors and Executive Officers of the Registrant

The information contained in the sections captioned Proposal I; Election of Directors and Section 16(a) Beneficial Ownership Reporting Compliance of the definitive proxy statement is incorporated herein by reference.

ITEM 11. Executive Compensation

The information contained in the section captioned Executive Compensation of the definitive proxy statement is incorporated herein by reference.

ITEM 12. Security Ownership of Certain Beneficial Owners and Management Equity Compensation Plan Information

The following table provides information as of December 31, 2004 with respect to shares of our common stock that may be issued under our existing equity compensation plans (in thousands, except per share amounts):

| Plan Category | Number of shares of common stock to be issued upon exercise of outstanding options, warrants and rights | Weighted-average exercise price of outstanding options, warrants and rights | Number of shares of common stock remaining available for future issuance under equity compensation plans (excluding shares reflected in column (a))(1) |
|--|---|---|--|
| | (a) | (b) | (c) |
| Equity Compensation plans approved by shareholders | 1,556 | \$25.11 | 542 |
| Equity Compensation plans not approved by shareholders | 80(2) | 24.13 | — |
| Total | 1,636 | \$25.06 | 542 |

(1) Includes shares available for issuance under restricted stock grants.

(2) On October 15, 1997, 10,000 options with an exercise price of \$32.25, on December 15, 1998, 40,000 options with an exercise price of \$22.50, and on November 30, 1999, 10,000 options with an exercise price of \$19.25 were granted to each of our non-employee directors: Carl D. Covitz, Larry S. Flax, Steven C. Good and Kenneth B. Roath; Peter S. Gold participated only in the 1998 and 1999 grants. All of these options were granted with an exercise price equal to fair market value on the date of grant, vest during the non-employee directors continued service with Arden over a three-year period, with one third of the options vesting on each anniversary of the grant date and expire ten years from the anniversary of the grant date, subject to earlier termination upon the happening of certain events. From these grants, Mr. Roath and Mr. Good exercised 50,000 and 40,000 options, respectively, during 2003. In addition, Mr. Roath forfeited 10,000 options upon his retirement in 2003. Mr. Covitz, Mr. Flax and Mr. Good exercised 50,000, 40,000 and 20,000 options, respectively, during 2004.

The other information contained in the section captioned Security Ownership of Principal Stockholders and Management of the definitive proxy statement is incorporated herein by reference.

ITEM 13. Certain Relationships and Related Transactions

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The information contained in the section captioned Certain Relationships and Related Transactions of the definitive proxy statement is incorporated herein by reference.

ITEM 14. *Principal Accountant Fees and Services*

The information contained in the section captioned Proposal 2: Ratification of Appointment of Independent Auditors of the definitive proxy statement is incorporated herein by reference.

Table of Contents**PART IV****ITEM 15. Exhibits, Financial Statement Schedules and Reports on Form 8-K****(a) Financial Statements**

The following consolidated financial information is included as a separate section of this Annual Report on Form 10-K:

| | <u>Page No.</u> |
|--|-----------------|
| Report of Independent Auditors | F-1 |
| Consolidated Balance Sheets as of December 31, 2004 and 2003 | F-2 |
| Consolidated Statements of Income for the years ended December 31, 2004, 2003 and 2002 | F-3 |
| Consolidated Statements of Stockholders' Equity for the years ended December 31, 2004, 2003 and 2002 | F-4 |
| Consolidated Statements of Cash Flows for the years ended December 31, 2004, 2003 and 2002 | F-5 |
| Notes to Financial Statements | F-6 |

All other schedules are omitted since the required information is not present in amounts sufficient to require submission of the schedule or because the information required is included in the financial statements and notes thereto.

(b) Reports on Form 8-K

Form 8-K filed on November 4, 2004, furnishing a press release announcing the registrant's earnings for the third quarter of 2004 (Item 12).

(c) Exhibits

| <u>Exhibit Number</u> | <u>Description</u> |
|-----------------------|--|
| 3.1* | Amended and Restated Articles of Incorporation as filed as an exhibit to Arden Realty's registration statement on Form S-11 (No. 333-08163). |
| 3.2* | Articles Supplementary of Class A Junior Participating Preferred Stock as filed as an exhibit to the current report on Form 8-K, dated August 26, 1998. |
| 3.3* | Articles Supplementary of the 8 5/8 Series B Cumulative Redeemable Preferred Stock dated September 7, 1999, filed as an exhibit to Arden Realty's annual report on Form 10-K dated March 27, 2000. |
| 3.4* | Bylaws of Registrant as filed as an exhibit to Arden Realty's registration statement on Form S-11 (No. 333-08163). |
| 3.5* | Certificate of Amendment of the Bylaws of Arden Realty dated July 14, 1998, filed as an exhibit to Arden Realty's quarterly report on Form 10-Q dated August 14, 1998. |
| 3.6* | Certificate of Amendment of the Bylaws of Arden Realty dated March 17, 2000, filed as an exhibit on Arden Realty's quarterly report on Form 10-Q dated May 11, 2000. |
| 4.1* | Rights Agreement, dated August 14, 1998, between Arden Realty and The Bank of New York, as filed as an exhibit to Arden Realty's current report on Form 8-K dated August 26, 1998. |
| 4.2* | Indenture between Arden Realty Limited Partnership and The Bank of New York, as trustee, dated March 14, 2000 as filed as an exhibit to Arden Realty Limited Partnership's registration statement on Form S-4 (No. 333-35406). |
| 4.3* | Form of Arden Realty Limited Partnership's unsecured 8.875% senior note due 2005, dated March 17, 2000 filed as an exhibit to Arden Realty Limited Partnership's registration statement on Form S-4 (No. 333-35406). |

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- 4.4* Form of Arden Realty Limited Partnership's unsecured 9.150% senior note due 2010, dated March 17, 2000 filed as an exhibit to Arden Realty Limited Partnership's registration statement on Form S-4 (No. 333-35406).
- 4.5* Form of Arden Realty Limited Partnership's unsecured 8.50% senior note due 2010, dated November 20, 2000 as filed as an exhibit to Arden Realty Limited Partnership's registration statement on Form S-4 (No. 333-53376).

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| Exhibit Number | Description |
|-------------------|---|
| 4.6* | Form of Arden Realty Limited Partnership's 7.00% Note due 2007, dated November 9, 2002 as filed as an exhibit to Arden Realty Limited Partnership's current report on Form 8-K filed on November 9, 2001. |
| 4.7* | Officers' certificate dated March 17, 2000 with respect to the terms of Arden Realty Limited Partnership's 8.875% senior note due 2005 and 9.150% Senior Notes due 2010 as filed as an exhibit to Arden Realty's annual report on Form 10-K filed on April 1, 2002. |
| 4.8* | Officers' certificate dated November 20, 2000 with respect to the terms of Arden Realty Limited Partnership's 8.50% Senior Notes due 2010 as filed as an exhibit to Arden Realty's annual report on Form 10-K filed on April 1, 2002. |
| 4.9* | Officers' certificate dated November 9, 2001 with respect to the terms of Arden Realty Limited Partnership's 7.00% Note due 2007, filed as an exhibit to Arden Realty Limited Partnership's current report on Form 8-K filed on November 9, 2001. |
| 4.10* | Second Amendment to Rights Agreement, dated as of June 19, 2003, between Arden Realty and the Bank of New York, as filed as an exhibit to Arden Realty's current report on Form 8-K dated July 1, 2003. |
| 10.1*^ | 1996 Stock Option and Incentive Plan of Arden Realty, Inc. and Arden Realty Limited Partnership as filed as an exhibit to Arden Realty's registration statement on Form S-11 (No. 333-08163). |
| 10.2*^ | Amendment Number 1 to the 1996 Stock Option and Incentive Plan of Arden Realty, Inc. and Arden Realty Limited Partnership as filed as an exhibit to Arden Realty's Schedule 14A filed on June 23, 1998. |
| 10.3*^ | Form of Officers and Directors Indemnification Agreement as filed as an exhibit to Arden Realty's registration statement on Form S-11 (No. 333-08163). |
| 10.4* | Loan Agreement dated June 8, 1998 by and between Arden Realty Finance III, L.L.C., a Delaware limited liability company and Lehman Brothers Realty Corporation, a Delaware corporation filed as an exhibit to Arden Realty's quarterly report on Form 10-Q filed on August 14, 1998. |
| 10.5* | Mortgage Note, dated June 8, 1998 for \$136,100,000 by and between Arden Realty Finance III, L.L.C., a Delaware limited liability company, and Lehman Brothers Realty Corporation, a Delaware corporation. (Exhibit B. to Exhibit 10.4 above). |
| 10.6* | Tenant Estoppel Certificate (Exhibit C. to Exhibit 10.4 above). |
| 10.7* | Subordination, Non-Disturbance and Attornment Agreement (Exhibit D. to Exhibit 10.4 above). |
| 10.8* | Deed of Trust, Assignment of Rents and Leases, Security Agreement, and Fixture Filing dated as of June 8, 1998 made by Arden Realty Finance III, L.L.C. as Grantor, to Commonwealth Land Title Company as Trustee for the benefit of Lehman Brothers Realty Corporation as Beneficiary, filed as an exhibit to Arden Realty's quarterly report on Form 10-Q filed on August 14, 1998. |
| 10.9* | Assignment of Leases and Rents dated June 8, 1998, by and between Arden Realty Finance III, L.L.C., a Delaware limited liability company and Lehman Brothers Realty Corporation, a Delaware corporation, its successors and assigns filed as an exhibit to Arden Realty's quarterly report on Form 10-Q filed on August 14, 1998. |
| 10.10* | Collateral Assignment of Management Agreement and Subordination Agreement dated as of June 8, 1998 among Arden Realty Finance III, L.L.C., a Delaware limited liability company (Borrower), Lehman Brothers Realty Corporation, a Delaware corporation, (Lender), and Arden Realty Limited Partnership, a Maryland limited partnership (Manager), filed as an exhibit to Arden Realty's quarterly report on Form 10-Q filed on August 14, 1998. |
| 10.11* | Security Agreement entered into as of June 8, 1998 by and between Arden Realty Finance III, L.L.C., a Delaware limited liability company and Lehman Brothers Realty Corporation, a Delaware corporation, filed as an exhibit to Arden Realty's quarterly report on Form 10-Q filed on August 14, 1998. |

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| Exhibit Number | Description |
|-------------------|--|
| 10.12* | Environmental Indemnity Agreement dated June 8, 1998 by Arden Realty Finance III, L.L.C., a Delaware limited liability company, in favor of Lehman Brothers Realty Corporation, a Delaware corporation, filed as an exhibit to Arden Realty's quarterly report on Form 10-Q filed on August 14, 1998. |
| 10.13* | Letter Agreement dated June 8, 1998 between Lehman Brothers Realty Corporation, Arden Realty Finance III, L.L.C., Arden Realty and Arden Realty Limited Partnership, filed as an exhibit to Arden Realty's quarterly report on Form 10-Q filed on August 14, 1998. |
| 10.14* | Loan Agreement by and between Arden Realty Finance IV, LLC, a Delaware limited liability company and Lehman Brothers Realty Corporation, a Delaware corporation, filed as an exhibit to Arden Realty's quarterly report on Form 10-Q filed on August 14, 1998. |
| 10.15* | Mortgage Note, dated June 8, 1998 for \$100,600,000 by and between Arden Realty Finance IV, L.L.C., a Delaware limited liability company (Maker), and Lehman Brothers Realty Corporation, a Delaware corporation (Exhibit B to Exhibit 10.14 above). |
| 10.16* | Tenant Estoppel Certificate (Exhibit C. to Exhibit 10.14 above). |
| 10.17* | Subordination, Non-Disturbance and Attornment Agreement (Exhibit D. to Exhibit 10.14 above). |
| 10.18* | Deed of Trust, Assignment of Rents and Leases, Security Agreement, and Fixture Filing dated as of June 8, 1998 made by Arden Realty Finance IV, L.L.C. as Grantor, to Commonwealth Land Title Company as Trustee for the benefit of Lehman Brothers Realty Corporation as Beneficiary, filed as an exhibit to Arden Realty's quarterly report on Form 10-Q filed on August 14, 1998. |
| 10.19* | Assignment of Leases and Rents dated June 8, 1998, by and between Arden Realty Finance IV, L.L.C., a Delaware limited liability company (Assignor), and Lehman Brothers Realty Corporation, a Delaware corporation, its successors and assigns (Assignee), filed as an exhibit to Arden Realty's quarterly report on Form 10-Q filed on August 14, 1998. |
| 10.20* | Collateral Assignment of Management Agreement and Subordination Agreement dated as of June 8, 1998 among Arden Realty Finance IV, L.L.C., a Delaware limited liability company (Borrower), Lehman Brothers Realty Corporation, a Delaware corporation, (Lender), and Arden Realty Limited Partnership, filed as an exhibit to Arden Realty's quarterly report on Form 10-Q filed on August 14, 1998. |
| 10.21* | Security Agreement entered into as of June 8, 1998 by and between Arden Realty Finance IV, L.L.C., a Delaware limited liability company (Debtor), and Lehman Brothers Realty Corporation, a Delaware corporation (Secured Party), filed as an exhibit to Arden Realty's quarterly report on Form 10-Q filed on August 14, 1998. |
| 10.22* | Environmental Indemnity Agreement dated June 8, 1998 by Arden Realty Finance IV, L.L.C., a Delaware limited liability company (Indemnitor), in favor of Lehman Brothers Realty Corporation, a Delaware corporation (Lender), filed as an exhibit to Arden Realty's quarterly report on Form 10-Q filed on August 14, 1998. |
| 10.23* | Letter Agreement dated June 8, 1998 between Lehman Brothers Realty Corporation, Arden Realty Finance IV, L.L.C., Arden Realty and Arden Realty Limited Partnership, filed as an exhibit to Arden Realty's quarterly report on Form 10-Q filed on August 14, 1998. |
| 10.24*^ | Amended and Restated Employment Agreement dated January 1, 1999, between Arden Realty and Mr. Robert Peddicord, filed as an exhibit to Arden Realty's quarterly report on Form 10-Q filed on August 8, 2000. |
| 10.25* | Miscellaneous Rights Agreement among Arden Realty, Arden Realty Limited Partnership, NAMIZ, Inc. and Mr. Ziman, filed as an exhibit to Arden Realty's registration statement on Form S- 11 (No. 333-08163). |
| 10.26* | Credit Facility documentation consisting of Second Amended and Restated Revolving Credit Agreement by and among Arden Realty Limited Partnership and a group of banks led by Wells Fargo Bank as filed as an exhibit to Arden Realty's quarterly report on Form 10-Q filed on May 12, 2000. |

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| Exhibit Number | Description |
|-------------------|---|
| 10.27* | Mortgage Financing documentation consisting of Loan Agreement by and between Arden Realty's special purpose financing subsidiary and Lehman Brothers Realty Corporation (the Loan Agreement includes the Mortgage Note, Deed of Trust, and form of Tenant Estoppel Certificate and Agreement as exhibits) as filed as an exhibit to Arden Realty's registration statement on Form S-11 (No. 333-30059). |
| 10.28* | Promissory Note, dated as of March 30, 1999, between Massachusetts Mutual Life Insurance Company and Arden Realty Finance V, L.L.C. filed as an exhibit to Arden Realty's current report on Form 8-K filed on April 20, 1999. |
| 10.29* | Deed of Trust and Security Agreement, dated as of March 30, 1999, with Arden Realty Finance V, L.L.C. as the Trustor and Massachusetts Mutual Life Insurance Company as the Beneficiary filed as an exhibit to Arden Realty's current report on Form 8-K filed on April 20, 1999. |
| 10.30* | Assignment of Leases and Rents, dated as of March 30, 1999, between Massachusetts Mutual Life Insurance Company and Arden Realty Finance V, L.L.C. filed as an exhibit to Arden Realty's current report on Form 8-K filed on April 20, 1999. |
| 10.31* | Subordination of Management Agreement, dated as of March 30, 1999, between Massachusetts Mutual Life Insurance Company and Arden Realty Finance V, L.L.C. filed as an exhibit to Arden Realty's current report on Form 8-K filed on April 20, 1999. |
| 10.32* | Environmental Indemnification and Hold Harmless Agreement, dated as of March 30, 1999, between Massachusetts Mutual Life Insurance Company and Arden Realty Finance V, L.L.C. filed as an exhibit to Arden Realty's current report on Form 8-K filed on April 20, 1999. |
| 10.33*^ | Amended and Restated Employment Agreement dated May 27, 1999, between Arden Realty and Mr. Randy J. Noblitt as filed as an exhibit to Arden Realty Limited Partnership's registration statement on Form S-4 (No. 333-53376). |
| 10.34*^ | Amended and Restated Employment Agreement dated July 27, 2000, by and between Arden Realty and Mr. Richard S. Ziman as filed as an exhibit to Arden Realty Limited Partnership's registration statement on Form S-4 (No. 333-53376). |
| 10.35*^ | Amended and Restated Employment Agreement dated July 27, 2000, by and between Arden Realty and Mr. Victor J. Coleman as filed as an exhibit to Arden Realty Limited Partnership's registration statement on Form S-4 (No. 333-53376). |
| 10.36*^ | Amendment to the 1996 Stock Option and Incentive Plan of Arden Realty, Inc. and Arden Realty Limited Partnership as filed as an exhibit to Arden Realty's Schedule 14A filed on April 25, 2000. |
| 10.37*^ | Second Amended and Restated 1996 Stock Option and Incentive Plan of Arden Realty, Inc. and Arden Realty Limited Partnership dated September 20, 2001 as filed as an exhibit to Arden Realty, Inc.'s quarterly report on Form 10-Q filed on November 14, 2001. |
| 10.38*^ | Form of Promissory Note entered on July 19, 2001 and September 28, 2001 between Arden Realty Limited Partnership and Andrew Sobel and Robert Peddicord, respectively, as filed as an exhibit to Arden Realty Limited Partnership's quarterly report on Form 10-Q filed on November 14, 2001. |
| 10.39*^ | Amended and Restated Employment Agreement dated June 2, 1999, between Arden Realty and Mr. Richard Davis as filed on an exhibit to Arden Realty Limited Partnership's annual report on Form 10-K filed on April 1, 2002. |
| 10.40*^ | Amended and Restated Employment Agreement dated March 29, 2002, between Mr. Andrew Sobel and Arden Realty, Inc. as filed as an exhibit to Arden Realty, Inc.'s quarterly report on Form 10-Q filed on August 14, 2002. |
| 10.41*^ | Form of Promissory Note entered into on February 18, 2002 between Arden Realty, Inc. and Mr. Andrew Sobel as filed as on exhibit to Arden Realty, Inc.'s quarterly report on Form 10-Q filed on August 14, 2002. |
| 10.42* | Term Loan Agreement between Arden Realty Limited Partnership and Wells Fargo Bank, National Association dated as of June 12, 2002 as filed as an exhibit to Arden Realty Limited Partnership's quarterly report on Form 10-Q filed on August 14, 2002. |

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| Exhibit Number | Description |
|-------------------|---|
| 10.43* | Third Amended and Restated Revolving Credit Agreement between Arden Realty Limited Partnership and a group of lenders led by Wells Fargo Bank dated as of August 9, 2002 as filed as an exhibit to Arden Realty Limited Partnership's quarterly report on Form 10-Q filed on November 12, 2002. |
| 10.44* | Amendment to Term Loan Agreement between Arden Realty Limited Partnership and Wells Fargo Bank, National Association dated as of September 19, 2002 as filed as an exhibit to Arden Realty Limited Partnership's quarterly report on Form 10-Q filed on November 12, 2002. |
| 10.45*^ | Amended and Restated Employment Agreement dated May 27, 1999, by and between Arden Realty Limited Partnership and Mr. David Swartz as filed as an exhibit to Arden Realty Limited Partnership's annual report on Form 10-K filed on March 27, 2003. |
| 10.46* | Second Amended and Restated Agreement of Limited Partnership of Arden Realty Limited Partnership, dated September 7, 1999, filed as an exhibit to Arden Realty's quarterly report on Form 10-Q filed with the Commission on November 15, 1999. |
| 10.47* | Admission of New Partners and Amendment to Limited Partnership Agreement entered into as of the 20th day of December, 2000, by and between Arden Realty Limited Partnership and the persons identified as the New Partners therein, filed as an exhibit to Arden Realty Limited Partnership's annual report on Form 10-K filed with the Commission on March 30, 2001. |
| 10.48* | Second Amendment to Limited Partnership Agreement entered into as of September 13, 2003, by Arden Realty Limited Partnership, filed as an exhibit to Arden Realty Limited Partnership's quarterly report on Form 10-Q filed with the Commission on November 13, 2003. |
| 10.49 | Confidential Resignation Agreement and General Release dated as of March 4, 2005 by and between Arden Realty, Inc. and Arden Realty Limited Partnership and Andrew J. Sobel. |
| 12.1 | Statement regarding computation of ratios. |
| 21.1* | Subsidiaries of Arden Realty Limited Partnership as filed as an exhibit to Arden Realty Limited Partnership's annual report on Form 10-K filed on March 27, 2003 are incorporated here by reference and in addition, Arden Realty Limited Partnership is included herein as a subsidiary of Arden Realty, Inc. |
| 23.1 | Consent of independent auditors. |
| 31.1 | Certification of Chief Executive Officer, pursuant to Rule 13a-14 promulgated under the Exchange Act, as created by Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of Chief Financial Officer, pursuant to Rule 13a-14 promulgated under the Exchange Act, as created by Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1 | Certification of Chief Executive Officer, pursuant to 18 U.S.C. Section 1350, as created by Section 906 of the Sarbanes-Oxley Act of 2002. |
| 32.2 | Certification of Chief Financial Officer, pursuant to 18 U.S.C. Section 1350, as created by Section 906 of the Sarbanes-Oxley Act of 2002. |

(*) Incorporated by reference.

(^) Management contract or compensatory plan or arrangement required to be identified by Item 15(a)3.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders

Arden Realty, Inc.

We have audited the accompanying consolidated balance sheets of Arden Realty, Inc. as of December 31, 2004 and 2003 and the related consolidated statements of income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2004. These financial statements are the responsibility of the management of Arden Realty, Inc. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Arden Realty, Inc. at December 31, 2004 and 2003 and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2004, in conformity with U.S. generally accepted accounting principles.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Arden Realty, Inc.'s internal control over financial reporting as of December 31, 2004, based on the criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our reporting dated March 10, 2005 expressed an unqualified opinion thereon.

/s/ ERNST & YOUNG LLP

Los Angeles, California
March 10, 2005

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Table of Contents**ARDEN REALTY, INC.****CONSOLIDATED BALANCE SHEETS**

(in thousands, except share data)

| | December 31, | |
|--|--------------------|--------------------|
| | 2004 | 2003 |
| Assets | | |
| Investment in real estate: | | |
| Land | \$ 450,439 | \$ 438,342 |
| Buildings and improvements | 2,175,571 | 2,029,276 |
| Tenant improvements and leasing commissions | 360,401 | 329,285 |
| | <u>2,986,411</u> | <u>2,796,903</u> |
| Less: accumulated depreciation and amortization | (488,808) | (432,814) |
| | <u>2,497,603</u> | <u>2,364,089</u> |
| Properties under development or renovation | 16,295 | 75,627 |
| Land available for development | 23,795 | 23,723 |
| Properties held for disposition, net | 14,288 | 183,260 |
| | <u>2,551,981</u> | <u>2,646,699</u> |
| Net investment in real estate | 2,551,981 | 2,646,699 |
| Cash and cash equivalents | 13,040 | 4,707 |
| Restricted cash | 14,788 | 19,694 |
| Rent and other receivables, net of allowance of \$3,748 and \$4,041 at December 31, 2004 and 2003, respectively | 5,953 | 3,688 |
| Deferred rent, net of allowance of \$1,933 and \$2,216 at December 31, 2004 and 2003, respectively | 42,886 | 44,203 |
| Prepaid financing costs, expenses and other assets, net of accumulated amortization of \$13,244 and \$13,781 at December 31, 2004 and 2003, respectively | 31,349 | 22,442 |
| | <u>2,659,997</u> | <u>2,741,433</u> |
| Total assets | <u>\$2,659,997</u> | <u>\$2,741,433</u> |
| Liabilities | | |
| Mortgage loans payable | \$ 375,417 | \$ 557,435 |
| Mortgage loan payable - property held for disposition | 7,222 | 7,394 |
| Unsecured lines of credit | 121,500 | 161,000 |
| Unsecured term loan | 125,000 | 125,000 |
| Unsecured senior notes, net of discount | 696,945 | 498,952 |
| Accounts payable and accrued expenses | 58,215 | 54,317 |
| Security deposits | 25,498 | 22,321 |
| Dividends payable | 33,494 | 32,535 |
| | <u>1,443,291</u> | <u>1,458,954</u> |
| Total liabilities | 1,443,291 | 1,458,954 |
| Minority interest | 20,414 | 72,194 |
| Stockholders' Equity | | |
| Preferred stock, \$.01 par value 20,000,000 shares authorized, none issued | | |
| Common stock, \$.01 par value, 100,000,000 shares authorized, 66,325,709 and 64,425,450 issued and outstanding at December 31, 2004 and 2003, respectively | 664 | 646 |
| Additional paid-in capital | 1,212,508 | 1,225,192 |

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| | | |
|---|-------------------|-------------------|
| Deferred compensation | (12,830) | (14,952) |
| Accumulated other comprehensive loss | (4,050) | (601) |
| | <u> </u> | <u> </u> |
| Total stockholders equity | 1,196,292 | 1,210,285 |
| | <u> </u> | <u> </u> |
| Total liabilities and stockholders equity | \$2,659,997 | \$2,741,433 |
| | <u> </u> | <u> </u> |

See accompanying notes to financial statements.

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Table of Contents**ARDEN REALTY, INC.****CONSOLIDATED STATEMENTS OF INCOME****(in thousands, except per share amounts)**

| | Year Ended December 31, | | |
|--|--------------------------------|----------------|----------------|
| | 2004 | 2003 | 2002 |
| Property revenues | \$ 409,193 | \$ 393,765 | \$ 374,135 |
| Property operating expenses | (133,635) | (125,979) | (117,019) |
| | <u>275,558</u> | <u>267,786</u> | <u>257,116</u> |
| General and administrative expenses | 19,503 | 16,931 | 12,581 |
| Interest expense | 88,856 | 93,093 | 87,827 |
| Depreciation and amortization | 121,687 | 111,952 | 100,317 |
| Interest income and other loss (income) | 508 | 401 | (2,063) |
| | <u>45,004</u> | <u>45,409</u> | <u>58,454</u> |
| Income from continuing operations before gain on sale of properties and impairment on investment in securities and minority interest | 45,004 | 45,409 | 58,454 |
| Gain on sale of operating properties | | | 1,967 |
| | <u>45,004</u> | <u>45,409</u> | <u>60,421</u> |
| Income from continuing operations before impairment on investment in securities and minority interest | 45,004 | 45,409 | 60,421 |
| Impairment on investment in securities | (2,700) | | |
| Minority interest | (5,255) | (5,375) | (5,816) |
| | <u>37,049</u> | <u>40,034</u> | <u>54,605</u> |
| Income from continuing operations | 37,049 | 40,034 | 54,605 |
| Discontinued operations, net of minority interest | 6,253 | 12,538 | 15,570 |
| Gain on sale of discontinued properties | 30,473 | 5,937 | |
| | <u>73,775</u> | <u>58,509</u> | <u>70,175</u> |
| Net income | \$ 73,775 | \$ 58,509 | \$ 70,175 |
| Basic net income per common share: | | | |
| Income from continuing operations | \$ 0.57 | \$ 0.63 | \$ 0.85 |
| Income from discontinued operations | 0.56 | 0.29 | 0.24 |
| | <u>1.13</u> | <u>0.92</u> | <u>1.09</u> |
| Net income per common share basic | \$ 1.13 | \$ 0.92 | \$ 1.09 |
| Weighted average number of common shares basic | <u>65,372</u> | <u>63,553</u> | <u>64,151</u> |
| Diluted net income per common share: | | | |
| Income from continuing operations | \$ 0.56 | \$ 0.63 | \$ 0.85 |
| Income from discontinued operations | 0.56 | 0.29 | 0.24 |
| | <u>1.12</u> | <u>0.92</u> | <u>1.09</u> |
| Net income per common share diluted | \$ 1.12 | \$ 0.92 | \$ 1.09 |
| Weighted average number of common shares diluted | <u>65,740</u> | <u>63,815</u> | <u>64,351</u> |

See accompanying notes to financial statements.

Table of Contents**ARDEN REALTY, INC.****CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY**

(in thousands, except share amounts)

| | Common Stock | | Additional Paid in Capital | Retained Earnings | Deferred Compensation | Accumulated Other Comprehensive Loss | Total Stockholders Equity |
|---|--------------|--------|----------------------------------|----------------------|--------------------------|---|---------------------------------|
| | Shares | Amount | | | | | |
| Balance at January 1, 2002 | 64,098,110 | \$ 641 | \$ 1,345,698 | \$ | \$ (9,133) | \$ | \$ 1,337,206 |
| OP units converted | 121,875 | 2 | 2,488 | | | | 2,490 |
| Stock options exercised | 423,999 | 4 | 9,074 | | | | 9,078 |
| Stock compensation | 187,500 | 2 | 4,813 | | (4,815) | | |
| Amortization of stock compensation | | | | | 1,444 | | 1,444 |
| Forfeiture of stock compensation | (51,267) | | (1,245) | | 1,245 | | |
| Stock repurchases | (1,796,000) | (18) | (40,675) | | | | (40,693) |
| Unrealized loss on interest rate hedges | | | | | | (2,995) | (2,995) |
| Reclassification adjustment for losses included in earnings | | | | | | 227 | 227 |
| Net income | | | | 70,175 | | | 70,175 |
| Comprehensive income | | | | | | | 67,407 |
| Dividends declared and payable | | | (59,380) | (70,175) | | | (129,555) |
| Balance at December 31, 2002 | 62,984,217 | \$ 631 | \$ 1,260,773 | \$ | \$ (11,259) | \$ (2,768) | \$ 1,247,377 |
| OP units converted | 29,076 | | 495 | | | | 495 |
| Stock options exercised | 1,162,523 | 12 | 27,934 | | | | 27,946 |
| Stock option expense | | | 41 | | | | 41 |
| Stock compensation | 252,500 | 3 | 6,276 | | (6,279) | | |
| Amortization of stock compensation | | | | | 2,545 | | 2,545 |
| Forfeiture of stock compensation | (2,866) | | (41) | | 41 | | |
| Unrealized loss on interest rate hedges | | | | | | (155) | (155) |
| Reclassification adjustment for losses included in earnings | | | | | | 2,322 | 2,322 |
| Net income | | | | 58,509 | | | 58,509 |
| Comprehensive income | | | | | | | 60,676 |
| Dividends declared and payable | | | (70,286) | (58,509) | | | (128,795) |
| Balance at December 31, 2003 | 64,425,450 | \$ 646 | \$ 1,225,192 | \$ | \$ (14,952) | \$ (601) | \$ 1,210,285 |
| OP units converted | 16,000 | | 285 | | | | 285 |
| Stock options exercised | 1,750,592 | 18 | 42,727 | | | | 42,745 |
| Stock option expense | | | 44 | | | | 44 |
| Stock compensation | 136,500 | | 1,596 | | (1,596) | | |
| Amortization of stock compensation | | | 665 | | 3,641 | | 4,306 |
| Forfeiture of stock compensation | (2,833) | | (77) | | 77 | | |
| Write-off of preferred OP units original issuance costs | | | 1,075 | | | | 1,075 |

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| | | | | | | | |
|---|------------|-------|-------------|----------|------------|-----------|-------------|
| Unrealized loss on interest rate hedges | | | | | (4,315) | (4,315) | |
| Reclassification adjustment for losses included in earnings | | | | | 866 | 866 | |
| Net income | | | 73,775 | | | 73,775 | |
| Comprehensive income | | | | | | 70,326 | |
| Dividends declared and payable | | | (58,999) | (73,775) | | (132,774) | |
| Balance at December 31, 2004 | 66,325,709 | \$664 | \$1,212,508 | \$ | \$(12,830) | \$(4,050) | \$1,196,292 |

See accompanying notes to financial statements.

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ARDEN REALTY, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

| | Year Ended December 31, | | |
|---|-------------------------|-----------|-----------|
| | 2004 | 2003 | 2002 |
| Operating Activities: | | | |
| Net income | \$ 73,775 | \$ 58,509 | \$ 70,175 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Minority interest, including discontinued operations | 6,202 | 5,873 | 6,236 |
| Depreciation and amortization, including discontinued operations | 126,582 | 120,316 | 111,418 |
| Amortization of loan costs and fees | 3,801 | 3,972 | 3,807 |
| Gain on sale of property | (30,473) | (5,937) | (1,967) |
| Gain on repayment of mortgage loan receivable | | | (750) |
| Impairment on investment in securities | 2,700 | | |
| Amortization of deferred compensation | 3,760 | 2,251 | 1,199 |
| Changes in operating assets and liabilities: | | | |
| Rent and other receivables | (2,265) | (771) | 6,768 |
| Deferred rent | (1,015) | (557) | (4,657) |
| Prepaid financing costs, expenses and other assets | (4,783) | (1,494) | (2,997) |
| Accounts payable and accrued expenses | 3,338 | (2,356) | 9,728 |
| Security deposits | 3,285 | 1,676 | 962 |
| Net cash provided by operating activities | 184,907 | 181,482 | 199,922 |
| Investing Activities: | | | |
| Acquisitions and improvements to commercial properties | (198,309) | (111,365) | (251,534) |
| Proceeds from sales of properties | 187,072 | 91,010 | 24,287 |
| Proceeds from repayment of mortgage note receivable | | | 14,245 |
| Net cash used in investing activities | (11,237) | (20,355) | (213,002) |
| Financing Activities: | | | |
| Proceeds from term loan | | | 125,000 |
| Repayments of mortgage loans | (182,190) | (5,825) | (2,798) |
| Proceeds from unsecured lines of credit | 465,500 | 102,500 | 255,937 |
| Repayments of unsecured lines of credit | (505,000) | (150,086) | (227,700) |
| Proceeds from issuances of unsecured senior notes, net of discount | 197,033 | | |
| Decrease (increase) in restricted cash | 5,012 | 804 | (1,730) |
| Proceeds from issuance of common stock, net of offering costs | 42,745 | 27,946 | 9,078 |
| Repurchase of common stock | | | (40,693) |
| Distributions to minority interests | (3,388) | (3,443) | (3,527) |
| Distributions to preferred operating partnership unit holders | (3,234) | (4,312) | (4,312) |
| Redemption of preferred operating partnership units | (50,000) | | |
| Dividends paid | (131,815) | (128,067) | (129,153) |
| Net cash used in financing activities | (165,337) | (160,483) | (19,898) |

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| | | | |
|---|-------------------|-------------------|-------------------|
| Net increase (decrease) in cash and cash equivalents | 8,333 | 644 | (32,978) |
| Cash and cash equivalents at beginning of period | 4,707 | 4,063 | 37,041 |
| | <u> </u> | <u> </u> | <u> </u> |
| Cash and cash equivalents at end of period | \$ 13,040 | \$ 4,707 | \$ 4,063 |
| | <u> </u> | <u> </u> | <u> </u> |
| Supplemental Disclosure of Cash Flow Information: | | | |
| Cash paid during the period for interest, net of amount capitalized | \$ 87,572 | \$ 96,547 | \$ 94,007 |
| | <u> </u> | <u> </u> | <u> </u> |

See accompanying notes to financial statements.

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ARDEN REALTY, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Business

Description of Business

The terms Arden Realty, us, we and our as used in these financial statements refer to Arden Realty, Inc. Through our controlling interest in Arden Realty Limited Partnership, or the Operating Partnership, and our other subsidiaries, we own, manage, lease, develop, renovate and acquire commercial office properties located in Southern California. As of December 31, 2004, our portfolio was comprised of 120 primarily suburban office properties and 197 buildings containing approximately 18.2 million net rentable square feet. As of December 31, 2004, our operating portfolio was 91.2% occupied.

The minority interests at December 31, 2004 consist of limited partnership interests in the Operating Partnership of approximately 2.5%.

Organization and Formation of the Company

We were incorporated in Maryland in May 1996 and are the sole general partner of Arden Realty Limited Partnership, or the Operating Partnership. We conduct substantially all of our business through the Operating Partnership and certain other owned subsidiaries, which hold our interests in our real estate assets. Commencing with our taxable year ended December 31, 1996, we have operated and qualified as a real estate investment trust (REIT) for federal income tax purposes.

2. Basis of Presentation and Summary of Significant Accounting Policies

Basis of Presentation

The accompanying consolidated financial statements include the accounts of Arden Realty, Inc., the Operating Partnership, and our subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

We consolidate all entities for which we have controlling financial interest as measured by a majority of the voting interest. For entities in which the controlling financial interest is not clearly indicated by ownership of a majority of the voting interest, we would consolidate those entities for which we own a majority of the financial interest in profits or losses or entities that we control by agreement. We also consolidate all variable interest entities for which we are the primary beneficiary.

Arden Realty and the Operating Partnership currently own 100% of all of our consolidated subsidiaries and do not have any unconsolidated investments.

Risks and Uncertainties

The preparation of financial statements, in conformity with accounting principles generally accepted in the United States, requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Our properties are all located in Southern California. As a result of our geographic concentration, the operations of these properties could be affected by the economic conditions in this region.

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Segment Information

We view our operations as principally one segment, the operation of commercial real estate located in Southern California, and the financial information disclosed herein represents all of the financial information related to this principal operating segment.

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Commercial Properties

Our properties are stated at depreciated cost. Write-downs to estimated fair value are recognized whenever a property's estimated undiscounted future cash flows are less than its book value. We carry properties held for disposition at the lower of their depreciated cost or fair value less cost to sell. Based on our assessment, no write-downs to estimated fair value were necessary as of December 31, 2004 and 2003.

Property acquisitions are accounted for in accordance with Statement of Financial Accounting Standards (SFAS) No. 141, Business Combinations. The fair value of the real estate acquired is allocated to the acquired tangible assets, consisting of land, building and tenant improvements, and identified intangible assets and liabilities, consisting of the value of above-market and below-market leases, other value of in-place leases and value of tenant relationships, if any, based in each case on their fair values.

The fair value of the tangible assets of an acquired property (which includes land, building and tenant improvements) is determined by valuing the property as if it were vacant, and the as-if-vacant value is then allocated to land, building and tenant improvements based on management's determination of the relative fair values of these assets. We determine the as-if-vacant fair value of a property using methods similar to those used by independent appraisers. Factors considered by management in performing these analyses include an estimate of carrying costs during the expected lease-up periods considering current market conditions and costs to execute similar leases. In estimating carrying costs, management includes estimates of lost rental revenue, real estate taxes, insurance and other operating expenses during the expected lease-up periods based on current market demand. We also estimate costs to execute similar leases including leasing commissions, concessions, legal and other related costs.

In allocating the fair value of the identified intangible assets and liabilities of an acquired property, above-market and below-market in-place lease values are recorded based on the present value (using an interest rate which reflects the risks associated with the leases acquired) of the difference between (i) the contractual amounts to be paid pursuant to the in-place leases and (ii) management's estimate of fair market lease rates for the corresponding in-place leases, measured over a period equal to the remaining non-cancelable term of the lease. The capitalized above-market and below-market lease values are amortized into rental income over the remaining non-cancelable terms of the respective leases.

The aggregate value of other acquired intangible assets, consisting of in-place leases and tenant relationships, if any, is measured by the excess of (i) the purchase price paid for a property after adjusting existing in-place leases to market rental rates over (ii) the estimated fair value of the property as if vacant, determined as set forth above. This aggregate value is allocated between in-place lease values and tenant relationships based on management's evaluation of the specific characteristics of each tenant's lease. Should acquisitions of properties result in allocating material amounts to the value of tenant relationships, an amount would be separately allocated and amortized over the estimated life of the relationship.

Costs related to the acquisition, development, construction and improvement of properties are capitalized. Interest, real estate taxes, insurance and other development related costs incurred during construction periods are capitalized and depreciated on the same basis as the related asset.

Repair and maintenance costs are charged to expenses as incurred and significant replacements and betterments are capitalized. Repairs and maintenance costs include all costs that do not extend the useful life of an asset or increase its operating efficiency. Significant replacements and betterments represent costs that extend an asset's useful life or increase its operating efficiency.

Depreciation

Depreciation is calculated under the straight-line method using depreciable lives of ten to forty seven years for building and building improvements and five-year lives for furniture, fixtures and equipment. Amortization of tenant improvements is calculated using the straight-line method over the term of the related lease.

Costs associated with leasing properties are capitalized and amortized to expense on a straight-line basis over the related lease term.

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Cash Equivalents

Cash equivalents consist of highly liquid investments with original maturities of three months or less when acquired.

Restricted Cash

Restricted cash at December 31, 2004 and 2003 consisted of \$9.7 million and \$13.7 million, respectively, in cash deposits as required by certain of our mortgage loans payable and \$5.1 million and \$6.0 million, respectively, in impound accounts for real estate taxes and insurance, as required by certain of our mortgage loans payable.

Prepaid Financing Costs

Costs associated with obtaining long-term financing are capitalized and amortized to interest expense over the term of the related loan.

Revenue Recognition

Minimum rent, including rental abatements and contractual fixed increases attributable to operating leases, is recognized on a straight-line basis over the term of the related lease. Amounts expected to be received in later years are included in deferred rents. Property operating expense reimbursements due from tenants for common area maintenance, real estate taxes and other recoverable costs are recognized in the period the related expenses are incurred.

The Company recognizes gains on sales of real estate pursuant to the provisions of SFAS No. 66 Accounting for Sales for Real Estate. The specific timing of a sale is measured against various criteria in SFAS No. 66 related to the terms of the transaction and any continuing involvement in the form of management or financial assistance associated with the property. If the sales criteria are not met, the Company defers gain recognition and accounts for the continued operations of the property by applying the finance, installment or cost recovery methods, as appropriate, until the sales criteria are met.

Allowance for Rents and Other Receivables

We periodically evaluate the collectibility of amounts due from tenants and maintain an allowance for doubtful accounts for estimated losses resulting from the inability of tenants to make required payments under lease agreements. We also maintain an allowance for deferred rent receivable that arises from the straight-lining of rents. We exercise judgment in establishing these allowances and consider payment history and current credit status in developing these estimates.

Income Taxes

We generally will not be subject to federal income taxes as long as we continue to qualify as a REIT. A REIT will generally not be subject to federal income taxation on that portion of income that qualifies as REIT taxable income and to the extent that it distributes such taxable income to its stockholders and complies with certain requirements. As a REIT, we are allowed to reduce taxable income by all or a portion of distributions to stockholders and must distribute at least 90% of our taxable income to qualify as a REIT. As dividends have eliminated taxable income, and compliance with certain requirements have been met, no Federal income tax provision has been reflected in the accompanying consolidated financial statements. State income tax requirements are essentially the equivalent of the Federal rules.

During 2004, 2003 and 2002, we declared annual dividends of \$2.02 per share.

Fair Value of Financial Instruments

Our disclosures of estimated fair value of financial instruments at December 31, 2004 and 2003 were determined using available market information and appropriate valuation methods. Considerable judgment is necessary to interpret market data and develop estimated fair value. The use of different market assumptions or estimation methods may have a material effect on the estimated fair value amounts.

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Our cash equivalents, mortgage notes receivable, unsecured lines of credit, interest rate hedge agreements, accounts payable and other financial instruments are carried at amounts that reasonably approximate their fair value amounts.

The estimated fair value of our mortgage loans payable and unsecured senior notes is as follows (in thousands):

| | December 31, 2004 | | December 31, 2003 | |
|------------------------|-------------------|----------------------|-------------------|----------------------|
| | Carrying Amount | Estimated Fair Value | Carrying Amount | Estimated Fair Value |
| Mortgage loans payable | \$382,639 | \$389,755 | \$564,829 | \$581,945 |
| Unsecured senior notes | \$696,945 | \$712,137 | \$498,952 | \$540,904 |

The estimated fair value is based on interest rates available at each of the dates presented for issuance of debt with similar terms and remaining maturities. The estimated fair value amounts of our notes payable above are not necessarily indicative of the amounts that we could realize in a current market exchange.

Interest Rate Hedge Agreements

We have periodically entered into interest rate hedge agreements to effectively convert floating rate debt into fixed rate debt or to remove the variability associated with forecasted issuances of fixed rate debt. Net amounts received or paid under these agreements are recognized as an adjustment to interest expense when such amounts are incurred or earned. Our objective in using interest rate hedge agreements is to manage our exposure to interest rate movements.

During 2002, such agreements were used to fix the floating interest rate associated with \$50 million of the Wells Fargo unsecured line of credit and the entire \$125 million balance of the unsecured term loan. In August 2004, we settled \$150 million of forward-starting swaps we entered into in 2003 in conjunction with a forecasted \$200 million issuance of unsecured senior notes. We expensed approximately \$130,000 of ineffectiveness relating to this settlement during 2004.

In 2003, we also entered into reverse interest rate hedge agreements to float \$100 million of the fixed interest rate associated with the 7.00% senior unsecured notes due in November of 2007. Under these reverse hedges, we will receive interest at a fixed rate of 7.00% and pay interest at a variable rate averaging the six-month LIBOR in arrears plus 3.10%. The interest rate hedges mature at the same time the notes are due. These hedges qualify as fair value hedges for accounting purposes. Net semi-annual interest payments will be recognized as increases or decreases in interest expense. The fair value of the interest rate hedges will be recognized on our balance sheet and the carrying value of the senior unsecured notes will be increased or decreased by an offsetting amount.

In 2004, we entered into \$300 million of forward-starting swaps that effectively fixed the 10-year Treasury rate at an average rate of approximately 4.37% for borrowings that are expected to occur in 2005 to primarily refinance some of our scheduled debt maturities. The forward-starting interest rate swaps were entered into at current market rates and, therefore, had no initial cost.

Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities* (SFAS 133), as amended and interpreted, establishes accounting and reporting standards for derivative instruments and for hedging activities. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative and the resulting destination. Derivatives used to hedge the exposure to changes in the fair value of an asset, liability, or firm commitment attributable to a particular risk, are considered fair value hedges. Derivatives used to hedge the exposure to variability in expected future cash flows, or other types of forecasted transactions, are considered cash flow hedges.

For derivatives designated as fair value hedges, changes in the fair value of the derivative and the hedged item related to the hedged risk are recognized in earnings. For derivatives designated as cash flow hedges, the effective portion of changes in the fair value of the derivative is initially reported in other comprehensive income (loss), outside of earnings and subsequently reclassified to earnings when the hedged

transaction affects earnings.

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Under SFAS 133, our \$175 million in floating-to-fixed hedges and our \$300 million in forward-starting hedges outstanding as of December 31, 2004 are classified as cash flow hedges. The fair value of these instruments of (\$3.7) million at December 31, 2004 has been deferred in accumulated other comprehensive loss on our balance sheet. Of the amount deferred in other comprehensive loss at December 31, 2004, we estimate that approximately \$4.8 million will be reclassified out of other comprehensive loss as an increase to interest expense during 2005. The estimated fair value of these interest rate hedge agreements are dependent on changes in market interest rates and other market factors that affect the value of such agreements. Consequently, the estimated current fair value may significantly change during the term of the agreements. Any estimated gain or loss from these agreements will be amortized into earnings as we recognize the interest expense for the underlying floating-rate loans at the fixed interest rate provided under our agreements in the case of the fixed-to-floating hedges or as part of interest expense for future borrowings in the case of the forward-starting hedges. If the underlying debt related to these hedges were to be repaid prior to maturity, we would recognize into interest expense any unamortized gain or loss at the time of such early repayment.

Under SFAS 133, our \$100 million in fixed-to-floating hedges are classified as fair value hedges with their fair value of approximately \$162,000 reported in both the unsecured senior notes and accounts payable and accrued expenses line items on our balance sheet. The estimated fair value of these interest rate hedge agreements are dependent on changes in market interest rates and other market factors that affect the value of such agreements. Consequently, the estimated current fair value may significantly change during the term of the agreements. During the years ended December 31, 2004 and 2003, we recognized approximately \$1.6 million and \$400,000, respectively, as a reduction of interest expense related to our fair value hedges. If the underlying debt related to these hedges were to be repaid prior to maturity, we would recognize into interest expense any unamortized gain or loss at the time of such early repayment.

New Accounting Standards

In December 2004, the FASB issued SFAS No. 123R, which is a revision of SFAS No. 123. SFAS No. 123R supersedes APB Opinion No. 25, and its related implementation guidance. SFAS No. 123R requires companies to record compensation expense for share-based payments to employees, including grants of employee stock options, at fair value. SFAS No. 123R is effective for most public companies at the beginning of the first interim or annual period beginning after June 15, 2005. We believe that the implementation of the provisions of SFAS No. 123R will not have a material impact on our financial position or results of operations.

Reclassifications

Certain prior year amounts on our consolidated balance sheets and consolidated statements of income have been reclassified to confirm with the current year presentation for properties sold and classified as held for disposition pursuant to SFAS 144.

Table of Contents**3. Commercial Properties***Property Dispositions*

| Property | Major Area | Submarket | Date of Sale | Property Type | Square Feet | Sales Price (\$000 s) |
|--|-------------------|-----------------------|----------------------|----------------------|--------------------|------------------------------|
| Tower Plaza Retail Univision 5999 Center Drive | Riverside | Temecula | February 4, 2004 | Retail | 133,481 | \$ 17,050 |
| 10251 Vista Sorrento Waples Center | Los Angeles | Culver City/Fox Hills | March 16, 2004 | Office | 161,650 | 52,500 |
| | San Diego | Sorrento Mesa | August 24, 2004 | Office | 69,386 | 9,250 |
| | San Diego | Sorrento Mesa | December 29, 2004 | Office | 28,119 | (A) |
| Morehouse Center | San Diego | Sorrento Mesa | December 29, 2004 | Office | 181,207 | (A) |
| 91 Freeway Center | Los Angeles | Artesia | December 29, 2004 | Office | 93,277 | (A) |
| Norwalk | Los Angeles | Norwalk | December 29, 2004 | Office | 122,175 | (A) |
| 1501 Hughes Way | Los Angeles | Suburban Long Beach | December 29, 2004 | Office | 77,060 | (A) |
| 3901 Via Oro | Los Angeles | Suburban Long Beach | December 29, 2004 | Office | 53,195 | (A) |
| Glendale Corporate Center | Los Angeles | Glendale | December 29, 2004 | Office | 108,209 | (A) |
| Whittier | Los Angeles | Whittier | December 29, 2004 | Office | 135,415 | (A) |
| South Bay Tech | Los Angeles | 190th Corridor | December 29, 2004 | Office | 104,815 | (A) |
| Sub-total | | | | | 1,267,989 | 78,800 |
| | | | | | | 126,000(B) |
| | | | | | 1,267,989 | \$204,800 |

(A) Portfolio sale.

(B) Includes approximately \$12.5 million in proceeds held in escrow at the end of 2004 as part of a 1031 exchange transaction to be completed in 2005.

Property Acquisitions

| Property | County | Submarket | Date of Purchase | Property Type | Square Feet | Purchase Price (\$000 s) |
|-------------------------|---------------|------------------|-------------------------|----------------------|--------------------|---------------------------------|
| Homestore | Los Angeles | Westlake Village | October 4, 2004 | Office | 137,762 | \$32,300 |
| Warner Corporate Center | Los Angeles | Woodland Hills | October 11, 2004 | Office | 253,000 | 64,500 |
| | | | | | 390,762 | \$96,800 |

Discontinued Operations and Properties held for Disposition

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SFAS 144, effective January 1, 2002, requires, among other things, that the operating results of real estate properties classified as held for disposition subsequent to January 1, 2002 be included in discontinued operations in the statements of income for all periods presented. SFAS 144 provides that long-lived assets classified as held for disposition as a result of disposal activities that were initiated prior to January 1, 2002, are to be accounted for in accordance with Financial Accounting Standards No. 121 (SFAS 121). Accordingly, the operating results for the properties classified as held for disposition prior to January 1, 2002 and sold prior to December 31, 2002 are included in income from continuing operations for the year ended December 31, 2002. In order to increase the comparability of our consolidated statements of income for the years ended December 31, 2004, 2003 and 2002, the tables below summarize the operating results of one property classified as held for disposition at December 31, 2004, twelve properties sold during 2004 and eight properties sold during 2003.

As of December 31, 2004, properties held for disposition consisted of one property with approximately 167,000 square feet. See footnote 13.

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The results of operations for the properties classified as discontinued operations for the years ended December 31, 2004, 2003 and 2002 are as follows (in thousands):

| | For the Years Ended December 31, | | |
|---|----------------------------------|------------------|------------------|
| | 2004 | 2003 | 2002 |
| Revenues | \$ 20,533 | \$ 33,794 | \$ 41,978 |
| Property operating expenses | (7,781) | (11,711) | (14,199) |
| Depreciation and amortization | (4,895) | (8,372) | (11,100) |
| Interest expense | (659) | (674) | (689) |
| Interest and other income | 2 | | |
| Minority interest | (947) | (499) | (420) |
| Discontinued operations, net of minority interest | <u>\$ 6,253</u> | <u>\$ 12,538</u> | <u>\$ 15,570</u> |
| Gain on sale of discontinued properties | <u>\$ 30,473</u> | <u>\$ 5,937</u> | <u>\$</u> |

Capitalized Interest

We capitalize interest and taxes related to buildings under construction and renovation to the extent those assets qualify for capitalization.

Total interest incurred and the amount capitalized was as follows (in thousands):

| | For the Years Ended December 31, | | |
|----------------------------|----------------------------------|------------------|------------------|
| | 2004 | 2003 | 2002 |
| Total interest incurred(1) | \$ 90,451 | \$ 96,263 | \$ 94,162 |
| Amount capitalized | (936) | (2,496) | (5,646) |
| Amount expensed(1) | <u>\$ 89,515</u> | <u>\$ 93,767</u> | <u>\$ 88,516</u> |

(1) Includes interest expense related to a property currently classified as held for disposition.

Future Minimum Lease Payments

Future minimum lease payments to be received under noncancelable operating leases existing as of December 31, 2004, are as follows (in thousands):

| | |
|------------|---------------------|
| 2005 | \$ 349,967 |
| 2006 | 305,034 |
| 2007 | 254,490 |
| 2008 | 196,735 |
| 2009 | 144,404 |
| Thereafter | 274,098 |
| Total | <u>\$ 1,524,728</u> |

The above future minimum lease payments do not include payments received for tenant reimbursements of specified operating expenses.

We lease the land underlying the office buildings or parking structures at six of our buildings. Ground lease expense, including amounts netted against parking revenues, was approximately \$1.8 million, \$2.0 mil-

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lion and \$1.9 million for the years ended December 31, 2004, 2003 and 2002, respectively. Future minimum ground lease payments due under existing ground leases are as follows (in thousands):

| | |
|------------|------------|
| 2005 | \$ 1,815 |
| 2006 | 1,840 |
| 2007 | 1,865 |
| 2008 | 1,865 |
| 2009 | 1,865 |
| Thereafter | 109,056 |
| | <hr/> |
| Total | \$ 118,306 |
| | <hr/> |

4. Non-Real Estate Investments

During the year ended December 31, 2004, an impairment of \$2.7 million was recognized in connection with our investment in the securities of a non-publicly traded company that provides distributed energy generation to commercial property owners. This impairment represents our entire investment in this company.

We recorded this impairment after analyzing information received from this company regarding their current business and financial strategies which indicated to us that the recoverability of our investment was unlikely.

5. Mortgage Loans and Unsecured Indebtedness

A summary of mortgage loans payable, unsecured lines of credit and unsecured senior notes is as follows:

| Type of Debt | December 31, 2004 | December 31, 2003 | Stated Annual Interest Rate at December 31, 2004 | Fixed/Floating Rate | Number of Properties Securing Loan | Maturity Date |
|-----------------------------------|----------------------|----------------------|---|------------------------|---|---------------|
| (in thousands) | | | | | | |
| Mortgage Loans Payable: | | | | | | |
| <i>Fixed Rate</i> | | | | | | |
| Mortgage Financing I(1) | \$ | \$ 175,000 | | | | |
| Mortgage Financing III(2) | 132,323 | 134,544 | 6.74% | Fixed | 22 | 4/08 |
| Mortgage Financing IV(2) | 108,194 | 109,960 | 6.61% | Fixed | 12 | 4/08 |
| Mortgage Financing V(2) | 103,504 | 105,899 | 6.94% | Fixed | 12 | 4/09 |
| Mortgage Financing VI(2) | 21,325 | 21,578 | 7.54% | Fixed | 3 | 4/09 |
| Activity Business Center(2),(3) | 7,222 | 7,394 | 8.85% | Fixed | 1 | 5/06 |
| 145 South Fairfax(2) | 3,869 | 3,912 | 8.93% | Fixed | 1 | 1/27 |
| Marin Corporate Center(2) | 2,585 | 2,724 | 9.00% | Fixed | 1 | 7/15 |
| Conejo Business Center(2) | 2,531 | 2,669 | 8.75% | Fixed | (Note 4) | 7/15 |
| Conejo Business Center(2) | 1,086 | 1,149 | 7.88% | Fixed | (Note 4) | 7/15 |
| | <hr/> | <hr/> | | | | |
| | 382,639 | 564,829 | | | | |
| Unsecured Lines of Credit: | | | | | | |
| <i>Floating Rate</i> | | | | | | |
| Wells Fargo \$310 mm(5) | | | | LIBOR + 0.90% | | |
| | 111,500 | 158,000 | 3.57% | (Notes 6, 7) | | 4/06 |
| City National Bank \$20 mm(5) | 10,000 | 3,000 | 3.21% | LIBOR + 0.90% | | 8/05 |
| | <hr/> | <hr/> | | Note 8 | | |
| | 121,500 | 161,000 | | | | |
| Unsecured Term Loan: | | | | | | |
| <i>Fixed Rate</i> | | | | | | |

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Wells Fargo \$125 mm(5)

125,000

125,000

4.55%

Fixed (Note 9)

2/12(10)

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| Type of Debt | December 31, 2004 | December 31, 2003 | Stated Annual Interest Rate at December 31, 2004 | Fixed/Floating Rate | Number of Properties Securing Loan | Maturity Date |
|--------------------------------|----------------------|----------------------|---|------------------------|--|---------------|
| (in thousands) | | | | | | |
| Unsecured Senior Notes: | | | | | | |
| <i>Fixed Rate</i> | | | | | | |
| 2005 Notes(11),(12) | 199,974 | 199,872 | 8.88% | Fixed | | 3/05 |
| 2007 Notes(11) | 149,395 | 149,907 | 7.00% | (Note 13) | | 11/07 |
| 2010 Notes(11) | 49,785 | 49,744 | 9.15% | Fixed | | 3/10 |
| 2010 Notes(11) | 99,513 | 99,429 | 8.50% | Fixed | | 11/10 |
| 2011 Notes(11), (14) | 198,278 | | 5.20% | Fixed | | 9/11 |
| | 696,945 | 498,952 | | | | |
| Total Debt | \$ 1,326,084 | \$ 1,349,781 | | | | |

- (1) This mortgage financing was repaid in full on April 9, 2004.
- (2) Requires monthly payments of principal and interest.
- (3) This loan is secured by a property currently classified as held for disposition. This loan was repaid in January of 2005. See footnote 13.
- (4) Both mortgage loans are secured by the Conejo Business Center property.
- (5) Requires monthly payments of interest only, with outstanding principal balance due upon maturity.
- (6) This line of credit also has an annual 20 basis point facility fee on the entire \$310 million commitment amount. In June 2004, we amended this line of credit to reduce the interest rate from LIBOR + 1.00% to LIBOR + 0.90%.
- (7) We have entered into interest rate swap agreements to fix the interest rate on \$50 million of the outstanding balance on this line of credit at 3.95% through April of 2006.
- (8) On October 4, 2004, we amended this line of credit to reduce the interest rate from LIBOR + 1.00% or Prime Rate 1.875% to LIBOR + 0.90% or Prime Rate 1.975%.
- (9) In 2002, we entered into interest rate swap agreements that fixed the interest rate on the entire balance of this loan. In June 2004, we amended this loan to reduce its effective interest rate by 20 basis points. After this amendment and after taking into effect the interest rate swap agreements for this loan, it will have an effective interest rate of 4.55% in 2005 and 4.70% in 2006.
- (10) On February 18, 2005, we extended the maturity of this loan to February of 2012. See footnote 13.
- (11) Requires semi-annual interest payments only, with the principal balance due upon maturity.
- (12) These notes were redeemed in March of 2005. See footnote 13.
- (13) In 2003, we entered into interest rate swap agreements to float the interest rate on \$100 million of the outstanding balance of these notes at a rate of LIBOR + 3.1% through November of 2007. Including these swap agreements, the effective interest rate on these notes was approximately 6.53% as of December 31, 2004.
- (14) On August 18, 2004, we issued \$200 million of unsecured senior notes.

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Our Operating Partnership has an unsecured line of credit with a total commitment of \$20 million from City National Bank. This line of credit accrues interest at LIBOR + 0.90% or the City National Bank Prime Rate less 1.975% and is scheduled to mature on August 1, 2005. Proceeds from this line of credit are used, among other things, to provide funds for tenant improvements and capital expenditures and provide for working capital and other corporate purposes. As of December 31, 2004 and 2003, there was \$10.0 million and \$3.0 million outstanding on this line of credit, respectively, and \$10.0 and \$17.0 million was available for additional borrowings, respectively.

Our Operating Partnership also has an unsecured line of credit with a group of banks led by Wells Fargo. The line of credit provides for borrowings up to \$310 million with an option to increase the amount to \$350 million and bears interest at a rate ranging between LIBOR + 0.65% and LIBOR + 1.15% (including an annual facility fee ranging from 0.15% to 0.40% based on the aggregate amount of the line of credit) depending on the Operating Partnership's unsecured debt rating. This line of credit matures in April 2006. In addition, as long as the Operating Partnership maintains an unsecured debt rating of BBB-/ Baa3 or better, the agreement contains a competitive bid option, whereby the lenders may bid on the interest rate to be charged for up to \$150 million of the unsecured line of credit. The Operating Partnership also has the option to convert the interest rate on this line of credit to the higher of Wells Fargo's prime rate or the Federal Funds rate plus 0.5%. As of December 31, 2004 and 2003, \$111.5 million and \$158.0 million was outstanding on this line of

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credit, respectively, and \$198.5 million and \$152.0 million was available for additional borrowings, respectively.

Following is a summary of scheduled principal payments for our total debt outstanding as of December 31, 2004 (in thousands):

| Year | Amount |
|--------------|---------------------|
| 2005 | \$ 216,871(1) |
| 2006 | 251,101(2),(3) |
| 2007 | 158,035 |
| 2008 | 230,726 |
| 2009 | 112,291 |
| Thereafter | 357,060 |
| Total | \$ 1,326,084 |

(1) Includes \$200 million of unsecured senior notes redeemed in March of 2005. See footnote 13.

(2) Includes \$111.5 million outstanding on our Wells Fargo unsecured line of credit.

(3) Includes \$125 million outstanding on our Wells Fargo unsecured term loan. The maturity date of this loan was extended to February of 2012 subsequent to year-end. See footnote 13.

6. Stockholders Equity

A common Operating Partnership unit, or common OP Unit, and a share of our common stock have essentially the same economic characteristics as they share equally in the total net income or loss and distributions of the Operating Partnership. A common OP Unit may be redeemed for cash or, at the election of the Operating Partnership, for shares of our common stock on a one-for-one basis.

During the years ended December 31, 2004 and 2003, we redeemed an aggregate of 16,000 and 29,076 common OP Units, respectively, of the Operating Partnership for shares of our common stock.

During the years ended December 31, 2004 and 2003, we issued a total of 1,750,592 and 1,162,523 common shares, respectively, relating to exercises of stock options.

In September 2004, we redeemed the \$50 million of 5.625% Series B Cumulative Redeemable Preferred Operating Partnership Units at par plus accrued unpaid distributions. These Preferred OP Units were originally issued in September of 1999. In conjunction with this redemption, we expensed approximately \$1.1 million of original issuance costs.

During 2004, we issued a total of 136,500 restricted stock awards to several key executive officers, directors and employees. Holders of these shares have full voting rights and will receive any dividends but are prohibited from selling or transferring unvested shares. The fair market value on the dates of grants for these restricted shares ranged from \$29.30 to \$32.66. These restricted shares vest equally on the anniversary date of the awards over 3 years.

We recorded compensation expense of approximately \$600,000 during 2004 for the grants described above based upon the market value of these shares on the dates of the awards.

On December 10, 2004, we declared a quarterly dividend of \$0.505 per share to stockholders of record on December 31, 2004. This dividend was paid on January 19, 2005. We declared annual dividends of \$2.02 per common share for each of the years ended December 31, 2004 and 2003.

7. Commitments and Contingencies

Capital Commitments

As of December 31, 2004, we had approximately \$44.8 million outstanding in capital commitments related to tenant improvements, renovation costs, operating leases and general property-related capital expenditures.

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We are presently subject to various lawsuits, claims and proceedings of a nature considered normal to our ordinary course of business, none of which if determined unfavorably to us is expected to have a material adverse effect on our cash flows, financial condition or results from operations. There were no material changes in our legal procedures during the year ended December 31, 2004.

Concentration of Credit Risk

We maintain our cash and cash equivalents at financial institutions. The combined account balances at each institution periodically exceed FDIC insurance coverage, and as a result, there is a concentration of credit risk related to amounts on deposit in excess of FDIC insurance coverage. Management believes that the risk is not significant.

We generally do not require collateral or other security from our tenants, other than security deposits or letters of credit. As of December 31, 2004 and 2003, we had a total of approximately \$39.3 million and \$33.5 million, respectively, of total lease security available, including security deposits and existing letters of credit.

8. Related Party Transactions

At December 31, 2004 and 2003, we have four promissory notes totaling approximately \$486,000 relating to two of our officers. These notes originated during 2001 and 2002 and mature between July of 2006 and September of 2011. Two of these notes bear interest at fixed rates ranging from 5.75% to 6.00%. The remaining note bears interest at LIBOR + 1.10%. These notes are personally guaranteed by the respective officers and are included as part of other receivables in our balance sheets at December 31, 2004 and 2003.

We lease approximately 7,300 square feet of office space to two companies in which three of our officers have investment interests. The total annual rents from these leases is approximately \$175,000. We also lease approximately 34,000 square feet to a company related to one of our independent directors. The total annual rents from this lease is approximately \$497,000. The terms under these leases are comparable to those that would have been negotiated at inception with unaffiliated third parties.

9. Earnings Per Share

The following table sets forth the computation of basic and diluted net income per share for the years ended December 31, 2004, 2003 and 2002 (in thousands, except per share amounts):

| | 2004 | 2003 | 2002 |
|---|----------|----------|----------|
| Income from continuing operations | \$37,049 | \$40,034 | \$54,605 |
| Discontinued operations, net of minority interest | 6,253 | 12,538 | 15,570 |
| Gain on sale of discontinued properties | 30,473 | 5,937 | |
| | <hr/> | <hr/> | <hr/> |
| Net income | \$73,775 | \$58,509 | \$70,175 |
| | <hr/> | <hr/> | <hr/> |
| Weighted average shares basic | 65,372 | 63,553 | 64,151 |
| Weighted average diluted stock options | 368 | 262 | 200 |
| | <hr/> | <hr/> | <hr/> |
| Weighted average shares diluted | 65,740 | 63,815 | 64,351 |
| | <hr/> | <hr/> | <hr/> |
| Basic net income per common share: | | | |
| Income from continuing operations | \$ 0.57 | \$ 0.63 | \$ 0.85 |
| Income from discontinued operations | 0.56 | 0.29 | 0.24 |
| | <hr/> | <hr/> | <hr/> |

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| | | | |
|--------------------------------------|-------------------|-------------------|-------------------|
| Net income per common share basic | \$ 1.13 | \$ 0.92 | \$ 1.09 |
| | <u> </u> | <u> </u> | <u> </u> |
| Diluted net income per common share: | | | |
| Income from continuing operations | \$ 0.56 | \$ 0.63 | \$ 0.85 |
| Income from discontinued operations | 0.56 | 0.29 | 0.24 |
| | <u> </u> | <u> </u> | <u> </u> |
| Net income per common share diluted | \$ 1.12 | \$ 0.92 | \$ 1.09 |
| | <u> </u> | <u> </u> | <u> </u> |

See discussion of discontinued operations in footnote 3 above.

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Beginning in 2004, we have reclassified in all periods presented for financial presentation purposes the operating results of Next>edge, our taxable REIT subsidiary, or TRS, from general and administrative expenses to interest income and other loss in our consolidated statements of income. Next>edge provides energy consulting services to commercial real estate owners. The following is a breakdown of the components of interest and other income (loss) for the years ended December 31, 2004, 2003 and 2002 (in thousands):

| | <u>2004</u> | <u>2003</u> | <u>2002</u> |
|----------------------------------|----------------|-----------------|----------------|
| Net loss from Next>edge | \$(960) | \$(1,135) | \$ (478) |
| Interest and other income | 452 | 734 | 2,541 |
| Interest income and other (loss) | <u>\$(508)</u> | <u>\$ (401)</u> | <u>\$2,063</u> |

11. Stock Option Plan

We established a stock option plan for the purpose of attracting and retaining executive officers, directors and other key employees. As of December 31, 2004, 6,500,000 of our authorized shares of common stock have been reserved for issuance under that plan. All holders of the above options have a ten-year period to exercise such options and all options were granted at exercise prices equal to the market prices at the date of the grant.

A summary of stock option activity and related information for the years ended December 31, 2004, 2003 and 2002 follows:

| | <u>2004</u> | | <u>2003</u> | | <u>2002</u> | |
|--|----------------------------|---|----------------------------|---|----------------------------|---|
| | <u>Options (000 s)</u> | <u>Weighted- Average Exercise Price</u> | <u>Options (000 s)</u> | <u>Weighted- Average Exercise Price</u> | <u>Options (000 s)</u> | <u>Weighted- Average Exercise Price</u> |
| Outstanding, beginning of period | 3,426 | \$24.77 | 4,479 | \$24.91 | 5,014 | \$24.63 |
| Granted | | | 268 | 20.81 | 164 | 25.60 |
| Exercised | (1,750) | 24.42 | (1,162) | 24.04 | (424) | 21.40 |
| Forfeited | (40) | 28.12 | (159) | 27.37 | (275) | 25.68 |
| Outstanding at end of year | <u>1,636</u> | <u>\$25.06</u> | <u>3,426</u> | <u>\$24.77</u> | <u>4,479</u> | <u>\$24.91</u> |
| Exercisable at end of the period | <u>1,366</u> | <u>\$25.71</u> | <u>2,952</u> | <u>\$25.03</u> | <u>3,691</u> | <u>\$24.75</u> |
| Weighted-average fair value of options granted | <u>\$</u> | | <u>\$ 0.49</u> | | <u>\$ 1.66</u> | |

Exercise prices for options outstanding as of December 31, 2004 ranged from \$19.13 to \$32.25. The weighted average remaining contractual life of those options is approximately 5 years.

Prior to January 1, 2003 we elected to follow Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees (APB 25) and related interpretations in accounting for our employee and directors stock options because, as discussed below, the alternative fair value accounting provided for under FASB Statement No. 123, Accounting for Stock-Based Compensation (SFAS 123) requires use of option

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valuation models that were not developed for use in valuing employee stock options and that do not necessarily provide a reliable single measure of the fair value of our employee and director stock options. Under APB 25, because the exercise price of employee and director stock options we granted equals the market price of the underlying stock on the date of grant, no compensation expense is recognized.

Beginning on January 1, 2003, we adopted prospectively the provisions of SFAS No. 148, Accounting for Stock-Based Compensation Transition and Disclosure under which we began expensing the costs of new stock options granted to employees. There were no grants of stock options in 2004. We used the Black-Scholes option valuation model to estimate the fair value of the stock options granted in 2003 with the following weighted-average assumptions for 2003: risk-free interest rate of 2.92%, dividend yield of 9.70% and a volatility factor of the expected market price for our common stock of 0.186. During 2004 and 2003, we recognized approximately \$44,000 and \$41,000, respectively, of stock option based employee compensation costs for the stock options granted in 2003.

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Below we also present pro forma information regarding net income and earnings per share as if we had expensed all of our stock options granted prior to 2003. The fair value for these options was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted-average assumptions for 2002: risk-free interest rate of 4.28%, dividend yield of 7.80% and a volatility factor of the expected market price of our common stock of 0.190. The weighted average expected life of the options is approximately 7 to 10 years.

For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the options vesting periods. Our pro forma information for the years ended December 31, 2004, 2003 and 2002 follows (in thousands, except earnings per share information):

| | <u>2004</u> | <u>2003</u> | <u>2002</u> |
|--|-----------------|-----------------|-----------------|
| Net income available to common stockholders, as reported | \$73,775 | \$58,509 | \$70,175 |
| Stock based employee compensation costs for options granted prior to 2003 assuming fair value method | (201) | (843) | (1,477) |
| Net income available to common stockholders, as adjusted | <u>\$73,574</u> | <u>\$57,666</u> | <u>\$68,698</u> |
| Earnings per share: | | | |
| Basic as reported | <u>\$ 1.13</u> | <u>\$ 0.92</u> | <u>\$ 1.09</u> |
| Basic as adjusted | <u>\$ 1.13</u> | <u>\$ 0.91</u> | <u>\$ 1.07</u> |
| Diluted as reported | <u>\$ 1.12</u> | <u>\$ 0.92</u> | <u>\$ 1.09</u> |
| Diluted as adjusted | <u>\$ 1.12</u> | <u>\$ 0.90</u> | <u>\$ 1.07</u> |

12. Employee Retirement Savings Plan*401(k) Plan*

Effective June 12, 1997, we adopted a retirement savings plan pursuant to Section 401(k) of the Internal Revenue Code whereby participants may contribute a portion of their compensation to their respective retirement accounts in an amount not to exceed the maximum allowed under the Internal Revenue Code. The plan provides for matching contributions by us, which amounted to approximately \$1.0 million in 2004, \$888,000 in 2003 and \$844,000 in 2002. Plan participants are immediately vested in their contributions and are vested equally over four years in matching contributions by us.

Deferred Compensation Plan

We also have a Deferred Compensation Plan, or the Plan. This plan provides certain key employees, with supplemental deferred benefits in the form of retirement payments.

During 2004 and 2003, we made contributions to the Plan totaling approximately \$600,000 and \$400,000, respectively. The contributions made by us on behalf of the Plan participants vest 100% to the benefit of the Plan participants after seven years of service to us. A life insurance policy has been purchased on the life of each Plan participant naming us as sole beneficiary to provide a reimbursement to us for all or a portion of the contributions made under the Plan including the cost of the use of our money.

13. Subsequent Events

On January 5, 2005, we sold an approximate 167,000 square foot property located in San Diego County for approximately \$16.7 million. In conjunction with this sale we repaid a \$7.2 million mortgage loan outstanding on this property. This property was classified as held for

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disposition in our balance sheet at December 31, 2004 and 2003. Also on this date, we acquired 707 Broadway, an approximate 170,000 square foot, 96.6% leased office property located in San Diego County for approximately \$48.0 million. Approximately \$2 million of the purchase price for 707 Broadway was funded with the issuance of OP Units.

On January 5, 2005, Andrew Sobel, Executive Vice President Strategic Planning, announced his resignation to pursue other business interests effective February 28, 2005. As part of his separation, Mr. Sobel

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entered into a Confidential Resignation Agreement and General Release and a Consulting Agreement with a term of 3 years. These agreements provide for the following:

Severance pay in an amount equal to 24 months' base salary, plus an amount equal to Mr. Sobel's 2003 bonus and an amount equal to the value of 16,080 unvested stock options for a total amount of \$1,503,487;

The payment of premiums for Mr. Sobel and his dependents' health and dental benefits coverage for no longer the duration of his Consulting Agreement;

Monthly consulting fee of \$25,000;

The continued vesting over the term of the Consulting Agreement of 91,417 unvested restricted stock awards, which are held by Mr. Sobel pursuant to restricted stock agreements with Arden Realty, Inc.;

An agreement by Mr. Sobel not to engage in any business activity, during the term of the Consulting Agreement, that is the same or similar to Mr. Sobel's work for Arden Realty, Inc. and that is within the same geographic territory and which is directly competitive with the business conducted by Arden Realty, Inc. at the time of Mr. Sobel's resignation; and

Customary confidentiality, release of claims, non-disparagement, non-solicitation, and indemnification provisions.

Upon the termination of his employment, Mr. Sobel forfeited 13,329 unvested restricted stock awards and 24,120 stock options (including the 16,080 for which he received payment as described above).

On February 18, 2005, we extended the maturity of our Operating Partnership's \$125 million unsecured term loan with a group of banks led by Wells Fargo Bank from June of 2006 to February of 2012. In conjunction with this extension, our Operating Partnership also entered into a series of interest rate swap agreements to fix the interest rate through the extension period. Under these interest rate swap agreements, the interest rate on this loan is fixed at 5.29% from June of 2006 through May of 2007, 5.55% from June of 2007 through November of 2008, 5.76% from December of 2008 through May of 2010 and 5.99% from June of 2010 through February of 2012.

On February 28, 2005, our Operating Partnership issued \$300 million of senior unsecured notes due in March of 2015. Including offering expenses and the settlement of forward-starting swaps discussed in footnote 2, the all-in effective rate of these unsecured notes is approximately 5.5%. The proceeds from this issuance were used to redeem the notes discussed below and to reduce the outstanding balance on our Wells Fargo unsecured line of credit.

On March 1, 2005, our Operating Partnership redeemed all of its \$200 million, 8.875% senior unsecured notes, maturing March 1, 2005. The total paid for the redemption was 100% of the principal amount of \$200 million, plus interest accrued through March 1, 2005.

Table of Contents**14. Quarterly Results unaudited**

Following is a quarterly summary of our revenue and expenses for the years ended December 31, 2004 and 2003. Revenue and expenses may fluctuate significantly from quarter to quarter due to our development, renovation, acquisition and sales activity.

For the Quarter Ended (in thousands, except per share amounts)

| | March 31, 2004 | June 30, 2004 | September 30, 2004 | December 31, 2004 |
|---|-----------------------|----------------------|---------------------------|--------------------------|
| Revenue | \$ 99,829 | \$ 100,518 | \$ 103,277 | \$ 105,569 |
| Property operating expenses | (32,465) | (32,528) | (34,657) | (33,985) |
| General and administrative | (4,484) | (4,665) | (4,823) | (5,531) |
| Interest expense | (23,147) | (21,019) | (21,352) | (23,338) |
| Depreciation and amortization | (28,882) | (30,481) | (30,595) | (31,729) |
| Interest and other income | 766 | (436) | (178) | (660) |
| Impairment on investment in securities | | (2,700) | | |
| Minority interest | (1,345) | (1,267) | (2,406) | (237) |
| Discontinued operations, net of minority interest | 2,160 | 1,305 | 973 | 1,815 |
| Gain on sale of discontinued properties | 6,429 | 400 | 937 | 22,707 |
| Net Income | \$ 18,861 | \$ 9,127 | \$ 11,176 | \$ 34,611 |
| Net income per share: | | | | |
| Basic | \$ 0.29 | \$ 0.14 | \$ 0.17 | \$ 0.53 |
| Diluted | \$ 0.29 | \$ 0.14 | \$ 0.17 | \$ 0.52 |

For the Quarter Ended (in thousands, except per share amounts)

| | March 31, 2003 | June 30, 2003 | September 30, 2003 | December 31, 2003 |
|---|-----------------------|----------------------|---------------------------|--------------------------|
| Revenue | \$ 96,022 | \$ 97,361 | \$ 100,136 | \$ 100,246 |
| Property operating expenses | (29,786) | (31,077) | (33,463) | (31,653) |
| General and administrative | (3,590) | (3,981) | (4,391) | (4,969) |
| Interest expense | (22,866) | (23,085) | (23,785) | (23,357) |
| Depreciation and amortization | (26,973) | (27,979) | (28,998) | (28,002) |
| Interest and other income | 104 | 149 | (171) | (483) |
| Minority interest | (1,391) | (1,354) | (1,285) | (1,345) |
| Discontinued operations, net of minority interest | 4,557 | 2,848 | 2,498 | 2,635 |
| (Loss) Gain on sale of discontinued properties | (639) | 6,021 | | 555 |
| Net Income | \$ 15,438 | \$ 18,903 | \$ 10,541 | \$ 13,627 |
| Net income per share: | | | | |
| Basic | \$ 0.24 | \$ 0.30 | \$ 0.17 | \$ 0.21 |

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| | | | | |
|---------|---------|---------|---------|---------|
| Diluted | \$ 0.24 | \$ 0.30 | \$ 0.16 | \$ 0.21 |
|---------|---------|---------|---------|---------|

Note: Net income per share on a quarter by quarter basis may not sum to the year to date net income per share due to rounding.

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Table of Contents**15. Schedule of Commercial Properties and Accumulated Depreciation**

December 31, 2004
(in thousands, except square foot data)

| | Initial Costs | | Basis Step Up | | | Total Costs | | Accumulated | | | Year Built/ Renovated | |
|---------------------------|-------------------|---------------------------------------|---------------------------------------|--|---------------------------------------|--------------------|-------------|-------------|-------------|----------|--------------------------|------------|
| | Square Footage | Buildings and Land Improvements | Buildings and Land Improvements | Costs Capitalized Subsequent to Acquisition(2) | Buildings and Land Improvements | Total Depreciation | Liabilities | Liabilities | Liabilities | | | |
| Century Park Center | 235,178 | \$ 7,190 | \$ 17,262 | \$ | \$ | \$ 12,292 | \$ 7,190 | \$ 29,554 | \$ 36,744 | \$ 8,549 | \$ | 1972/94 |
| Beverly Atrium | 59,582 | 4,127 | 11,524 | 118 | 326 | 2,951 | 4,245 | 14,801 | 19,046 | 4,290 | | 1989 |
| Woodland Hills | 229,616 | 6,566 | 14,765 | 365 | 880 | 7,992 | 6,931 | 23,637 | 30,568 | 7,853 | | 1972/95 |
| Anaheim City Centre | 177,266 | 515 | 11,208 | 94 | 2,075 | 4,480 | 609 | 17,763 | 18,372 | 5,112 | | 1986/91 |
| 425 West Broadway | 72,317 | 1,500 | 4,462 | 305 | 918 | 2,201 | 1,805 | 7,581 | 9,386 | 2,164 | | 1984 |
| 1950 Sawtelle | 104,171 | 1,988 | 7,268 | | | 2,761 | 1,988 | 10,029 | 12,017 | 2,655 | 6,671(3) | 1988/95 |
| Bristol Plaza | 84,033 | 1,820 | 3,381 | 257 | 485 | 1,957 | 2,077 | 5,823 | 7,900 | 1,763 | | 1982 |
| 16000 Ventura | 175,275 | 1,700 | 17,145 | 185 | 1,929 | 4,974 | 1,885 | 24,048 | 25,933 | 6,573 | 11,319(3) | 1980/96 |
| 5000 East Spring | 168,967 | | 10,903 | | 424 | 6,151 | | 17,478 | 17,478 | 5,133 | | 1989/95 |
| 70 South Lake | 101,236 | 1,360 | 9,086 | | | 3,066 | 1,360 | 12,152 | 13,512 | 3,623 | | 1982/94 |
| Westwood Terrace | 136,707 | 2,103 | 16,888 | | | 4,073 | 2,103 | 20,961 | 23,064 | 5,485 | | 1988 |
| Westlake | | | | | | | | | | | | |
| 5601 Lindero | 106,144 | 2,576 | 7,747 | | | 4,148 | 2,576 | 11,895 | 14,471 | 3,714 | | 1989 |
| 6100 Wilshire | 202,675 | 1,200 | 19,886 | | | 6,702 | 1,200 | 26,588 | 27,788 | 7,471 | | 1986 |
| Calabasas Commerce Center | 126,771 | 1,262 | 9,721 | | | 3,000 | 1,262 | 12,721 | 13,983 | 3,297 | 7,878(3) | 1990 |
| Long Beach Airport | | | | | | | | | | | | |
| DF&G | 272,013 | | 14,457 | | | 1,549 | | 16,006 | 16,006 | 3,487 | | 1987/95 |
| Skyview Center | 398,261 | 6,514 | 33,696 | | | 9,232 | 6,514 | 42,928 | 49,442 | 10,830 | | 1981/87/95 |
| 400 Corporate Pointe | 165,487 | 3,383 | 17,779 | 74 | 391 | 6,494 | 3,457 | 24,664 | 28,121 | 6,041 | | 1987 |
| 5832 Bolsa | 49,355 | 690 | 3,611 | 15 | 80 | 1,541 | 705 | 5,232 | 5,937 | 1,936 | | 1985 |
| 9665 Wilshire | 159,645 | 6,697 | 22,574 | 139 | 473 | 10,396 | 6,836 | 33,443 | 40,279 | 8,666 | | 1972/92/93 |
| 701 B Street | 548,310 | 3,722 | 35,662 | 64 | 626 | 16,123 | 3,786 | 52,411 | 56,197 | 13,553 | | 1982/96 |
| 100 West Broadway | 191,371 | 4,570 | 15,276 | | | 4,393 | 4,570 | 19,669 | 24,239 | 4,507 | | 1987/96 |
| 303 Glenoaks | 177,898 | 6,500 | 18,132 | | | 6,617 | 6,500 | 24,749 | 31,249 | 5,706 | | 1983/96 |
| 10351 Santa Monica | 96,899 | 3,080 | 8,014 | | | 1,961 | 3,080 | 9,975 | 13,055 | 2,330 | 5,388(3) | 1984 |
| 2730 Wilshire | 55,531 | 3,515 | 4,413 | | | 1,651 | 3,515 | 6,064 | 9,579 | 1,636 | 4,478(3) | 1985 |
| Grand Avenue Plaza | 82,872 | 620 | 2,909 | | | 4,132 | 620 | 7,041 | 7,661 | 1,428 | 5,675(3) | 1980/98 |

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| | Square Footage | Initial Costs | | Basis Step Up | Total Costs | | | | Year Built/ Renovated | | |
|----------------------------------|----------------|--------------------|--------------|--------------------|--------------|--|--------------------|--------------|--------------------------|-----------------------------|--------------|
| | | Buildings and Land | Improvements | Buildings and Land | Improvements | Costs Capitalized Subsequent to Acquisition(2) | Buildings and Land | Improvements | | Accumulated Depreciation(1) | Accumbrances |
| Burbank Executive Plaza | 63,320 | 1,100 | 4,418 | | 2,511 | 1,100 | 6,929 | 8,029 | 2,026 | | 1987/83 |
| 333 N. Glenoaks Center Promenade | 82,939 | 1,500 | 5,976 | | 3,309 | 1,500 | 9,285 | 10,785 | 2,413 | | 1978/83 |
| Los Angeles Corporate Center | 177,072 | 2,310 | 9,296 | | 3,433 | 2,310 | 12,729 | 15,039 | 2,992 | | 1982 |
| 5200 West Century | 389,615 | 26,781 | 15,165 | | 9,677 | 26,781 | 24,842 | 51,623 | 6,990 | | 1986 |
| 15250 Ventura | 312,700 | 2,080 | 9,510 | | 15,728 | 2,080 | 25,238 | 27,318 | 4,907 | | 1982/98/99 |
| 10350 Santa Monica | 112,142 | 2,560 | 10,313 | | 3,800 | 2,560 | 14,113 | 16,673 | 3,430 | | 1970/90-91 |
| 535 N. Brand Blvd. | 42,696 | 860 | 3,458 | | 855 | 860 | 4,313 | 5,173 | 971 | | 1979 |
| 10780 Santa Monica | 109,104 | 1,600 | 8,427 | | 11,739 | 1,600 | 20,166 | 21,766 | 2,951 | | 1973/92/99 |
| 4900 California | 93,211 | 2,625 | 7,531 | | 2,880 | 2,625 | 10,411 | 13,036 | 2,668 | | 1984 |
| Clarendon Crest | 155,791 | 4,680 | 14,133 | | 3,756 | 4,680 | 17,889 | 22,569 | 4,122 | | 1983 |
| Noble Professional Center | 43,222 | 1,300 | 3,741 | | 1,529 | 1,300 | 5,270 | 6,570 | 1,279 | 3,106(3) | 1990 |
| South Bay Centre | 52,599 | 1,657 | 4,817 | | 1,344 | 1,657 | 6,161 | 7,818 | 1,479 | 3,481(3) | 1985/93 |
| 8383 Wilshire Parkway Center I | 204,197 | 4,775 | 13,646 | | 5,716 | 4,775 | 19,362 | 24,137 | 4,654 | 12,420(3) | 1984 |
| Centerpointe La Palma | 424,588 | 13,570 | 43,213 | | 14,756 | 13,570 | 57,969 | 71,539 | 13,573 | | 1971/93 |
| 299 N. Euclid | 61,289 | 1,480 | 5,651 | | 1,053 | 1,480 | 6,704 | 8,184 | 1,563 | | 1992/95 |
| 2800 28th Street | 603,582 | 16,011 | 60,874 | | 13,223 | 16,011 | 74,097 | 90,108 | 16,782 | 32,918(3) | 1986/88/90 |
| 1000 Town Center | 74,573 | 1,050 | 5,738 | | 5,700 | 1,050 | 11,438 | 12,488 | 2,790 | | 1983/99 |
| Mariner Court | 106,481 | 2,938 | 8,425 | | 4,054 | 2,938 | 12,479 | 15,417 | 2,919 | | 1979 |
| Pacific Gateway | 108,508 | 2,800 | 10,638 | | 2,029 | 2,800 | 12,667 | 15,467 | 2,793 | | 1989 |
| Irvine Corporate Center | 105,436 | 2,350 | 9,176 | | 1,781 | 2,350 | 10,957 | 13,307 | 2,571 | 6,660(3) | 1989 |
| Crown Cabot Financial | 225,805 | 6,288 | 18,417 | | 6,818 | 6,288 | 25,235 | 31,523 | 6,832 | | 1982/90 |
| 120 S. Spalding | 126,781 | 1,808 | 5,295 | | 4,559 | 1,808 | 9,854 | 11,662 | 1,849 | | 1980/88/99 |
| 1370 Valley Vista | 174,222 | 7,056 | 20,667 | | 9,352 | 7,056 | 30,019 | 37,075 | 7,064 | | 1989 |
| Foremost Professional Plaza | 64,877 | 2,775 | 8,287 | | 4,863 | 2,775 | 13,150 | 15,925 | 3,189 | 7,943(3) | 1984 |
| Northpoint | 81,962 | 2,698 | 7,900 | | 1,643 | 2,698 | 9,543 | 12,241 | 2,179 | 5,378(3) | 1988 |
| Conejo Business Center | 60,311 | 2,049 | 6,001 | | 1,090 | 2,049 | 7,091 | 9,140 | 1,579 | 8,664 | 1992 |
| | 105,145 | 1,800 | 19,022 | | 3,790 | 1,800 | 22,812 | 24,612 | 4,498 | | 1991 |
| | 69,425 | 2,489 | 6,960 | | 1,740 | 2,489 | 8,700 | 11,189 | 1,677 | 3,617 | 1991 |

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| | Square Footage | Initial Costs | | Basis Step Up | | Total Costs | | | Accumulated Depreciation | Encumbrances | Year Built/ Renovated |
|------------------------------|----------------|---------------|----------------------------|--|----------------------------|-------------|----------------------------|--------|--------------------------|--------------|--------------------------|
| | | Land | Buildings and Improvements | Land | Buildings and Improvements | Land | Buildings and Improvements | Total | | | |
| | | | | Costs Capitalized Subsequent to Acquisition(2) | | | | | | | |
| Marin Corporate Center | 51,776 | 1,956 | 5,589 | 1,108 | 1,956 | 6,697 | 8,653 | 1,089 | 2,585 | 1986 | |
| 145 South Fairfax | 54,398 | 1,825 | 5,325 | 2,473 | 1,825 | 7,798 | 9,623 | 1,513 | 3,869 | 1984 | |
| Bernardo Regency | 48,052 | 1,625 | 4,764 | 1,722 | 1,625 | 6,486 | 8,111 | 1,465 | | 1986 | |
| Fountain Valley City Centre | 303,267 | 8,250 | 23,513 | 5,941 | 8,250 | 29,454 | 37,704 | 6,305 | | 1982 | |
| Wilshire Pacific Plaza | 101,229 | 3,750 | 10,996 | 4,052 | 3,750 | 15,048 | 18,798 | 3,520 | | 1976/87 | |
| World Savings Center | 473,581 | | 106,259 | 27,569 | | 133,828 | 133,828 | 26,957 | | 1983 | |
| Sunset Point Plaza | 59,186 | 2,075 | 6,077 | 1,360 | 2,075 | 7,437 | 9,512 | 1,525 | 3,359(3) | 1988 | |
| Activity Business Center | 167,170 | 3,650 | 10,690 | 2,581 | 3,650 | 13,271 | 16,921 | 2,634 | 7,222 | 1987 | |
| Westlake Gardens | 50,267 | 1,831 | 5,405 | 2,311 | 1,831 | 7,716 | 9,547 | 2,226 | | 1998 | |
| 9100 Wilshire | 328,697 | 16,250 | 47,593 | 10,957 | 16,250 | 58,550 | 74,800 | 13,075 | | 1971/90 | |
| Westwood Center | 314,366 | 3,159 | 24,374 | 85,669 | 3,159 | 110,043 | 113,202 | 13,432 | | 1965/2000 | |
| 1919 Santa Monica | 43,766 | 2,580 | 7,623 | 1,296 | 2,580 | 8,919 | 11,499 | 1,697 | 3,620(3) | 1991 | |
| 600 Corporate Pointe | 275,113 | 8,575 | 34,632 | 8,273 | 8,575 | 42,905 | 51,480 | 8,556 | 17,214(3) | 1989 | |
| 150 East Colorado Boulevard | 61,657 | 1,988 | 5,880 | 2,588 | 1,988 | 8,468 | 10,456 | 1,860 | 4,635(3) | 1979/97 | |
| 5161 Lankershim | 180,940 | 5,016 | 24,908 | 4,723 | 5,016 | 29,631 | 34,647 | 6,136 | 13,196(3) | 1985/97 | |
| Huntington Beach Plaza | 53,459 | 1,109 | 3,284 | 1,335 | 1,109 | 4,619 | 5,728 | 1,068 | 1,468(3) | 1984/96 | |
| Fountain Valley Plaza | 107,313 | 2,949 | 8,728 | 3,282 | 2,949 | 12,010 | 14,959 | 2,302 | 4,699(3) | 1982 | |
| Newport Irvine Center | 75,184 | 2,215 | 6,554 | 1,784 | 2,215 | 8,338 | 10,553 | 1,895 | 3,154(3) | 1981/97 | |
| Von Karman Corporate Center | 452,378 | 11,513 | 34,077 | 11,792 | 11,513 | 45,869 | 57,382 | 10,219 | 18,592(3) | 1981/84 | |
| South Coast Executive Center | 61,292 | 1,563 | 4,526 | 1,369 | 1,563 | 5,895 | 7,458 | 1,281 | 2,199(3) | 1979/97 | |
| City Centre I | 141,903 | 4,792 | 14,172 | 3,724 | 4,792 | 17,896 | 22,688 | 3,491 | 6,859(3) | 1985/97 | |
| Orange Financial Center | 307,920 | 10,379 | 34,714 | 9,792 | 10,379 | 44,506 | 54,885 | 9,325 | 17,679(3) | 1985/95 | |
| Carlsbad Corporate Center | 129,000 | 3,722 | 12,104 | 8,882 | 3,722 | 20,986 | 24,708 | 3,836 | 9,068(3) | 1996 | |
| Balboa Corporate Center | 70,987 | 2,759 | 7,884 | 1,209 | 2,759 | 9,093 | 11,852 | 1,501 | 5,580(3) | 1990 | |

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| | Initial Costs | | | Basis Step Up | | Total Costs | | | | | Year Built/ Renovated | |
|-----------------------------|-------------------|--------------------------|--------------|--------------------------|--------------|--|--------------------------|--------------|--------------------------------------|-------------|--------------------------|------------|
| | Square Footage | Buildings and Land | Improvements | Buildings and Land | Improvements | Costs Capitalized Subsequent to Acquisition(2) | Buildings and Land | Improvements | Accumulated Total Depreciation(3) | Liabilities | | |
| Panorama Corporate Center | 130,396 | 6,512 | 19,249 | | | 4,408 | 6,512 | 23,657 | 30,169 | 4,312 | 12,544(3) | 1991 |
| Ruffin Corporate Center | 45,059 | 1,766 | 5,222 | | | 71 | 1,766 | 5,293 | 7,059 | 939 | 3,330(3) | 1990 |
| Skypark Office Plaza | 203,946 | 5,733 | 21,047 | | | 7,322 | 5,733 | 28,369 | 34,102 | 5,719 | | 1986 |
| Governor Park Plaza | 104,441 | 3,382 | 10,005 | | | 3,299 | 3,382 | 13,304 | 16,686 | 3,265 | 4,890(3) | 1986 |
| 5120 Shoreham | 37,813 | 1,224 | 3,621 | | | 1,283 | 1,224 | 4,904 | 6,128 | 1,430 | 2,903(3) | 1984 |
| Torreyana Science Park | 81,204 | 5,035 | 14,878 | | | 648 | 5,035 | 15,526 | 20,561 | 2,845 | 9,236(3) | 1980/97 |
| Camarillo Business Park | 154,298 | 3,522 | 10,427 | | | 3,680 | 3,522 | 14,107 | 17,629 | 3,305 | 8,100(3) | 1984/97 |
| 5702 Bolsa | 27,731 | 589 | 1,745 | | | 178 | 589 | 1,923 | 2,512 | 382 | 915(3) | 1987/97 |
| 5672 Bolsa | 12,110 | 254 | 753 | | | 65 | 254 | 818 | 1,072 | 159 | 321(3) | 1987 |
| 5632 Bolsa | 21,568 | 458 | 1,358 | | | 92 | 458 | 1,450 | 1,908 | 275 | 822(3) | 1987 |
| Huntington Commerce Center | 69,749 | 992 | 2,941 | | | 578 | 992 | 3,519 | 4,511 | 777 | 1,513(3) | 1987 |
| Savi Tech Center | 242,327 | 5,876 | 17,396 | | | 3,390 | 5,876 | 20,786 | 26,662 | 4,630 | 14,320(3) | 1989 |
| Yorba Linda Business Park | 165,710 | 2,629 | 7,796 | | | 1,230 | 2,629 | 9,026 | 11,655 | 1,904 | 4,057(3) | 1988 |
| Cymer Technology Center | 155,612 | 5,446 | 16,109 | | | 2,819 | 5,446 | 18,928 | 24,374 | 3,324 | 10,615(3) | 1986 |
| Poway Industrial | 112,000 | 1,876 | 5,561 | | | 305 | 1,876 | 5,866 | 7,742 | 1,091 | 3,397(3) | 1991/96 |
| 10180 Scripps Ranch | 43,560 | 1,165 | 3,448 | | | 298 | 1,165 | 3,746 | 4,911 | 688 | 1,941(3) | 1978/96 |
| Via Frontera | 77,920 | 1,792 | 5,306 | | | 1,024 | 1,792 | 6,330 | 8,122 | 1,495 | 2,797(3) | 1982/97 |
| Westridge | 48,955 | 1,807 | 5,345 | | | 616 | 1,807 | 5,961 | 7,768 | 1,204 | 2,890(3) | 1984/96 |
| 6060 Center Drive | 256,665 | 4,299 | 48,701 | | | 12,046 | 4,299 | 60,747 | 65,046 | 7,118 | | 2000 |
| Howard Hughes Spectrum Club | 36,959 | 2,500 | 7,500 | | | 37 | 2,500 | 7,537 | 10,037 | 1,271 | | 1993 |
| 6080 Center Drive | 286,568 | 5,082 | 49,853 | | | 23,702 | 5,082 | 73,555 | 78,637 | 7,209 | | 2001 |
| 6100 Center Drive | 284,798 | 2,513 | 57,079 | | | 24,174 | 2,513 | 81,253 | 83,766 | 3,390 | | 2002 |
| 11075 Santa Monica | 35,996 | 1,225 | 3,588 | | | 1,407 | 1,225 | 4,995 | 6,220 | 1,196 | | 1983 |
| Continental Grand Plaza | 237,494 | 7,125 | 39,416 | | | 9,252 | 7,125 | 48,668 | 55,793 | 9,634 | 26,011(3) | 1986 |
| Calabasas Tech | 283,692 | 11,513 | 32,696 | | | 8,501 | 11,513 | 41,197 | 52,710 | 8,745 | | 1990/2001 |
| Oceangate Tower | 218,554 | 3,080 | 19,838 | | | 4,290 | 3,080 | 24,128 | 27,208 | 4,603 | | 1971/93/94 |

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| | Initial Costs | | | Basis Step Up | | Total Costs | | | | | Year Built/ Renovated |
|--|-------------------|---------------------------------------|---------------------------------------|--|---------------------------------------|---------------------------------------|---------------------------------------|--------------------------------|--------------------|------------------|--------------------------|
| | Square Footage | Buildings and Land Improvements | Buildings and Land Improvements | Costs Capitalized Subsequent to Acquisition(2) | Buildings and Land Improvements | Buildings and Land Improvements | Buildings and Land Improvements | Accumulated Depreciation(1) | Encumbrances | | |
| Genesee Executive Plaza Solar Drive Business Center | 155,014 | 6,750 | 19,691 | 5,651 | 6,750 | 25,342 | 32,092 | 5,295 | 15,908(3) | 1984 | |
| 601 S. Glenoaks | 138,341 | 4,250 | 12,447 | 2,093 | 4,250 | 14,540 | 18,790 | 2,680 | | 1982 | |
| Tourney Pointe | 74,745 | 2,450 | 7,132 | 1,712 | 2,450 | 8,844 | 11,294 | 1,574 | 5,535(3) | 1990 | |
| Hillside Corporate Center | 219,673 | 6,047 | 20,312 | 12,880 | 6,047 | 33,192 | 39,239 | 6,592 | | 1985/98/2000 | |
| Westlake Gardens II | 61,000 | 2,213 | 7,336 | 2,285 | 2,213 | 9,621 | 11,834 | 1,792 | | 1998 | |
| Howard Hughes Tower | 48,874 | 1,831 | 5,493 | 1,448 | 1,831 | 6,941 | 8,772 | 1,280 | | 1999 | |
| 2001 Wilshire Blvd. | 316,014 | 5,830 | 44,839 | 14,405 | 5,830 | 59,244 | 65,074 | 11,543 | | 1987 | |
| Carmel Valley Centre | 99,565 | 5,006 | 14,540 | 1,861 | 5,006 | 16,401 | 21,407 | 2,593 | | 1980 | |
| Carmel View Office Plaza | 109,518 | 4,900 | 23,336 | 1,794 | 4,900 | 25,130 | 30,030 | 1,440 | | 1987/89 | |
| Crossroads | 77,672 | 3,100 | 9,342 | 972 | 3,100 | 10,314 | 13,414 | 675 | | 1985 | |
| Governor Executive Center | 134,477 | 3,950 | 12,810 | 1,723 | 3,950 | 14,533 | 18,483 | 969 | | 1979 | |
| Governor Executive Center II | 52,828 | 1,500 | 9,670 | 368 | 1,500 | 10,038 | 11,538 | 521 | | 1988 | |
| Homestore | 433,545 | 5,585 | 56,892 | 4,093 | 5,585 | 60,985 | 66,570 | 3,594 | | 1984/86 | |
| Warner Corporate Center | 101,433 | 1,959 | 17,958 | 2,895 | 1,959 | 20,853 | 22,812 | 1,545 | | 1989 | |
| | 137,762 | 9,128 | 19,253 | 3,790 | 9,128 | 23,043 | 32,171 | 386 | | 2000 | |
| | 253,000 | 2,860 | 53,725 | 8,806 | 2,860 | 62,531 | 65,391 | 603 | | 1988 | |
| | 18,110,660 | \$452,473 | \$1,879,789 | \$1,616 | \$8,607 | \$660,848 | \$454,089 | \$2,549,244 | \$3,003,333 | \$491,442 | \$382,639 |

- (1) The depreciable lives for buildings and improvements and furniture, fixtures and equipment range from five to forty seven years. Tenant improvements and leasing costs are depreciated over the remaining term of the lease.
- (2) Amounts shown net of write-offs of fully depreciated assets and include total capitalized interest of \$54.6 million.
- (3) All of these properties are collateral for our \$365.3 million mortgage financings. The encumbrance allocated to an individual property is based on the related individual release price.

Table of Contents**ARDEN REALTY, INC.****15. Schedule of Commercial Properties and Accumulated Depreciation (continued)**

The changes in our investment in commercial properties and related accumulated depreciation for each of the periods in the three years ended December 31, 2004, 2003 and 2002 are as follows (in thousands):

| | Arden Realty, Inc. | | |
|---|----------------------------------|-----------------------------|-----------------------------|
| | For the Years Ended December 31, | | |
| | 2004 | 2003 | 2002 |
| Commercial Properties: | | | |
| Balance at beginning of period | \$ 3,008,081 | \$ 3,045,208 | \$ 2,797,052 |
| Improvements | 93,811 | 77,532 | 95,073 |
| Disposition of property | (196,999) | (97,632) | (24,094) |
| Write offs of fully depreciated assets | (65,591) | (37,913) | (24,129) |
| Acquisition of properties | 97,503 | 22,054 | 134,938 |
| Transfers from (to) properties under development and land available for development | 66,528 | | 66,368 |
| Reclassification to other assets | | (1,168) | |
| | <u> </u> | <u> </u> | <u> </u> |
| Balance at end of period | <u>\$ 3,003,333</u> | <u>\$ 3,008,081</u> | <u>\$ 3,045,208</u> |
| Accumulated Depreciation: | | | |
| Balance at beginning of period | \$ (460,732) | \$ (392,611) | \$ (307,082) |
| Depreciation for period | (125,315) | (118,416) | (111,022) |
| Disposition of property | 29,817 | 12,325 | 1,982 |
| Write offs of fully depreciated assets | 65,591 | 37,913 | 24,129 |
| Transfers to (from) properties under development and land available for development | (803) | | (618) |
| Reclassification to other assets | | 57 | |
| | <u> </u> | <u> </u> | <u> </u> |
| Balance at end of period | <u>\$ (491,442)</u> | <u>\$ (460,732)</u> | <u>\$ (392,611)</u> |