HIGHWOODS PROPERTIES INC
Form 10-Q
July 26, 2012

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

FORM 10-Q

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

For the quarterly period ended June 30, 2012

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

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

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

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

3100 Smoketree Court, Suite 600
Raleigh, NC 27604
(Address of principal executive offices) (Zip Code)
919-872-4924
(Registrants’ telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Highwoods Properties, Inc. Yes S No £ Highwoods Realty Limited Partnership Yes S No £

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of 'large accelerated filer,' 'accelerated filer' and 'smaller reporting company' in Rule 12b-2 of the Securities Exchange Act.
Highwoods Properties, Inc.
Large accelerated filer S Accelerated filer £ Non-accelerated filer £ Smaller reporting company £

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Securities Exchange Act).
Highwoods Properties, Inc. Yes £ No S Highwoods Realty Limited Partnership Yes £ No S

The Company had 76,070,588 shares of Common Stock outstanding as of July 19, 2012.

HIGHWOODS PROPERTIES, INC.
HIGHWOODS REALTY LIMITED PARTNERSHIP

QUARTERLY REPORT FOR THE PERIOD ENDED JUNE 30, 2012

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

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

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

Certain information contained herein is presented as of July 19, 2012, the latest practicable date for financial information prior to the filing of this Quarterly Report.

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HIGHWOODS PROPERTIES, INC.
Consolidated Balance Sheets
(Unaudited and in thousands, except share and per share data)

	June 30, 2012	December 31, 2011
Assets:		
Real estate assets, at cost:		
Land	$366,925	$ 364,022
Buildings and tenant improvements	3,117,730	3,078,308
Development in process	6,094	—
Land held for development	102,482	105,206
	3,593,231	3,547,536
Less-accumulated depreciation	(913,016)	(877,383)
Net real estate assets	2,680,215	2,670,153
For-sale residential condominiums	2,434	4,751
Real estate and other assets, net, held for sale	36,751	50,335
Cash and cash equivalents	6,527	11,188
Restricted cash	20,757	26,666
Accounts receivable, net of allowance of $3,262 and $3,548, respectively	21,882	30,093
Mortgages and notes receivable, net of allowance of $118 and $61, respectively	17,056	18,600
Accrued straight-line rents receivable, net of allowance of $866 and $1,294, respectively	113,695	104,284
Investments in and advances to unconsolidated affiliates	77,089	100,367
Deferred financing and leasing costs, net of accumulated amortization of $70,572 and $62,319, respectively	126,680	127,774
Prepaid expenses and other assets	41,907	36,781
Total Assets	$3,144,993	$ 3,180,992
Liabilities, Noncontrolling Interests in the Operating Partnership and Equity:		
Mortgages and notes payable	$1,823,128	$ 1,903,213
Accounts payable, accrued expenses and other liabilities	137,108	148,821
Financing obligations	30,822	31,444
Total Liabilities	1,991,058	2,083,478
Commitments and contingencies		
Noncontrolling interests in the Operating Partnership	124,880	110,655
Equity:		
Preferred Stock, $.01 par value, 50,000,000 authorized shares;		
8.625% Series A Cumulative Redeemable Preferred Shares (liquidation preference $1,000 per share), 29,077 shares issued and outstanding	29,077	29,077
Common Stock, $.01 par value, 200,000,000 authorized shares;		
75,619,288 and 72,647,697 shares issued and outstanding, respectively	756	726
Additional paid-in capital	1,884,392	1,803,997
Distributions in excess of net income available for common stockholders	(878,984)	(845,853)
Accumulated other comprehensive loss	(10,779)	(5,734)
Total Stockholders' Equity	1,024,462	982,213
Noncontrolling interests in consolidated affiliates	4,593	4,646
Total Equity	1,029,055	986,859
Total Liabilities, Noncontrolling Interests in the Operating Partnership and Equity	$3,144,993	$ 3,180,992

See accompanying notes to consolidated financial statements.

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HIGHWOODS PROPERTIES, INC.
Consolidated Statements of Income
(Unaudited and in thousands, except per share amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Rental and other revenues	$130,735	$114,651	$258,768	$226,981
Operating expenses:				
Rental property and other expenses	47,089	39,931	92,288	79,838
Depreciation and amortization	40,276	32,684	78,105	65,621
General and administrative	8,900	7,978	18,573	15,771
Total operating expenses	96,265	80,593	188,966	161,230
Interest expense:				
Contractual	23,643	22,940	47,591	45,371
Amortization of deferred financing costs	900	821	1,802	1,642
Financing obligations	(48)	146	(96)	437
	24,495	23,907	49,297	47,450
Other income:				
Interest and other income	1,737	1,899	3,967	3,772
Losses on debt extinguishment	(973)	(24)	(973)	(24)
	764	1,875	2,994	3,748
Income from continuing operations before disposition of property and condominiums and equity in earnings of unconsolidated affiliates	10,739	12,026	23,499	22,049
Gains on disposition of property	—	200	—	200
Gains on for-sale residential condominiums	110	116	175	154
Equity in earnings of unconsolidated affiliates	1,508	1,353	1,346	2,820
Income from continuing operations	12,357	13,695	25,020	25,223
Discontinued operations:				
Income from discontinued operations	756	739	1,291	1,654
Net gains on disposition of discontinued operations	1,385	—	6,519	—
	2,141	739	7,810	1,654
Net income	14,498	14,434	32,830	26,877
Net (income) attributable to noncontrolling interests in the Operating Partnership	(686)	(623)	(1,513)	(1,130)
Net (income) attributable to noncontrolling interests in consolidated affiliates	(223)	(182)	(407)	(305)
Dividends on Preferred Stock	(627)	(1,622)	(1,254)	(3,299)
Excess of Preferred Stock redemption/repurchase cost over carrying value	—	(1,895)	—	(1,895)
Net income available for common stockholders	$12,962	$10,112	$29,656	$20,248
Earnings per Common Share – basic:				
Income from continuing operations available for common stockholders	$0.15	$0.13	$0.30	$0.26
Income from discontinued operations available for common stockholders	0.02	0.01	0.10	0.02
Net income available for common stockholders	$0.17	$0.14	$0.40	$0.28
Weighted average Common Shares outstanding – basic	74,662	72,211	73,749	72,015
Earnings per Common Share – diluted:				
Income from continuing operations available for common stockholders	$0.15	$0.13	$0.30	$0.26
	0.02	0.01	0.10	0.02

Income from discontinued operations available for common stockholders				
Net income available for common stockholders	$0.17	$0.14	$0.40	$0.28
Weighted average Common Shares outstanding – diluted	78,521	76,197	77,601	75,987
Dividends declared per Common Share	$0.425	$0.425	$0.850	$0.850
Net income available for common stockholders:				
Income from continuing operations available for common stockholders	$10,923	$9,410	$22,226	$18,677
Income from discontinued operations available for common stockholders	2,039	702	7,430	1,571
Net income available for common stockholders	$12,962	$10,112	$29,656	$20,248

See accompanying notes to consolidated financial statements.

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HIGHWOODS PROPERTIES, INC.
Consolidated Statements of Comprehensive Income
(Unaudited and in thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Comprehensive income/(loss):				
Net income	$14,498	$14,434	$32,830	$26,877
Other comprehensive income/(loss):				
Unrealized gains/(losses) on tax increment financing bond	296	(336)	583	(471)
Unrealized losses on cash flow hedges	(7,481)	—	(7,087)	—
Amortization of cash flow hedges	782	(29)	1,459	(58)
Total other comprehensive loss	(6,403)	(365)	(5,045)	(529)
Total comprehensive income	8,095	14,069	27,785	26,348
Less-comprehensive (income) attributable to noncontrolling interests	(909)	(805)	(1,920)	(1,435)
Comprehensive income attributable to the Company	$7,186	$13,264	$25,865	$24,913

See accompanying notes to consolidated financial statements.

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HIGHWOODS PROPERTIES, INC.
Consolidated Statements of Equity
(Unaudited and in thousands, except share amounts)

	Number of Common Shares	Common Stock	Series A Cumulative Redeemable Preferred Shares	Additional Paid-In Capital	Accumulated Other Compre-hensive Loss	Non-Controlling Interests in Consolidated Affiliates	Distributions in Excess of Net Income Available for Common Stockholders	Total
Balance at December 31, 2011	72,647,697	$ 726	$ 29,077	$ 1,803,997	$ (5,734)	$ 4,646	$ (845,853)	$ 986,859
Issuances of Common Stock, net	2,794,340	28	—	91,808	—	—	—	91,836
Conversions of Common Units to Common Stock	18,366	—	—	631	—	—	—	631
Dividends on Common Stock		—	—	—	—	—	(62,787)	(62,787)
Dividends on Preferred Stock		—	—	—	—	—	(1,254)	(1,254)
Adjustment of noncontrolling interests in the Operating Partnership to fair value		—	—	(16,501)	—	—	—	(16,501)
Distributions to noncontrolling interests in consolidated affiliates		—	—	—	—	(460)	—	(460)
Issuances of restricted stock	158,885	—	—	—	—	—	—	—
Share-based compensation expense		2	—	4,457	—	—	—	4,459
Net (income) attributable to noncontrolling interests in the Operating Partnership		—	—	—	—	—	(1,513)	(1,513)
Net (income) attributable to noncontrolling interests in consolidated affiliates		—	—	—	—	407	(407)	—
Comprehensive income:								
Net income		—	—	—	—	—	32,830	32,830

Other comprehensive loss		—	—	—	(5,045)	—	—		(5,045)
Total comprehensive income									27,785
Balance at June 30, 2012	75,619,288	$ 756	$ 29,077	$ 1,884,392	$ (10,779)	$ 4,593		$ (878,984)	$ 1,029,055

	Number of Common Shares	Common Stock	Series A Cumulative Redeemable Preferred Shares	Series B Cumulative Redeemable Preferred Shares	Additional Paid-In Capital	Accumulated Other Compre-hensive Loss	Non-Controlling Interests in Consolidated Affiliates	Distributions in Excess of Net Income Available for Common Stockholders	Total
Balance at December 31, 2010	71,690,487	$ 717	$ 29,092	$ 52,500	$ 1,766,886	$ (3,648)	$ 4,460	$ (761,785)	$ 1,088,222
Issuances of Common Stock, net	556,652	6	—	—	16,978	—	—	—	16,984
Conversions of Common Units to Common Stock	18,737	—	—	—	635	—	—	—	635
Dividends on Common Stock		—	—	—	—	—	—	(61,069)	(61,069)
Dividends on Preferred Stock		—	—	—	—	—	—	(3,299)	(3,299)
Adjustment of noncontrolling interests in the Operating Partnership to fair value		—	—	—	(6,957)	—	—	—	(6,957)
Distributions to noncontrolling interests in consolidated affiliates		—	—	—	—	—	(319)	—	(319)
Issuances of restricted stock	133,552	—	—	—	—	—	—	—	—
Redemptions/repurchases of Preferred Stock		—	(5)	(52,500)	1,895	—	—	(1,895)	(52,505)
Share-based compensation expense		1	—	—	3,452	—	—	—	3,453
Net (income) attributable to noncontrolling interests in the Operating Partnership		—	—	—	—	—	—	(1,130)	(1,130)
Net (income) attributable to noncontrolling interests in consolidated affiliates		—	—	—	—	—	305	(305)	—
Comprehensive income:									
Net income		—	—	—	—	—	—	26,877	26,877
Other comprehensive loss		—	—	—	—	(529)	—	—	(529)

Total comprehensive income									26,348
Balance at June 30, 2011	72,399,428	$724	$29,087	$—	$1,782,889	$(4,177)	$4,446	$(802,606)	$1,010,363

See accompanying notes to consolidated financial statements.

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HIGHWOODS PROPERTIES, INC.
Consolidated Statements of Cash Flows
(Unaudited and in thousands)

	Six Months Ended June 30,	
	2012	2011
Operating activities:		
Net income	$32,830	$26,877
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	79,113	67,274
Amortization of lease incentives and acquisition-related intangible assets and liabilities	180	968
Share-based compensation expense	4,459	3,453
Allowance for losses on accounts and accrued straight-line rents receivable	538	1,029
Amortization of deferred financing costs	1,802	1,642
Amortization of cash flow hedges	1,459	(58)
Losses on debt extinguishment	973	24
Net gains on disposition of property	(6,519)	(200)
Gains on for-sale residential condominiums	(175)	(154)
Equity in earnings of unconsolidated affiliates	(1,346)	(2,820)
Changes in financing obligations	(584)	(245)
Distributions of earnings from unconsolidated affiliates	2,225	2,162
Changes in operating assets and liabilities:		
Accounts receivable	7,298	(1,821)
Prepaid expenses and other assets	(3,158)	(644)
Accrued straight-line rents receivable	(9,415)	(6,098)
Accounts payable, accrued expenses and other liabilities	(16,352)	(3,794)
Net cash provided by operating activities	93,328	87,595
Investing activities:		
Investment in acquired real estate and related intangible assets, net of cash acquired	—	(7,761)
Investment in development in process	(1,531)	(2,598)
Investment in tenant improvements and deferred leasing costs	(43,851)	(28,456)
Investment in building improvements	(19,758)	(5,632)
Net proceeds from disposition of real estate assets	19,898	2,063
Net proceeds from disposition of for-sale residential condominiums	2,492	2,401
Distributions of capital from unconsolidated affiliates	901	632
Repayments of mortgages and notes receivable	1,544	235
Investments in and advances to unconsolidated affiliates	(2,750)	(39,402)
Changes in restricted cash and other investing activities	4,031	(395)
Net cash used in investing activities	(39,024)	(78,913)
Financing activities:		
Dividends on Common Stock	(62,787)	(61,069)
Redemptions/repurchases of Preferred Stock	—	(52,505)
Dividends on Preferred Stock	(1,254)	(3,299)
Distributions to noncontrolling interests in the Operating Partnership	(3,158)	(3,215)
Distributions to noncontrolling interests in consolidated affiliates	(460)	(319)
Proceeds from the issuance of Common Stock	95,289	16,984
Costs paid for the issuance of Common Stock	(1,316)	—
Repurchase of shares related to tax withholdings	(2,137)	—
Borrowings on revolving credit facility	106,300	124,700
Repayments of revolving credit facility	(392,800)	(79,300)

Borrowings on mortgages and notes payable	225,000	200,000
Repayments of mortgages and notes payable	(19,359)	(153,522)
Payments on financing obligations	(38)	—
Additions to deferred financing costs and other financing activities	(2,245)	(2,104)
Net cash used in financing activities	(58,965)	(13,649)
Net decrease in cash and cash equivalents	(4,661)	(4,967)
Cash and cash equivalents at beginning of the period	11,188	14,206
Cash and cash equivalents at end of the period	$6,527	$9,239

See accompanying notes to consolidated financial statements.

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HIGHWOODS PROPERTIES, INC.
Consolidated Statements of Cash Flows – Continued
(Unaudited and in thousands)

Supplemental disclosure of cash flow information:

	Six Months Ended June 30,	
	2012	2011
Cash paid for interest, net of amounts capitalized	$48,063	$44,948

Supplemental disclosure of non-cash investing and financing activities:

	Six Months Ended June 30,	
	2012	2011
Unrealized losses on cash flow hedges	$(7,087)	$—
Conversion of Common Units to Common Stock	631	635
Changes in accrued capital expenditures	(2,448)	1,525
Write-off of fully depreciated real estate assets	28,629	23,352
Write-off of fully amortized deferred financing and leasing costs	8,765	8,247
Unrealized gains on marketable securities of non-qualified deferred compensation plan	216	210
Adjustment of noncontrolling interests in the Operating Partnership to fair value	16,501	6,957
Unrealized gains/(losses) on tax increment financing bond	583	(471)
Reduction of advances to unconsolidated affiliates related to acquisition activities	26,000	—

See accompanying notes to consolidated financial statements.

HIGHWOODS PROPERTIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2012
(tabular dollar amounts in thousands, except per share data)
(Unaudited)

1. Description of Business and Significant Accounting Policies

Description of Business

Highwoods Properties, Inc., together with its consolidated subsidiaries (the “Company”), is a fully-integrated, self-administered and self-managed equity real estate investment trust (“REIT”) that provides leasing, management, development, construction and other customer-related services for its properties and for third parties. The Company conducts virtually all of its activities through Highwoods Realty Limited Partnership (the “Operating Partnership”). At June 30, 2012, the Company and/or the Operating Partnership wholly owned: 304 in-service office, industrial and retail properties, comprising 29.5 million square feet; nine for-sale residential condominiums; 581 acres of undeveloped land suitable for future development, of which 518 acres are considered core assets; and one office property under development.

The Company is the sole general partner of the Operating Partnership. At June 30, 2012, the Company owned all of the Preferred Units and 75.2 million, or 95.3%, of the Common Units in the Operating Partnership. Limited partners, including one officer and two directors of the Company, own the remaining 3.7 million Common Units. In the event the Company issues shares of Common Stock, the net proceeds are contributed to the Operating Partnership in exchange for additional Common Units. Generally, the Operating Partnership is required to redeem each Common Unit at the request of the holder thereof for cash equal to the value of one share of the Company’s Common Stock, $0.01 par value, based on the average of the market price for the 10 trading days immediately preceding the notice date of such redemption, provided that the Company at its option may elect to acquire any such Common Units presented for redemption for cash or one share of Common Stock. The Common Units owned by the Company are not redeemable. During the six months ended June 30, 2012, the Company redeemed 18,366 Common Units for a like number of shares of Common Stock. The redemptions, in conjunction with the proceeds from issuances of Common Stock contributed to the Operating Partnership in exchange for additional Common Units, increased the percentage of Common Units owned by the Company from 95.1% at December 31, 2011 to 95.3% at June 30, 2012.

Common Stock Offerings

The Company has entered into equity sales agreements with various financial institutions to offer and sell, from time to time, shares of its Common Stock by means of ordinary brokers' transactions on the New York Stock Exchange or otherwise at market prices prevailing at the time of sale, at prices related to prevailing market prices or at negotiated prices or as otherwise agreed with any of the institutions. During the three and six months ended June 30, 2012, the Company issued 1,836,976 and 2,622,476 shares, respectively, of Common Stock under these agreements at an average gross sales price of $33.72 and $33.45 per share, respectively, raising net proceeds, after sales commissions and expenses, of $61.0 million and $86.4 million, respectively.

Basis of Presentation

Our Consolidated Financial Statements are prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”). Our Consolidated Balance Sheet at December 31, 2011 was recast from previously reported amounts to reflect in real estate and other assets, net, held for sale those properties which qualified as held for sale during the three months ended June 30, 2012. Our Consolidated Statements of Income for the three and six months ended June 30, 2011 were recast from previously reported amounts to reflect in discontinued operations the operations for those properties that qualified for discontinued operations. Prior period amounts related to capital expenditures in our Consolidated Statements of Cash Flows have been reclassified to conform to the current period presentation.

Our Consolidated Financial Statements include the Operating Partnership, wholly owned subsidiaries and those entities in which we have the controlling financial interest. All intercompany transactions and accounts have been eliminated. At June 30, 2012 and December 31, 2011, we had involvement with no entities that we concluded to be variable interest entities.

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1. Description of Business and Significant Accounting Policies – Continued

The unaudited interim consolidated financial statements and accompanying unaudited consolidated financial information, in the opinion of management, contain all adjustments (including normal recurring accruals) necessary for a fair presentation of our financial position, results of operations and cash flows. We have omitted certain notes and other information from the interim consolidated financial statements presented in this Quarterly Report on Form 10-Q as permitted by SEC rules and regulations. These Consolidated Financial Statements should be read in conjunction with our 2011 Annual Report on Form 10-K.

Use of Estimates

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

Recently Issued Accounting Standards

As a result of adopting certain new or amended accounting pronouncements in the first quarter of 2012, we have enhanced our disclosure of assets and liabilities measured at fair value and elected to continue use of credit valuation adjustments on a net basis by counterparty as part of the calculation to determine the fair value of our derivatives. Our disclosures now include: (1) significant transfers between Levels 1 and 2 of the fair value hierarchy, if any; (2) additional quantitative and qualitative information regarding fair value measurements categorized as Level 3 of the fair value hierarchy; and (3) the hierarchy classification for items whose fair value is not recorded on our Consolidated Balance Sheets but was disclosed previously in our Notes to Consolidated Financial Statements. Additionally, we have presented comprehensive income in a separate financial statement entitled Consolidated Statements of Comprehensive Income.

2. Real Estate Assets

Acquisitions

During the second quarter of 2012, we acquired a 178,300 square foot office property in Cary, NC from our DLF I joint venture for an agreed upon value of $26.0 million by reducing the balance of the advance due to us from the joint venture.

Dispositions

During the second quarter of 2012, we sold a non-core office property in Pinellas County, FL for gross proceeds of $9.5 million. We recorded gain on disposition of discontinued operations of $1.4 million related to this disposition.

During the first quarter of 2012, we sold 96 vacant rental residential units in Kansas City, MO for gross proceeds of $11.0 million. We recorded gain on disposition of discontinued operations of $5.1 million related to this disposition.

3. Mortgages and Notes Receivable

The following table sets forth our mortgages and notes receivable:

	June 30, 2012	December 31, 2011
Seller financing (first mortgages)	$15,853	$ 17,180
Less allowance	—	—
	15,853	17,180
Promissory notes	1,321	1,481
Less allowance	(118)	(61)
	1,203	1,420
Mortgages and notes receivable, net	$17,056	$ 18,600

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HIGHWOODS PROPERTIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(tabular dollar amounts in thousands, except per share data)

3. Mortgages and Notes Receivable - Continued

Our mortgages and notes receivable consist primarily of seller financing issued in conjunction with two disposition transactions in 2010. This seller financing is evidenced by first mortgages secured by the assignment of rents and the underlying real estate assets. We evaluate the collectibility of the receivables by monitoring the leasing statistics and market fundamentals of these assets. As of June 30, 2012, the payments on both mortgages receivable were current and there were no other indications of impairment on the receivables. We may be required to take impairment charges in the future if and to the extent the underlying collateral diminishes in value.

The following table sets forth our notes receivable allowance, which relates only to promissory notes:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Beginning notes receivable allowance	$122	$497	$61	$868
Bad debt expense	—	162	—	184
Recoveries/write-offs/other	(4)	(42)	57	(435)
Total notes receivable allowance	$118	$617	$118	$617

4. Investments in and Advances to Affiliates

Unconsolidated Affiliates

We have equity interests of up to 50.0% in various joint ventures with unrelated third parties and a secured debt interest in one of those joint ventures, as described below. The following table sets forth the combined, summarized income statements for our unconsolidated joint ventures on the purchase accounting basis:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Income Statements:				
Rental and other revenues	$26,049	$24,779	$50,869	$49,996
Expenses:				
Rental property and other expenses	12,666	10,774	24,082	22,771
Depreciation and amortization	5,919	6,295	12,484	12,911
Impairment of real estate assets	—	—	7,180	—
Interest expense	5,267	5,858	11,097	11,865
Total expenses	23,852	22,927	54,843	47,547
Income/(loss) before disposition of properties	2,197	1,852	(3,974)	2,449
Gains on disposition of properties	6,275	—	6,275	—
Net income	$8,472	$1,852	$2,301	$2,449
Our share of:				
Depreciation and amortization of real estate assets	$1,675	$2,033	$3,773	$4,126
Impairment of real estate assets	$—	$—	$1,002	$—
Interest expense	$1,843	$2,033	$3,823	$4,194

Net income	$1,133	$749	$338	$1,670
Our share of net income	$1,133	$749	$338	$1,670
Management and other fees adjustments	375	604	1,008	1,150
Equity in earnings of unconsolidated affiliates	$1,508	$1,353	$1,346	$2,820

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4. Investments in and Advances to Affiliates - Continued

In 2011, we provided a $38.3 million interest-only secured loan to our DLF I joint venture that originally was scheduled to mature in March 2012. The loan bears interest at LIBOR plus 500 basis points. The maturity date of the loan has been extended to September 30, 2012. In the second quarter of 2012, we acquired an office property from the joint venture by reducing the balance of the advance due to us from the joint venture. We deferred our share of the gain recorded by the joint venture related to this transaction. We recorded interest income from this loan in interest and other income of $0.2 million and $0.3 million during the three months ended June 30, 2012 and 2011, respectively, and $0.7 million and $0.3 million during the six months ended June 30, 2012 and 2011, respectively.

In the second quarter of 2012, our DLF II joint venture obtained a $50.0 million, three-year secured mortgage loan from a third party lender, bearing a fixed interest rate of 3.5% on $39.1 million of the loan and a floating interest rate of LIBOR plus 250 basis points on $10.9 million of the loan, which was used by the joint venture to repay a secured loan at maturity to a third party lender.

During the first quarter of 2012, we recorded $1.0 million as our share of impairment of real estate assets on two office properties in our DLF I joint venture, due to a decline in projected occupancy and a change in the assumed holding period of those assets, which reduced the expected future cash flows from the properties.

5. Intangible Assets and Below Market Lease Liabilities

The following table sets forth total intangible assets and acquisition-related below market lease liabilities, net of accumulated amortization:

	June 30, 2012	December 31, 2011
Assets:		
Deferred financing costs	$20,112	$18,044
Less accumulated amortization	(7,488)	(5,797)
	12,624	12,247
Deferred leasing costs (including lease incentives and acquisition-related intangible assets)	177,140	172,049
Less accumulated amortization	(63,084)	(56,522)
	114,056	115,527
Deferred financing and leasing costs, net	$126,680	$127,774
Liabilities (in accounts payable, accrued expenses and other liabilities):		
Acquisition-related below market lease liabilities	$16,346	$16,441
Less accumulated amortization	(1,966)	(971)
	$14,380	$15,470

The following table sets forth amortization of intangible assets and acquisition-related below market lease liabilities:

	Three Months Ended June 30,	Six Months Ended June 30,

	2012	2011	2012	2011
Amortization of deferred financing costs	$900	$821	$1,802	$1,642
Amortization of deferred leasing costs and acquisition-related intangible assets (in depreciation and amortization)	$7,266	$4,401	$13,706	$8,757
Amortization of lease incentives (in rental and other revenues)	$340	$303	$683	$641
Amortization of acquisition-related intangible assets (in rental and other revenues)	$324	$191	$594	$377
Amortization of acquisition-related below market lease liabilities (in rental and other revenues)	$(553)	$(25)	$(1,097)	$(50)

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

5. Intangible Assets and Below Market Lease Liabilities - Continued

The following table sets forth scheduled future amortization of intangible assets and below market lease liabilities:

	Amortization of Deferred Financing Costs	Amortization of Deferred Leasing Costs and Acquisition-Related Intangible Assets (in Depreciation and Amortization)	Amortization of Lease Incentives (in Rental and Other Revenues)	Amortization of Acquisition-Related Intangible Assets (in Rental and Other Revenues)	Amortization of Acquisition-Related Below Market Lease Liabilities (in Rental and Other Revenues)
July 1, 2012 through December 31, 2012	$2,234	$ 14,242	$772	$ 579	$ (1,229)
2013	3,262	21,834	1,167	765	(2,081)
2014	2,987	17,877	1,013	504	(2,005)
2015	2,264	13,879	779	328	(1,768)
2016	957	10,880	608	280	(1,498)
Thereafter	920	25,453	2,379	717	(5,799)
	$12,624	$ 104,165	$6,718	$ 3,173	$ (14,380)

The weighted average remaining amortization periods for deferred financing costs, deferred leasing costs and acquisition-related intangible assets (in depreciation and amortization), lease incentives (in rental and other revenues), acquisition-related intangible assets (in rental and other revenues) and acquisition-related below market lease liabilities (in rental and other revenues) were 3.8 years, 6.2 years, 7.8 years, 5.7 years and 8.9 years, respectively, as of June 30, 2012.

In connection with the acquisition of an office property in Cary, NC in the second quarter of 2012, we recorded $2.7 million of in-place lease intangible assets with a weighted average amortization period of 6.3 years at the date of the acquisition. The contractual rents of the in-place lease acquired were determined to be at market.

6. Mortgages and Notes Payable

The following table sets forth our mortgages and notes payable:

	June 30, 2012	December 31, 2011
Secured indebtedness	$743,492	$ 750,049
Unsecured indebtedness	1,079,636	1,153,164
Total mortgages and notes payable	$1,823,128	$ 1,903,213

At June 30, 2012, our secured mortgage loans were secured by real estate assets with an aggregate undepreciated book value of $1,237.7 million.

Our $475.0 million unsecured revolving credit facility is scheduled to mature on July 27, 2015 and includes an accordion feature that allows for an additional $75.0 million of borrowing capacity subject to additional lender commitments. Assuming no defaults have occurred, we have an option to extend the maturity for an additional year. The interest rate at our current credit ratings is LIBOR plus 150 basis points and the annual facility fee is 35 basis points. The interest rate and facility fee are based on the higher of the publicly announced ratings from Moody's Investors Service or Standard & Poor's Ratings Services. We use our revolving credit facility for working capital purposes and for the short-term funding of our development and acquisition activity and, in certain instances, the repayment of other debt. Continuing ability to borrow under the revolving credit facility allows us to quickly capitalize on strategic opportunities at short-term interest rates. There was $75.5 million and $28.1 million outstanding under our revolving credit facility at June 30, 2012 and July 19, 2012, respectively. At both June 30, 2012 and July 19, 2012, we had $0.1 million of outstanding letters of credit, which reduces the availability on our revolving credit facility. As a result, the unused capacity of our revolving credit facility at June 30, 2012 and July 19, 2012 was $399.4 million and $446.8 million, respectively.

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

6. Mortgages and Notes Payable - Continued

In the second quarter of 2012, we repurchased $12.1 million principal amount of unsecured notes due March 2017 bearing interest of 5.85% for a purchase price of 107.5% of par value. We recorded $1.0 million of loss on debt extinguishment related to this repurchase.

In the first quarter of 2012, we obtained a $225.0 million, seven-year unsecured bank term loan bearing interest of LIBOR plus 190 basis points. This floating interest rate effectively was fixed by the interest rate swaps discussed in Note 7. The proceeds were used to pay off amounts then outstanding under our revolving credit facility.

We are currently in compliance with the debt covenants and other requirements with respect to our outstanding debt.

7. Derivative Financial Instruments

We have six floating-to-fixed interest rate swaps for seven-year periods each with respect to an aggregate of $225.0 million LIBOR-based borrowings. These swaps effectively fix the underlying LIBOR rate at a weighted average of 1.678%. The counterparties under the swaps are major financial institutions. The swap agreements contain a provision whereby if we default on any of our indebtedness, if greater than $10.0 million and that results in repayment of such indebtedness being, or becoming capable of being accelerated by the lender, then we could also be declared in default on our derivative obligations. These swaps have been designated as and are being accounted for as cash flow hedges with changes in fair value recorded in other comprehensive income each reporting period. No gain or loss was recognized related to hedge ineffectiveness or to amounts excluded from effectiveness testing on our cash flow hedges during the six months ended June 30, 2012. As of June 30, 2012, we have not posted any collateral related to our interest rate swap liability.

Amounts reported in accumulated other comprehensive loss ("AOCL") related to derivatives will be reclassified to interest expense as interest payments are made on our variable-rate debt. During the period from July 1, 2012 through June 30, 2013, we estimate that $3.1 million will be reclassified as an increase to interest expense.

The following table sets forth the fair value of our derivative instruments:

	June 30, 2012	December 31, 2011
Liability Derivatives:		
Derivatives designated as cash flow hedges in other liabilities:		
Interest rate swaps	$7,763	$ 2,202

The following table sets forth the effect of our cash flow hedges on AOCL and interest expense:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Derivatives Designated as Cash Flow Hedges:				
Amount of unrealized losses recognized in AOCL on derivatives (effective portion):				

Interest rate swaps	$(7,481)	$—	$(7,087)	$—
Amount of (gains)/losses reclassified out of AOCL into contractual interest expense (effective portion):				
Interest rate swaps	$782	$(29)	$1,459	$(58)

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8. Noncontrolling Interests

Noncontrolling Interests in the Operating Partnership

Noncontrolling interests in the Operating Partnership relate to the ownership of Common Units by various individuals and entities other than the Company. Net income attributable to noncontrolling interests in the Operating Partnership is computed by applying the weighted average percentage of Common Units not owned by the Company during the period, as a percent of the total number of outstanding Common Units, to the Operating Partnership's net income for the period after deducting distributions on Preferred Units.

The following table sets forth noncontrolling interests in the Operating Partnership:

	Six Months Ended June 30,	
	2012	2011
Beginning noncontrolling interests in the Operating Partnership	$110,655	$120,838
Adjustments of noncontrolling interests in the Operating Partnership to fair value	16,501	6,957
Conversion of Common Units to Common Stock	(631)	(635)
Net income attributable to noncontrolling interests in the Operating Partnership	1,513	1,130
Distributions to noncontrolling interests in the Operating Partnership	(3,158)	(3,215)
Total noncontrolling interests in the Operating Partnership	$124,880	$125,075

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Net income available for common stockholders	$12,962	$10,112	$29,656	$20,248
Increase in additional paid in capital from conversion of Common Units to Common Stock	568	449	631	635
Change from net income available for common stockholders and transfers from noncontrolling interests	$13,530	$10,561	$30,287	$20,883

Noncontrolling Interests in Consolidated Affiliates

At June 30, 2012, noncontrolling interests in consolidated affiliates relates to our joint venture partner's 50.0% interest in office properties located in Richmond, VA. Our joint venture partner is an unrelated third party.

9. Disclosure About Fair Value of Financial Instruments

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

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

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

Level 2. Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the related assets or liabilities.

9. Disclosure About Fair Value of Financial Instruments - Continued

Our Level 2 asset is the fair value of our mortgages and notes receivable, which was estimated by the income approach utilizing contractual cash flows and market-based interest rates to approximate the price that would be paid in an orderly transaction between market participants.

Our Level 2 liabilities include (1) the fair value of our mortgages and notes payable, which was estimated by the income approach utilizing contractual cash flows and market-based interest rates to approximate the price that would be paid in an orderly transaction between market participants and (2) interest rate swaps whose fair value is determined using the market standard methodology of netting the discounted future fixed cash receipts and the discounted expected variable cash payments. The variable cash payments of our interest rate swaps are based on the expectation of future LIBOR interest rates (forward curves) derived from observed market LIBOR interest rate curves. In addition, credit valuation adjustments are incorporated in the fair values to account for potential nonperformance risk, but were concluded to not be significant inputs to the calculation for the periods presented.

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

Our Level 3 assets include our tax increment financing bond, which is not routinely traded but whose fair value is determined by the income approach utilizing contractual cash flows and market-based interest rates to estimate the projected redemption value based on quoted bid/ask prices for similar unrated municipal bonds and, if any, real estate assets and for-sale residential condominiums recorded at fair value on a non-recurring basis as a result of our quarterly impairment analysis, which were valued using broker opinion of value and substantiated by internal cash flow projections.

Our Level 3 liability is the fair value of our financing obligations, which was estimated by the income approach to approximate the price that would be paid in an orderly transaction between market participants, utilizing: (1) contractual cash flows; (2) market-based interest rates; and (3) a number of other assumptions including demand for space, competition for customers, changes in market rental rates, costs of operation and expected ownership periods.

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

	June 30, 2012	Level 1 Quoted Prices in Active Markets for Identical Assets or Liabilities	Level 2 Significant Observable Inputs	Level 3 Significant Unobservable Inputs
Assets:				
Mortgages and notes receivable, at fair value (1)	$17,330	$—	$17,330	$ —
	3,099	3,099	—	—

Marketable securities of non-qualified deferred compensation plan (in prepaid expenses and other assets)				
Tax increment financing bond (in prepaid expenses and other assets)	15,371	—	—	15,371
Total Assets	$35,800	$3,099	$17,330	$ 15,371
Noncontrolling Interests in the Operating Partnership	$124,880	$124,880	$—	$ —
Liabilities:				
Mortgages and notes payable, at fair value (1)	$1,918,241	$—	$1,918,241	$ —
Interest rate swaps (in accounts payable, accrued expenses and other liabilities)	7,763	—	7,763	—
Non-qualified deferred compensation obligation (in accounts payable, accrued expenses and other liabilities)	3,099	3,099	—	—
Financing obligations, at fair value (1)	21,141	—	—	21,141
Total Liabilities	$1,950,244	$3,099	$1,926,004	$ 21,141

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9. Disclosure About Fair Value of Financial Instruments - Continued

	December 31, 2011	Level 1 Quoted Prices in Active Markets for Identical Assets or Liabilities	Level 2 Significant Observable Inputs	Level 3 Significant Unobservable Inputs
Assets:				
Mortgages and notes receivable, at fair value (1)	$ 18,990	$—	$ 18,990	$ —
Marketable securities of non-qualified deferred compensation plan (in prepaid expenses and other assets)	3,149	3,149	—	—
Tax increment financing bond (in prepaid expenses and other assets)	14,788	—	—	14,788
Impaired real estate assets and for-sale residential condominiums	12,767	—	—	12,767
Total Assets	$ 49,694	$ 3,149	$ 18,990	$ 27,555
Noncontrolling Interests in the Operating Partnership	$ 110,655	$ 110,655	$—	$ —
Liabilities:				
Mortgages and notes payable, at fair value (1)	$ 1,992,937	$—	$ 1,992,937	$ —
Interest rate swaps (in accounts payable, accrued expenses and other liabilities)	2,202	—	2,202	—
Non-qualified deferred compensation obligation (in accounts payable, accrued expenses and other liabilities)	3,149	3,149	—	—
Financing obligations, at fair value (1)	18,866	—	—	18,866
Total Liabilities	$ 2,017,154	$ 3,149	$ 1,995,139	$ 18,866

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(1) Amounts carried at historical cost on our Consolidated Balance Sheets at June 30, 2012 and December 31, 2011, respectively.

The following table sets forth the changes in our Level 3 asset, which is recorded at fair value on our Consolidated Balance Sheets on a recurring basis:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Asset:				
Tax Increment Financing Bond:				
Beginning balance	$ 15,075	$ 15,564	$ 14,788	$ 15,699
Unrealized gains/(losses) (in AOCL)	296	(336)	583	(471)
Ending balance	$ 15,371	$ 15,228	$ 15,371	$ 15,228

In 2007, we acquired a tax increment financing bond associated with a parking garage developed by us. This bond amortizes to maturity in 2020. The estimated fair value at June 30, 2012 was $1.7 million below the outstanding principal due on the bond. If the discount rate used to fair value this bond was 100 basis points higher or lower, the fair value of the bond would have been $0.6 million lower or $0.6 million higher, respectively, as of June 30, 2012. We intend to hold this bond and have concluded that we will not be required to sell this bond before recovery of the bond principal. Payment of the principal and interest for the bond is guaranteed by us. We have recorded no credit losses related to the bond during the three and six months ended June 30, 2012 and 2011. There is no legal right of offset with the liability, which we report as a financing obligation, related to this tax increment financing bond.

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

9. Disclosure About Fair Value of Financial Instruments - Continued

The following table sets forth quantitative information about the unobservable inputs of our Level 3 asset, which is recorded at fair value on our Consolidated Balance Sheets on a recurring basis:

	Fair Value at June 30, 2012	Valuation Technique	Unobservable Input	Discount Rate
Tax increment financing bond	$15,371	Income approach	Discount rate	9.85 %

10. Share-based Payments

During the six months ended June 30, 2012, we granted 190,886 stock options with an exercise price equal to the closing market price of a share of our Common Stock on the date of grant. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model, which resulted in a weighted average grant date fair value per share of $5.47. During the six months ended June 30, 2012, we also granted 90,983 shares of time-based restricted stock and 67,902 shares of total return-based restricted stock with weighted average grant date fair values per share of $32.27 and $38.71, respectively. We recorded stock-based compensation expense of $2.0 million and $1.4 million during the three months ended June 30, 2012 and 2011, respectively, and $4.5 million and $3.5 million during the six months ended June 30, 2012 and 2011, respectively. At June 30, 2012, there was $7.6 million of total unrecognized stock-based compensation costs, which will be recognized over a weighted average remaining contractual term of 2.6 years.

11. Accumulated Other Comprehensive Loss

The following table sets forth the components of accumulated other comprehensive loss:

	Six Months Ended June 30,	
	2012	2011
Tax increment financing bond:		
Beginning balance	$(2,309)	$(2,543)
Unrealized gains/(losses) on tax increment financing bond	583	(471)
Ending balance	(1,726)	(3,014)
Cash flow hedges:		
Beginning balance	(3,425)	(1,105)
Unrealized losses on cash flow hedges	(7,087)	—
Amortization of cash flow hedges	1,459	(58)
Ending balance	(9,053)	(1,163)
Total accumulated other comprehensive loss	$(10,779)	$(4,177)

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

12. Discontinued Operations

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Rental and other revenues	$2,044	$2,907	$4,383	$6,169
Operating expenses:				
Rental property and other expenses	966	1,390	2,084	2,862
Depreciation and amortization	322	778	1,008	1,653
Total operating expenses	1,288	2,168	3,092	4,515
Income from discontinued operations	756	739	1,291	1,654
Net gains on disposition of discontinued operations	1,385	—	6,519	—
Total discontinued operations	$2,141	$739	$7,810	$1,654

The following table sets forth the major classes of assets and liabilities of our real estate and other assets held for sale, net:

	June 30, 2012	December 31, 2011
Assets:		
Land	$3,849	$ 5,749
Buildings and tenant improvements	49,460	65,860
Accumulated depreciation	(18,743)	(23,917)
Net real estate assets	34,566	47,692
Accrued straight line rents receivable	1,490	1,726
Deferred leasing costs, net	678	811
Prepaid expenses and other assets	17	106
Real estate and other assets, net, held for sale	$36,751	$ 50,335
Tenant security deposits, deferred rents and accrued costs (1)	$595	$ 238

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

As of June 30, 2012, real estate and other assets held for sale, net, included five office properties in Nashville, TN and one office property in Kansas City, MO. As of December 31, 2011, real estate and other assets held for sale, net, included five office properties in Nashville, TN, one office property in Pinellas County, FL and one office property and 96 residential units in Kansas City, MO. All of these properties qualified for discontinued operations.

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13. Earnings Per Share

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Earnings per Common Share - basic:				
Numerator:				
Income from continuing operations	$12,357	$13,695	$25,020	$25,223
Net (income) attributable to noncontrolling interests in the Operating Partnership from continuing operations	(584)	(586)	(1,133)	(1,047)
Net (income) attributable to noncontrolling interests in consolidated affiliates from continuing operations	(223)	(182)	(407)	(305)
Dividends on Preferred Stock	(627)	(1,622)	(1,254)	(3,299)
Excess of Preferred Stock redemption/repurchase cost over carrying value	—	(1,895)	—	(1,895)
Income from continuing operations available for common stockholders	10,923	9,410	22,226	18,677
Income from discontinued operations	2,141	739	7,810	1,654
Net (income) attributable to noncontrolling interests in the Operating Partnership from discontinued operations	(102)	(37)	(380)	(83)
Income from discontinued operations available for common stockholders	2,039	702	7,430	1,571
Net income available for common stockholders	$12,962	$10,112	$29,656	$20,248
Denominator:				
Denominator for basic earnings per Common Share – weighted average shares (1) (2)	74,662	72,211	73,749	72,015
Earnings per Common Share - basic:				
Income from continuing operations available for common stockholders	$0.15	$0.13	$0.30	$0.26
Income from discontinued operations available for common stockholders	0.02	0.01	0.10	0.02
Net income available for common stockholders	$0.17	$0.14	$0.40	$0.28
Earnings per Common Share - diluted:				
Numerator:				
Income from continuing operations	$12,357	$13,695	$25,020	$25,223
Net (income) attributable to noncontrolling interests in consolidated affiliates from continuing operations	(223)	(182)	(407)	(305)
Dividends on Preferred Stock	(627)	(1,622)	(1,254)	(3,299)
Excess of Preferred Stock redemption/repurchase cost over carrying value	—	(1,895)	—	(1,895)
Income from continuing operations available for common stockholders before net (income) attributable to noncontrolling interests in the Operating Partnership	11,507	9,996	23,359	19,724
Income from discontinued operations available for common stockholders	2,141	739	7,810	1,654
Net income available for common stockholders before net (income) attributable to noncontrolling interests in the Operating Partnership	$13,648	$10,735	$31,169	$21,378
Denominator:				
	74,662	72,211	73,749	72,015

Denominator for basic earnings per Common Share –weighted average shares (1) (2)				
Add:				
Stock options using the treasury method	141	202	129	185
Noncontrolling interests Common Units	3,718	3,784	3,723	3,787
Denominator for diluted earnings per Common Share – adjusted weighted average shares and assumed conversions (1)	78,521	76,197	77,601	75,987
Earnings per Common Share - diluted:				
Income from continuing operations available for common stockholders	$0.15	$0.13	$0.30	$0.26
Income from discontinued operations available for common stockholders	0.02	0.01	0.10	0.02
Net income available for common stockholders	$0.17	$0.14	$0.40	$0.28

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13. Earnings Per Share - Continued

(1) There were 0.5 million and 0.3 million options outstanding during the three months ended June 30, 2012 and 2011, respectively, and 0.5 million and 0.6 million options outstanding during the six months ended June 30, 2012 and 2011, respectively, that were not included in the computation of diluted earnings per share because the impact of including such options would be anti-dilutive.

(2) Includes all unvested restricted stock since dividends on restricted stock are non-forfeitable.

14. Segment Information

The following table summarizes the rental and other revenues and net operating income, the primary industry property-level performance metric which is defined as rental and other revenues less rental property and other expenses, for each reportable segment:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Rental and Other Revenues: (1)				
Office:				
Atlanta, GA	$16,209	$12,341	$31,993	$24,242
Greenville, SC	3,489	3,437	6,993	6,942
Kansas City, MO	3,560	3,441	7,163	6,960
Memphis, TN	10,130	10,077	20,268	20,179
Nashville, TN	14,321	13,572	28,186	26,315
Orlando, FL	2,756	2,619	5,443	4,936
Piedmont Triad, NC	5,072	5,273	10,152	10,637
Pittsburgh, PA	9,113	—	18,199	—
Raleigh, NC	20,400	20,103	40,179	39,421
Richmond, VA	12,095	11,668	23,605	23,046
Tampa, FL	17,579	17,064	34,715	33,436
Total Office Segment	114,724	99,595	226,896	196,114
Industrial:				
Atlanta, GA	3,849	4,028	7,623	7,962
Piedmont Triad, NC	3,087	2,825	6,251	5,802
Total Industrial Segment	6,936	6,853	13,874	13,764
Retail:				
Kansas City, MO	9,075	8,203	17,998	17,103
Total Retail Segment	9,075	8,203	17,998	17,103
Total Rental and Other Revenues	$130,735	$114,651	$258,768	$226,981

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HIGHWOODS PROPERTIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(tabular dollar amounts in thousands, except per share data)

14. Segment Information - Continued

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Net Operating Income: (1)				
Office:				
Atlanta, GA	$10,426	$7,973	$20,821	$15,464
Greenville, SC	2,051	2,067	4,183	4,142
Kansas City, MO	2,186	2,112	4,518	4,256
Memphis, TN	5,841	5,462	11,942	11,222
Nashville, TN	9,835	9,369	19,490	18,001
Orlando, FL	1,431	1,284	2,847	2,450
Piedmont Triad, NC	3,219	3,452	6,452	7,053
Pittsburgh, PA	4,627	—	8,910	—
Raleigh, NC	14,291	14,273	28,146	27,489
Richmond, VA	8,536	8,231	16,419	16,090
Tampa, FL	10,811	10,557	21,650	20,684
Total Office Segment	73,254	64,780	145,378	126,851
Industrial:				
Atlanta, GA	2,761	3,001	5,649	5,840
Piedmont Triad, NC	2,308	2,107	4,596	4,331
Total Industrial Segment	5,069	5,108	10,245	10,171
Retail:				
Kansas City, MO	5,323	4,832	10,857	10,121
Total Retail Segment	5,323	4,832	10,857	10,121
Total Net Operating Income	83,646	74,720	166,480	147,143
Reconciliation to income from continuing operations before disposition of property and condominiums and equity in earnings of unconsolidated affiliates:				
Depreciation and amortization	(40,276)	(32,684)	(78,105)	(65,621)
General and administrative expense	(8,900)	(7,978)	(18,573)	(15,771)
Interest expense	(24,495)	(23,907)	(49,297)	(47,450)
Other income	764	1,875	2,994	3,748
Income from continuing operations before disposition of property and condominiums and equity in earnings of unconsolidated affiliates	$10,739	$12,026	$23,499	$22,049

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(1) Net of discontinued operations.

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15. Subsequent Events

In early July 2012, the Company issued 451,300 shares of Common Stock from sales in the second quarter of 2012 under our equity sales agreements at an average gross sales price of $33.52 per share raising net proceeds, after sales commissions and expenses, of $14.9 million.

On July 13, 2012, we acquired two medical office properties in Greensboro, NC for $16.4 million. The transaction included the issuance of approximately 77,000 Common Units. We expect to expense approximately $0.1 million of costs related to this acquisition.

On July 13, 2012, we sold five non-core office buildings in Nashville, TN for $41.0 million. We expect to record gain on disposition of discontinued operations of $6.8 million related to this disposition.

On July 25, 2012, we sold three GSA-leased buildings in Jackson, MS and Atlanta, GA for $86.5 million. We expect to record gain on disposition of discontinued operations of $14.0 million related to this disposition.

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HIGHWOODS REALTY LIMITED PARTNERSHIP
Consolidated Balance Sheets
(Unaudited and in thousands, except unit and per unit data)

	June 30, 2012	December 31, 2011
Assets:		
Real estate assets, at cost:		
Land	$366,925	$ 364,022
Buildings and tenant improvements	3,117,730	3,078,308
Development in process	6,094	—
Land held for development	102,482	105,206
	3,593,231	3,547,536
Less-accumulated depreciation	(913,016)	(877,383)
Net real estate assets	2,680,215	2,670,153
For-sale residential condominiums	2,434	4,751
Real estate and other assets, net, held for sale	36,751	50,335
Cash and cash equivalents	6,631	11,151
Restricted cash	20,757	26,666
Accounts receivable, net of allowance of $3,262 and $3,548, respectively	21,882	30,093
Mortgages and notes receivable, net of allowance of $118 and $61, respectively	17,056	18,600
Accrued straight-line rents receivable, net of allowance of $866 and $1,294, respectively	113,695	104,284
Investments in and advances to unconsolidated affiliates	76,037	99,296
Deferred financing and leasing costs, net of accumulated amortization of $70,572 and $62,319, respectively	126,680	127,774
Prepaid expenses and other assets	41,826	36,781
Total Assets	$3,143,964	$ 3,179,884
Liabilities, Redeemable Operating Partnership Units and Equity:		
Mortgages and notes payable	$1,823,128	$ 1,903,213
Accounts payable, accrued expenses and other liabilities	137,047	148,821
Financing obligations	30,822	31,444
Total Liabilities	1,990,997	2,083,478
Commitments and contingencies		
Redeemable Operating Partnership Units:		
Common Units, 3,711,152 and 3,729,518 outstanding, respectively	124,880	110,655
Series A Preferred Units (liquidation preference $1,000 per unit), 29,077 units issued and outstanding	29,077	29,077
Total Redeemable Operating Partnership Units	153,957	139,732
Equity:		
Common Units:		
General partner Common Units, 789,216 and 759,684 outstanding, respectively	10,049	9,575
Limited partner Common Units, 74,421,263 and 71,479,204 outstanding, respectively	995,147	948,187
Accumulated other comprehensive loss	(10,779)	(5,734)
Noncontrolling interests in consolidated affiliates	4,593	4,646
Total Equity	999,010	956,674
Total Liabilities, Redeemable Operating Partnership Units and Equity	$3,143,964	$ 3,179,884

See accompanying notes to consolidated financial statements.

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HIGHWOODS REALTY LIMITED PARTNERSHIP
Consolidated Statements of Income
(Unaudited and in thousands, except per unit amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Rental and other revenues	$130,735	$114,651	$258,768	$226,981
Operating expenses:				
Rental property and other expenses	47,030	39,868	92,167	79,924
Depreciation and amortization	40,276	32,684	78,105	65,621
General and administrative	8,959	8,041	18,694	15,685
Total operating expenses	96,265	80,593	188,966	161,230
Interest expense:				
Contractual	23,643	22,940	47,591	45,371
Amortization of deferred financing costs	900	821	1,802	1,642
Financing obligations	(48)	146	(96)	437
	24,495	23,907	49,297	47,450
Other income:				
Interest and other income	1,737	1,899	3,967	3,772
Losses on debt extinguishment	(973)	(24)	(973)	(24)
	764	1,875	2,994	3,748
Income from continuing operations before disposition of property and condominiums and equity in earnings of unconsolidated affiliates	10,739	12,026	23,499	22,049
Gains on disposition of property	—	200	—	200
Gains on for-sale residential condominiums	110	116	175	154
Equity in earnings of unconsolidated affiliates	1,511	1,357	1,351	2,832
Income from continuing operations	12,360	13,699	25,025	25,235
Discontinued operations:				
Income from discontinued operations	756	739	1,291	1,654
Net gains on disposition of discontinued operations	1,385	—	6,519	—
	2,141	739	7,810	1,654
Net income	14,501	14,438	32,835	26,889
Net (income) attributable to noncontrolling interests in consolidated affiliates	(223)	(182)	(407)	(305)
Distributions on Preferred Units	(627)	(1,622)	(1,254)	(3,299)
Excess of Preferred Unit redemption/repurchase cost over carrying value	—	(1,895)	—	(1,895)
Net income available for common unitholders	$13,651	$10,739	$31,174	$21,390
Earnings per Common Unit – basic:				
Income from continuing operations available for common unitholders	$0.15	$0.13	$0.30	$0.26
Income from discontinued operations available for common unitholders	0.03	0.01	0.10	0.02
Net income available for common unitholders	$0.18	$0.14	$0.40	$0.28
Weighted average Common Units outstanding – basic	77,971	75,586	77,063	75,393
Earnings per Common Unit – diluted:				
Income from continuing operations available for common unitholders	$0.15	$0.13	$0.30	$0.26
Income from discontinued operations available for common unitholders	0.02	0.01	0.10	0.02
Net income available for common unitholders	$0.17	$0.14	$0.40	$0.28

Weighted average Common Units outstanding – diluted	78,112	75,788	77,192	75,578
Distributions declared per Common Unit	$0.425	$0.425	$0.850	$0.850
Net income available for common unitholders:				
Income from continuing operations available for common unitholders	$11,510	$10,000	$23,364	$19,736
Income from discontinued operations available for common unitholders	2,141	739	7,810	1,654
Net income available for common unitholders	$13,651	$10,739	$31,174	$21,390

See accompanying notes to consolidated financial statements.

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HIGHWOODS REALTY LIMITED PARTNERSHIP
Consolidated Statements of Comprehensive Income
(Unaudited and in thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Other comprehensive income/(loss):				
Net income	$14,501	$14,438	$32,835	$26,889
Other comprehensive income/(loss):				
Unrealized gains/(losses) on tax increment financing bond	296	(336)	583	(471)
Unrealized losses on cash flow hedges	(7,481)	—	(7,087)	—
Amortization of cash flow hedges	782	(29)	1,459	(58)
Total other comprehensive loss	(6,403)	(365)	(5,045)	(529)
Total comprehensive income	$8,098	$14,073	$27,790	$26,360
Less-comprehensive (income) attributable to noncontrolling interests	(223)	(182)	(407)	(305)
Comprehensive income attributable to the Operating Partnership	$7,875	$13,891	$27,383	$26,055

See accompanying notes to consolidated financial statements.

HIGHWOODS REALTY LIMITED PARTNERSHIP
Consolidated Statements of Capital
(Unaudited and in thousands, except unit amounts)

	Common Units General Partners' Capital	Common Units Limited Partners' Capital	Accumulated Other Comprehensive Loss	Noncontrolling Interests in Consolidated Affiliates	Total Partners' Capital
Balance at December 31, 2011	$9,575	$948,187	$ (5,734)	$ 4,646	$956,674
Issuances of Common Units, net	918	90,918	—	—	91,836
Distributions paid on Common Units	(656)	(64,941)	—	—	(65,597)
Distributions paid on Preferred Units	(13)	(1,241)	—	—	(1,254)
Share-based compensation expense	45	4,414	—	—	4,459
Distribution to noncontrolling interests in consolidated affiliates	—	—	—	(460)	(460)
Adjustment of Redeemable Common Units to fair value and contributions/distributions from/to the General Partner	(144)	(14,294)	—	—	(14,438)
Net (income) attributable to noncontrolling interests in consolidated affiliates	(4)	(403)		407	—
Comprehensive income:					
Net income	328	32,507	—	—	32,835
Other comprehensive loss	—	—	(5,045)	—	(5,045)
Total comprehensive income					27,790
Balance at June 30, 2012	$10,049	$995,147	$ (10,779)	$ 4,593	$999,010

	Common Units General Partners' Capital	Common Units Limited Partners' Capital	Accumulated Other Comprehensive Loss	Noncontrolling Interests in Consolidated Affiliates	Total Partners' Capital
Balance at December 31, 2010	$10,044	$994,610	$ (3,648)	$ 4,460	$1,005,466
Issuances of Common Units, net	170	16,814	—	—	16,984
Distributions paid on Common Units	(640)	(63,296)	—	—	(63,936)
Distributions paid on Preferred Units	(33)	(3,266)	—	—	(3,299)
Share-based compensation expense	35	3,418	—	—	3,453
Distribution to noncontrolling interests in consolidated affiliates	—	—	—	(319)	(319)
Adjustment of Redeemable Common Units to fair value and contributions/distributions from/to the General Partner	(48)	(4,769)	—	—	(4,817)
Net (income) attributable to noncontrolling interests in consolidated affiliates	(3)	(302)	—	305	—
Comprehensive income/(loss):					
Net income	269	26,620	—	—	26,889
Other comprehensive loss	—	—	(529)	—	(529)
Total comprehensive income					26,360
Balance at June 30, 2011	$9,794	$969,829	$ (4,177)	$ 4,446	$979,892

See accompanying notes to consolidated financial statements.

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HIGHWOODS REALTY LIMITED PARTNERSHIP
Consolidated Statements of Cash Flows
(Unaudited and in thousands)

	Six Months Ended June 30,	
	2012	2011
Operating activities:		
Net income	$32,835	$26,889
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	79,113	67,274
Amortization of lease incentives and acquisition-related intangible assets and liabilities	180	968
Share-based compensation expense	4,459	3,453
Allowance for losses on accounts and accrued straight-line rents receivable	538	1,029
Amortization of deferred financing costs	1,802	1,642
Amortization of cash flow hedges	1,459	(58)
Losses on debt extinguishment	973	24
Net gains on disposition of property	(6,519)	(200)
Gains on for-sale residential condominiums	(175)	(154)
Equity in earnings of unconsolidated affiliates	(1,351)	(2,832)
Changes in financing obligations	(584)	(245)
Distributions of earnings from unconsolidated affiliates	2,211	2,150
Changes in operating assets and liabilities:		
Accounts receivable	7,298	(1,821)
Prepaid expenses and other assets	(3,077)	(544)
Accrued straight-line rents receivable	(9,415)	(6,098)
Accounts payable, accrued expenses and other liabilities	(16,413)	(3,794)
Net cash provided by operating activities	93,334	87,683
Investing activities:		
Investment in acquired real estate and related intangible assets, net of cash acquired	—	(7,761)
Investment in development in process	(1,531)	(2,598)
Investment in tenant improvements and deferred leasing costs	(43,851)	(28,456)
Investment in building improvements	(19,758)	(5,632)
Net proceeds from disposition of real estate assets	19,898	2,063
Net proceeds from disposition of for-sale residential condominiums	2,492	2,401
Distributions of capital from unconsolidated affiliates	901	632
Repayments of mortgages and notes receivable	1,544	235
Investments in and advances to unconsolidated affiliates	(2,750)	(39,402)
Changes in restricted cash and other investing activities	4,031	(395)
Net cash used in investing activities	(39,024)	(78,913)
Financing activities:		
Distributions on Common Units	(65,597)	(63,936)
Redemptions/repurchases of Preferred Units	—	(52,505)
Distributions on Preferred Units	(1,254)	(3,299)
Distributions to noncontrolling interests in consolidated affiliates	(460)	(319)
Proceeds from the issuance of Common Units	95,289	16,984
Costs paid for the issuance of Common Units	(1,316)	—
Repurchase of units related to tax withholdings	(2,137)	—
Borrowings on revolving credit facility	106,300	124,700
Repayments of revolving credit facility	(392,800)	(79,300)
Borrowings on mortgages and notes payable	225,000	200,000

Repayments of mortgages and notes payable	(19,359)	(153,522)
Payments on financing obligations	(38)	—
Additions to deferred financing costs and other financing activities	(2,458)	(2,684)
Net cash used in financing activities	(58,830)	(13,881)
Net decrease in cash and cash equivalents	(4,520)	(5,111)
Cash and cash equivalents at beginning of the period	11,151	14,198
Cash and cash equivalents at end of the period	$6,631	$9,087

See accompanying notes to consolidated financial statements.

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HIGHWOODS REALTY LIMITED PARTNERSHIP
Consolidated Statements of Cash Flows - Continued
(Unaudited and in thousands)

Supplemental disclosure of cash flow information:

	Six Months Ended June 30,	
	2012	2011
Cash paid for interest, net of amounts capitalized	$48,063	$44,948

Supplemental disclosure of non-cash investing and financing activities:

	Six Months Ended June 30,	
	2012	2011
Unrealized losses on cash flow hedges	$(7,087)	$—
Changes in accrued capital expenditures	(2,448)	1,525
Write-off of fully depreciated real estate assets	28,629	23,352
Write-off of fully amortized deferred financing and leasing costs	8,765	8,247
Unrealized gains on marketable securities of non-qualified deferred compensation plan	216	210
Adjustment of Redeemable Common Units to fair value	14,225	4,237
Unrealized gains/(losses) on tax increment financing bond	583	(471)
Reduction of advances to unconsolidated affiliates related to acquisition activities	26,000	—

See accompanying notes to consolidated financial statements.

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HIGHWOODS REALTY LIMITED PARTNERSHIP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2012
(tabular dollar amounts in thousands, except per unit data)
(Unaudited)

1. Description of Business and Significant Accounting Policies

Description of Business

Highwoods Properties, Inc., together with its consolidated subsidiaries (the “Company”), is a fully-integrated, self-administered and self-managed equity real estate investment trust (“REIT”) that provides leasing, management, development, construction and other customer-related services for its properties and for third parties. The Company conducts virtually all of its activities through Highwoods Realty Limited Partnership (the “Operating Partnership”). At June 30, 2012, the Company and/or the Operating Partnership wholly owned: 304 in-service office, industrial and retail properties, comprising 29.5 million square feet; nine for-sale residential condominiums; 581 acres of undeveloped land suitable for future development, of which 518 acres are considered core assets; and one office property under development.

The Company is the sole general partner of the Operating Partnership. At June 30, 2012, the Company owned all of the Preferred Units and 75.2 million, or 95.3%, of the Common Units in the Operating Partnership. Limited partners, including one officer and two directors of the Company, own the remaining 3.7 million Common Units. In the event the Company issues shares of Common Stock, the net proceeds are contributed to the Operating Partnership in exchange for additional Common Units. Generally, the Operating Partnership is required to redeem each Common Unit at the request of the holder thereof for cash equal to the value of one share of the Company’s Common Stock, $0.01 par value, based on the average of the market price for the 10 trading days immediately preceding the notice date of such redemption, provided that the Company at its option may elect to acquire any such Common Units presented for redemption for cash or one share of Common Stock. The Common Units owned by the Company are not redeemable. During the six months ended June 30, 2012, the Company redeemed 18,366 Common Units for a like number of shares of Common Stock. The redemptions, in conjunction with the proceeds from issuances of Common Stock contributed to the Operating Partnership in exchange for additional Common Units, increased the percentage of Common Units owned by the Company from 95.1% at December 31, 2011 to 95.3% at June 30, 2012.

Common Stock Offerings

The Company has entered into equity sales agreements with various financial institutions to offer and sell, from time to time, shares of its Common Stock by means of ordinary brokers' transactions on the New York Stock Exchange or otherwise at market prices prevailing at the time of sale, at prices related to prevailing market prices or at negotiated prices or as otherwise agreed with any of the institutions. During the three and six months ended June 30, 2012, the Company issued 1,836,976 and 2,622,476 shares, respectively, of Common Stock under these agreements at an average gross sales price of $33.72 and $33.45 per share, respectively, raising net proceeds, after sales commissions and expenses, of $61.0 million and $86.4 million, respectively.

Basis of Presentation

Our Consolidated Financial Statements are prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”). Our Consolidated Balance Sheet at December 31, 2011 was revised from previously reported amounts to reflect in real estate and other assets, net, held for sale those properties which qualified as held for sale during the three months ended June 30, 2012. Our Consolidated Statements of Income for the three and six months ended June 30, 2011 were revised from previously reported amounts to reflect in discontinued operations the operations for those properties that qualified for discontinued operations. Prior period amounts related to capital expenditures in our Consolidated Statements of Cash Flows have been reclassified to conform to the current period presentation.

Our Consolidated Financial Statements include wholly owned subsidiaries and those entities in which we have the controlling financial interest. All intercompany transactions and accounts have been eliminated. At June 30, 2012 and December 31, 2011, we had involvement with no entities that we concluded to be variable interest entities.

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1. Description of Business and Significant Accounting Policies – Continued

The unaudited interim consolidated financial statements and accompanying unaudited consolidated financial information, in the opinion of management, contain all adjustments (including normal recurring accruals) necessary for a fair presentation of our financial position, results of operations and cash flows. We have omitted certain notes and other information from the interim consolidated financial statements presented in this Quarterly Report on Form 10-Q as permitted by SEC rules and regulations. These Consolidated Financial Statements should be read in conjunction with our 2011 Annual Report on Form 10-K.

Use of Estimates

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

Recently Issued Accounting Standards

As a result of adopting certain new or amended accounting pronouncements in the first quarter of 2012, we have enhanced our disclosure of assets and liabilities measured at fair value and elected to continue use of credit valuation adjustments on a net basis by counterparty as part of the calculation to determine the fair value of our derivatives. Our disclosures now include: (1) significant transfers between Levels 1 and 2 of the fair value hierarchy, if any; (2) additional quantitative and qualitative information regarding fair value measurements categorized as Level 3 of the fair value hierarchy; and (3) the hierarchy classification for items whose fair value is not recorded on our Consolidated Balance Sheets but was disclosed previously in our Notes to Consolidated Financial Statements. Additionally, we have presented comprehensive income in a separate financial statement entitled Consolidated Statements of Comprehensive Income.

2. Real Estate Assets

Acquisitions

During the second quarter of 2012, we acquired a 178,300 square foot office property in Cary, NC from our DLF I joint venture for an agreed upon value of $26.0 million by reducing the balance of the advance due to us from the joint venture.

Dispositions

During the second quarter of 2012, we sold a non-core office property in Pinellas County, FL for gross proceeds of $9.5 million. We recorded gain on disposition of discontinued operations of $1.4 million related to this disposition.

During the first quarter of 2012, we sold 96 vacant rental residential units in Kansas City, MO for gross proceeds of $11.0 million. We recorded gain on disposition of discontinued operations of $5.1 million related to this disposition.

3. Mortgages and Notes Receivable

The following table sets forth our mortgages and notes receivable:

	June 30, 2012	December 31, 2011
Seller financing (first mortgages)	$15,853	$ 17,180
Less allowance	—	—
	15,853	17,180
Promissory notes	1,321	1,481
Less allowance	(118)	(61)
	1,203	1,420
Mortgages and notes receivable, net	$17,056	$ 18,600

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

3. Mortgages and Notes Receivable - Continued

Our mortgages and notes receivable consist primarily of seller financing issued in conjunction with two disposition transactions in 2010. This seller financing is evidenced by first mortgages secured by the assignment of rents and the underlying real estate assets. We evaluate the collectibility of the receivables by monitoring the leasing statistics and market fundamentals of these assets. As of June 30, 2012, the payments on both mortgages receivable were current and there were no other indications of impairment on the receivables. We may be required to take impairment charges in the future if and to the extent the underlying collateral diminishes in value.

The following table sets forth our notes receivable allowance, which relates only to promissory notes:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Beginning notes receivable allowance	$122	$497	$61	$868
Bad debt expense	—	162	—	184
Recoveries/write-offs/other	(4)	(42)	57	(435)
Total notes receivable allowance	$118	$617	$118	$617

4. Investments in and Advances to Affiliates

Unconsolidated Affiliates

We have equity interests of up to 50.0% in various joint ventures with unrelated third parties and a secured debt interest in one of those joint ventures, as described below. The following table sets forth the combined, summarized income statements for our unconsolidated joint ventures on the purchase accounting basis:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Income Statements:				
Rental and other revenues	$25,057	$23,756	$48,854	$47,958
Expenses:				
Rental property and other expenses	12,076	10,155	22,877	21,526
Depreciation and amortization	5,607	6,053	11,861	12,299
Impairment of real estate assets	—	—	7,180	—
Interest expense	5,103	5,683	10,766	11,508
Total expenses	22,786	21,891	52,684	45,333
Income/(loss) before disposition of properties	2,271	1,865	(3,830)	2,625
Gains on disposition of properties	6,275	—	6,275	—
Net income	$8,546	$1,865	$2,445	$2,625
Our share of:				
Depreciation and amortization of real estate assets	$1,636	$1,995	$3,695	$4,050
Impairment of real estate assets	$—	$—	$1,002	$—
Interest expense	$1,823	$2,012	$3,782	$4,149

Net income	$1,142	$759	$356	$1,694
Our share of net income	$1,142	$759	$356	$1,694
Management and other fees adjustments	369	598	995	1,138
Equity in earnings of unconsolidated affiliates	$1,511	$1,357	$1,351	$2,832

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HIGHWOODS REALTY LIMITED PARTNERSHIP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(tabular dollar amounts in thousands, except per unit data)

4. Investments in and Advances to Affiliates - Continued

In 2011, we provided a $38.3 million interest-only secured loan to our DLF I joint venture that originally was scheduled to mature in March 2012. The loan bears interest at LIBOR plus 500 basis points. The maturity date of the loan has been extended to September 30, 2012. In the second quarter of 2012, we acquired an office property from the joint venture by reducing the balance of the advance due to us from the joint venture. We deferred our share of the gain recorded by the joint venture related to this transaction. We recorded interest income from this loan in interest and other income of $0.2 million and $0.3 million during the three months ended June 30, 2012 and 2011, respectively, and $0.7 million and $0.3 million during the six months ended June 30, 2012 and 2011, respectively.

In the second quarter of 2012, our DLF II joint venture obtained a $50.0 million, three-year secured mortgage loan from a third party lender, bearing a fixed interest rate of 3.5% on $39.1 million of the loan and a floating interest rate of LIBOR plus 250 basis points on $10.9 million of the loan, which was used by the joint venture to repay a secured loan at maturity to a third party lender.

During the first quarter of 2012, we recorded $1.0 million as our share of impairment of real estate assets on two office properties in our DLF I joint venture, due to a decline in projected occupancy and a change in the assumed holding period of those assets, which reduced the expected future cash flows from the properties.

5. Intangible Assets and Below Market Lease Liabilities

The following table sets forth total intangible assets and acquisition-related below market lease liabilities, net of accumulated amortization:

	June 30, 2012	December 31, 2011
Assets:		
Deferred financing costs	$20,112	$18,044
Less accumulated amortization	(7,488)	(5,797)
	12,624	12,247
Deferred leasing costs (including lease incentives and acquisition-related intangible assets)	177,140	172,049
Less accumulated amortization	(63,084)	(56,522)
	114,056	115,527
Deferred financing and leasing costs, net	$126,680	$127,774
Liabilities (in accounts payable, accrued expenses and other liabilities):		
Acquisition-related below market lease liabilities	$16,346	$16,441
Less accumulated amortization	(1,966)	(971)
	$14,380	$15,470

The following table sets forth amortization of intangible assets and acquisition-related below market lease liabilities:

	Three Months Ended June 30,	Six Months Ended June 30,

	2012	2011	2012	2011
Amortization of deferred financing costs	$900	$821	$1,802	$1,642
Amortization of deferred leasing costs and acquisition-related intangible assets (in depreciation and amortization)	$7,266	$4,401	$13,706	$8,757
Amortization of lease incentives (in rental and other revenues)	$340	$303	$683	$641
Amortization of acquisition-related intangible assets (in rental and other revenues)	$324	$191	$594	$377
Amortization of acquisition-related below market lease liabilities (in rental and other revenues)	$(553)	$(25)	$(1,097)	$(50)

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HIGHWOODS REALTY LIMITED PARTNERSHIP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(tabular dollar amounts in thousands, except per unit data)

5. Intangible Assets and Below Market Lease Liabilities - Continued

The following table sets forth scheduled future amortization of intangible assets and below market lease liabilities:

	Amortization of Deferred Financing Costs	Amortization of Deferred Leasing Costs and Acquisition-Related Intangible Assets (in Depreciation and Amortization)	Amortization of Lease Incentives (in Rental and Other Revenues)	Amortization of Acquisition-Related Intangible Assets (in Rental and Other Revenues)	Amortization of Acquisition-Related Below Market Lease Liabilities (in Rental and Other Revenues)
July 1, 2012 through December 31, 2012	$2,234	$ 14,242	$772	$ 579	$ (1,229)
2013	3,262	21,834	1,167	765	(2,081)
2014	2,987	17,877	1,013	504	(2,005)
2015	2,264	13,879	779	328	(1,768)
2016	957	10,880	608	280	(1,498)
Thereafter	920	25,453	2,379	717	(5,799)
	$12,624	$ 104,165	$6,718	$ 3,173	$ (14,380)

The weighted average remaining amortization periods for deferred financing costs, deferred leasing costs and acquisition-related intangible assets (in depreciation and amortization), lease incentives (in rental and other revenues), acquisition-related intangible assets (in rental and other revenues) and acquisition-related below market lease liabilities (in rental and other revenues) were 3.8 years, 6.2 years, 7.8 years, 5.7 years and 8.9 years, respectively, as of June 30, 2012.

In connection with the acquisition of an office property in Cary, NC in the second quarter of 2012, we recorded $2.7 million of in-place lease intangible assets with a weighted average amortization period of 6.3 years at the date of the acquisition. The contractual rents of the in-place lease acquired were determined to be at market.

6. Mortgages and Notes Payable

The following table sets forth our mortgages and notes payable:

	June 30, 2012	December 31, 2011
Secured indebtedness	$743,492	$ 750,049
Unsecured indebtedness	1,079,636	1,153,164
Total mortgages and notes payable	$1,823,128	$ 1,903,213

At June 30, 2012, our secured mortgage loans were secured by real estate assets with an aggregate undepreciated book value of $1,237.7 million.

Our $475.0 million unsecured revolving credit facility is scheduled to mature on July 27, 2015 and includes an accordion feature that allows for an additional $75.0 million of borrowing capacity subject to additional lender commitments. Assuming no defaults have occurred, we have an option to extend the maturity for an additional year. The interest rate at our current credit ratings is LIBOR plus 150 basis points and the annual facility fee is 35 basis points. The interest rate and facility fee are based on the higher of the publicly announced ratings from Moody's Investors Service or Standard & Poor's Ratings Services. We use our revolving credit facility for working capital purposes and for the short-term funding of our development and acquisition activity and, in certain instances, the repayment of other debt. Continuing ability to borrow under the revolving credit facility allows us to quickly capitalize on strategic opportunities at short-term interest rates. There was $75.5 million and $28.1 million outstanding under our revolving credit facility at June 30, 2012 and July 19, 2012, respectively. At both June 30, 2012 and July 19, 2012, we had $0.1 million of outstanding letters of credit, which reduces the availability on our revolving credit facility. As a result, the unused capacity of our revolving credit facility at June 30, 2012 and July 19, 2012 was $399.4 million and $446.8 million, respectively.

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HIGHWOODS REALTY LIMITED PARTNERSHIP
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(tabular dollar amounts in thousands, except per unit data)

6. Mortgages and Notes Payable - Continued

In the second quarter of 2012, we repurchased $12.1 million principal amount of unsecured notes due March 2017 bearing interest of 5.85% for a purchase price of 107.5% of par value. We recorded $1.0 million of loss on debt extinguishment related to this repurchase.

In the first quarter of 2012, we obtained a $225.0 million, seven-year unsecured bank term loan bearing interest of LIBOR plus 190 basis points. This floating interest rate effectively was fixed by the interest rate swaps discussed in Note 7. The proceeds were used to pay off amounts then outstanding under our revolving credit facility.

We are currently in compliance with the debt covenants and other requirements with respect to our outstanding debt.

7. Derivative Financial Instruments

We have six floating-to-fixed interest rate swaps for seven-year periods each with respect to an aggregate of $225.0 million LIBOR-based borrowings. These swaps effectively fix the underlying LIBOR rate at a weighted average of 1.678%. The counterparties under the swaps are major financial institutions. The swap agreements contain a provision whereby if we default on any of our indebtedness, if greater than $10.0 million and that results in repayment of such indebtedness being, or becoming capable of being accelerated by the lender, then we could also be declared in default on our derivative obligations. These swaps have been designated as and are being accounted for as cash flow hedges with changes in fair value recorded in other comprehensive income each reporting period. No gain or loss was recognized related to hedge ineffectiveness or to amounts excluded from effectiveness testing on our cash flow hedges during the six months ended June 30, 2012. As of June 30, 2012, we have not posted any collateral related to our interest rate swap liability.

Amounts reported in accumulated other comprehensive loss ("AOCL") related to derivatives will be reclassified to interest expense as interest payments are made on our variable-rate debt. During the period from July 1, 2012 through June 30, 2013, we estimate that $3.1 million will be reclassified as an increase to interest expense.

The following table sets forth the fair value of our derivative instruments:

	June 30, 2012	December 31, 2011
Liability Derivatives:		
Derivatives designated as cash flow hedges in other liabilities:		
Interest rate swaps	$7,763	$ 2,202

The following table sets forth the effect of our cash flow hedges on AOCL and interest expense:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Derivatives Designated as Cash Flow Hedges:				
Amount of unrealized losses recognized in AOCL on derivatives (effective portion):				

Interest rate swaps	$(7,481)	$—	$(7,087)	$—
Amount of (gains)/losses reclassified out of AOCL into contractual interest expense (effective portion):				
Interest rate swaps	$782	$(29)	$1,459	$(58)

8. Noncontrolling Interests

Noncontrolling Interests in Consolidated Affiliates

At June 30, 2012, noncontrolling interests in consolidated affiliates relates to our joint venture partner's 50.0% interest in office properties located in Richmond, VA. Our joint venture partner is an unrelated third party.

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9. Disclosure About Fair Value of Financial Instruments

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

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

Our Level 1 assets are investments in marketable securities that we use to pay benefits under our non-qualified deferred compensation plan. Our Level 1 liability is our non-qualified deferred compensation obligation.

Level 2. Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the related assets or liabilities.

Our Level 2 asset is the fair value of our mortgages and notes receivable, which was estimated by the income approach utilizing contractual cash flows and market-based interest rates to approximate the price that would be paid in an orderly transaction between market participants.

Our Level 2 liabilities include (1) the fair value of our mortgages and notes payable, which was estimated by the income approach utilizing contractual cash flows and market-based interest rates to approximate the price that would be paid in an orderly transaction between market participants and (2) interest rate swaps whose fair value is determined using the market standard methodology of netting the discounted future fixed cash receipts and the discounted expected variable cash payments. The variable cash payments of our interest rate swaps are based on the expectation of future LIBOR interest rates (forward curves) derived from observed market LIBOR interest rate curves. In addition, credit valuation adjustments are incorporated in the fair values to account for potential nonperformance risk, but were concluded to not be significant inputs to the calculation for the periods presented.

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

Our Level 3 assets include our tax increment financing bond, which is not routinely traded but whose fair value is determined by the income approach utilizing contractual cash flows and market-based interest rates to estimate the projected redemption value based on quoted bid/ask prices for similar unrated municipal bonds and, if any, real estate assets and for-sale residential condominiums recorded at fair value on a non-recurring basis as a result of our quarterly impairment analysis, which were valued using broker opinion of value and substantiated by internal cash flow projections.

Our Level 3 liability is the fair value of our financing obligations, which was estimated by the income approach to approximate the price that would be paid in an orderly transaction between market participants, utilizing: (1) contractual cash flows; (2) market-based interest rates; and (3) a number of other assumptions including demand for space, competition for customers, changes in market rental rates, costs of operation and expected ownership periods.

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HIGHWOODS REALTY LIMITED PARTNERSHIP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(tabular dollar amounts in thousands, except per unit data)

9. Disclosure About Fair Value of Financial Instruments - Continued

The following tables set forth the assets and liabilities that we measure at fair value by level within the fair value hierarchy. We determine the level based on the lowest level of substantive input used to determine fair value.

	June 30, 2012	Level 1 Quoted Prices in Active Markets for Identical Assets or Liabilities	Level 2 Significant Observable Inputs	Level 3 Significant Unobservable Inputs
Assets:				
Mortgages and notes receivable, at fair value (1)	$17,330	$—	$17,330	$ —
Marketable securities of non-qualified deferred compensation plan (in prepaid expenses and other assets)	3,099	3,099	—	—
Tax increment financing bond (in prepaid expenses and other assets)	15,371	—	—	15,371
Total Assets	$35,800	$3,099	$17,330	$ 15,371
Liabilities:				
Mortgages and notes payable, at fair value (1)	$1,918,241	$—	$1,918,241	$ —
Interest rate swaps (in accounts payable, accrued expenses and other liabilities)	7,763	—	7,763	—
Non-qualified deferred compensation obligation (in accounts payable, accrued expenses and other liabilities)	3,099	3,099	—	—
Financing obligations, at fair value (1)	21,141	—	—	21,141
Total Liabilities	$1,950,244	$3,099	$1,926,004	$ 21,141

	December 31, 2011	Level 1 Quoted Prices in Active Markets for Identical Assets or Liabilities	Level 2 Significant Observable Inputs	Level 3 Significant Unobservable Inputs
Assets:				
Mortgages and notes receivable, at fair value (1)	$ 18,990	$—	$18,990	$ —
Marketable securities of non-qualified deferred compensation plan (in prepaid expenses and other assets)	3,149	3,149	—	—
Tax increment financing bond (in prepaid expenses and other assets)	14,788	—	—	14,788

Impaired real estate assets and for-sale residential condominiums	12,767	—	—	12,767
Total Assets	$ 49,694	$ 3,149	$ 18,990	$ 27,555
Liabilities:				
Mortgages and notes payable, at fair value (1)	$ 1,992,937	$—	$ 1,992,937	$ —
Interest rate swaps (in accounts payable, accrued expenses and other liabilities)	2,202	—	2,202	—
Non-qualified deferred compensation obligation (in accounts payable, accrued expenses and other liabilities)	3,149	3,149	—	—
Financing obligations, at fair value (1)	18,866	—	—	18,866
Total Liabilities	$ 2,017,154	$ 3,149	$ 1,995,139	$ 18,866

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(1) Amounts carried at historical cost on our Consolidated Balance Sheets at June 30, 2012 and December 31, 2011, respectively.

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HIGHWOODS REALTY LIMITED PARTNERSHIP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(tabular dollar amounts in thousands, except per unit data)

9. Disclosure About Fair Value of Financial Instruments - Continued

The following table sets forth the changes in our Level 3 asset, which is recorded at fair value on our Consolidated Balance Sheets on a recurring basis:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Asset:				
Tax Increment Financing Bond:				
Beginning balance	$15,075	$15,564	$14,788	$15,699
Unrealized gains/(losses) (in AOCL)	296	(336)	583	(471)
Ending balance	$15,371	$15,228	$15,371	$15,228

In 2007, we acquired a tax increment financing bond associated with a parking garage developed by us. This bond amortizes to maturity in 2020. The estimated fair value at June 30, 2012 was $1.7 million below the outstanding principal due on the bond. If the discount rate used to fair value this bond was 100 basis points higher or lower, the fair value of the bond would have been $0.6 million lower or $0.6 million higher, respectively, as of June 30, 2012. We intend to hold this bond and have concluded that we will not be required to sell this bond before recovery of the bond principal. Payment of the principal and interest for the bond is guaranteed by us. We have recorded no credit losses related to the bond during the three and six months ended June 30, 2012 and 2011. There is no legal right of offset with the liability, which we report as a financing obligation, related to this tax increment financing bond.

The following table sets forth quantitative information about the unobservable inputs of our Level 3 asset, which is recorded at fair value on our Consolidated Balance Sheets on a recurring basis:

	Fair Value at June 30, 2012	Valuation Technique	Unobservable Input	Discount Rate
Tax increment financing bond	$15,371	Income approach	Discount rate	9.85 %

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HIGHWOODS REALTY LIMITED PARTNERSHIP
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(tabular dollar amounts in thousands, except per unit data)

10. Share-based Payments

During the six months ended June 30, 2012, the Company granted 190,886 stock options with an exercise price equal to the closing market price of a share of its Common Stock on the date of grant. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model, which resulted in a weighted average grant date fair value per share of $5.47. During the six months ended June 30, 2012, the Company also granted 90,983 shares of time-based restricted stock and 67,902 shares of total return-based restricted stock with weighted average grant date fair values per share of $32.27 and $38.71, respectively. We recorded stock-based compensation expense of $2.0 million and $1.4 million during the three months ended June 30, 2012 and 2011, respectively, and $4.5 million and $3.5 million during the six months ended June 30, 2012 and 2011, respectively. At June 30, 2012, there was $7.6 million of total unrecognized stock-based compensation costs, which will be recognized over a weighted average remaining contractual term of 2.6 years.

11. Accumulated Other Comprehensive Loss

The following table sets forth the components of accumulated other comprehensive loss:

	Six Months Ended June 30,	
	2012	2011
Tax increment financing bond:		
Beginning balance	$(2,309)	$(2,543)
Unrealized gains/(losses) on tax increment financing bond	583	(471)
Ending balance	(1,726)	(3,014)
Cash flow hedges:		
Beginning balance	(3,425)	(1,105)
Unrealized losses on cash flow hedges	(7,087)	—
Amortization of cash flow hedges	1,459	(58)
Ending balance	(9,053)	(1,163)
Total accumulated other comprehensive loss	$(10,779)	$(4,177)

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HIGHWOODS REALTY LIMITED PARTNERSHIP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(tabular dollar amounts in thousands, except per unit data)

12. Discontinued Operations

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Rental and other revenues	$2,044	$2,907	$4,383	$6,169
Operating expenses:				
Rental property and other expenses	966	1,390	2,084	2,862
Depreciation and amortization	322	778	1,008	1,653
Total operating expenses	1,288	2,168	3,092	4,515
Income from discontinued operations	756	739	1,291	1,654
Net gains on disposition of discontinued operations	1,385	—	6,519	—
Total discontinued operations	$2,141	$739	$7,810	$1,654

The following table sets forth the major classes of assets and liabilities of our real estate and other assets held for sale, net:

	June 30, 2012	December 31, 2011
Assets:		
Land	$3,849	$ 5,749
Buildings and tenant improvements	49,460	65,860
Accumulated depreciation	(18,743)	(23,917)
Net real estate assets	34,566	47,692
Accrued straight line rents receivable	1,490	1,726
Deferred leasing costs, net	678	811
Prepaid expenses and other assets	17	106
Real estate and other assets, net, held for sale	$36,751	$ 50,335
Tenant security deposits, deferred rents and accrued costs (1)	$595	$ 238

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

As of June 30, 2012, real estate and other assets held for sale, net, included five office properties in Nashville, TN and one office property in Kansas City, MO. As of December 31, 2011, real estate and other assets held for sale, net, included five office properties in Nashville, TN, one office property in Pinellas County, FL and one office property and 96 residential units in Kansas City, MO. All of these properties qualified for discontinued operations.

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HIGHWOODS REALTY LIMITED PARTNERSHIP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(tabular dollar amounts in thousands, except per unit data)

13. Earnings Per Unit

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Earnings per Common Unit - basic:				
Numerator:				
Income from continuing operations	$12,360	$13,699	$25,025	$25,235
Net (income) attributable to noncontrolling interests in consolidated affiliates from continuing operations	(223)	(182)	(407)	(305)
Distributions on Preferred Units	(627)	(1,622)	(1,254)	(3,299)
Excess of Preferred Unit redemption/repurchase cost over carrying value	—	(1,895)	—	(1,895)
Income from continuing operations available for common unitholders	11,510	10,000	23,364	19,736
Income from discontinued operations available for common unitholders	2,141	739	7,810	1,654
Net income available for common unitholders	$13,651	$10,739	$31,174	$21,390
Denominator:				
Denominator for basic earnings per Common Unit – weighted average units (1) (2)	77,971	75,586	77,063	75,393
Earnings per Common Unit - basic:				
Income from continuing operations available for common unitholders	$0.15	$0.13	$0.30	$0.26
Income from discontinued operations available for common unitholders	0.03	0.01	0.10	0.02
Net income available for common unitholders	$0.18	$0.14	$0.40	$0.28
Earnings per Common Unit - diluted:				
Numerator:				
Income from continuing operations	$12,360	$13,699	$25,025	$25,235
Net (income) attributable to noncontrolling interests in consolidated affiliates from continuing operations	(223)	(182)	(407)	(305)
Distributions on Preferred Units	(627)	(1,622)	(1,254)	(3,299)
Excess of Preferred Unit redemption/repurchase cost over carrying value	—	(1,895)	—	(1,895)
Income from continuing operations available for common unitholders	11,510	10,000	23,364	19,736
Income from discontinued operations available for common unitholders	2,141	739	7,810	1,654
Net income available for common unitholders	$13,651	$10,739	$31,174	$21,390
Denominator:				
Denominator for basic earnings per Common Unit –weighted average units (1) (2)	77,971	75,586	77,063	75,393
Add:				
Stock options using the treasury method	141	202	129	185
Denominator for diluted earnings per Common Unit – adjusted weighted average units and assumed conversions (1)	78,112	75,788	77,192	75,578
Earnings per Common Unit - diluted:				
Income from continuing operations available for common unitholders	$0.15	$0.13	$0.30	$0.26
Income from discontinued operations available for common unitholders	0.02	0.01	0.10	0.02

Net income available for common unitholders	$0.17	$0.14	$0.40	$0.28

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(1) There were 0.5 million and 0.3 million options outstanding during the three months ended June 30, 2012 and 2011, respectively, and 0.5 million and 0.6 million options outstanding during the six months ended June 30, 2012 and 2011, respectively, that were not included in the computation of diluted earnings per unit because the impact of including such options would be anti-dilutive.

(2) Includes all unvested restricted stock since dividends on restricted stock are non-forfeitable.

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HIGHWOODS REALTY LIMITED PARTNERSHIP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(tabular dollar amounts in thousands, except per unit data)

14. Segment Information

The following table summarizes the rental and other revenues and net operating income, the primary industry property-level performance metric which is defined as rental and other revenues less rental property and other expenses, for each reportable segment:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Rental and Other Revenues: (1)				
Office:				
Atlanta, GA	$16,209	$12,341	$31,993	$24,242
Greenville, SC	3,489	3,437	6,993	6,942
Kansas City, MO	3,560	3,441	7,163	6,960
Memphis, TN	10,130	10,077	20,268	20,179
Nashville, TN	14,321	13,572	28,186	26,315
Orlando, FL	2,756	2,619	5,443	4,936
Piedmont Triad, NC	5,072	5,273	10,152	10,637
Pittsburgh, PA	9,113	—	18,199	—
Raleigh, NC	20,400	20,103	40,179	39,421
Richmond, VA	12,095	11,668	23,605	23,046
Tampa, FL	17,579	17,064	34,715	33,436
Total Office Segment	114,724	99,595	226,896	196,114
Industrial:				
Atlanta, GA	3,849	4,028	7,623	7,962
Piedmont Triad, NC	3,087	2,825	6,251	5,802
Total Industrial Segment	6,936	6,853	13,874	13,764
Retail:				
Kansas City, MO	9,075	8,203	17,998	17,103
Total Retail Segment	9,075	8,203	17,998	17,103
Total Rental and Other Revenues	$130,735	$114,651	$258,768	$226,981

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(tabular dollar amounts in thousands, except per unit data)

14. Segment Information - Continued

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Net Operating Income: (1)				
Office:				
Atlanta, GA	$10,435	$7,980	$20,837	$15,456
Greenville, SC	2,052	2,069	4,186	4,140
Kansas City, MO	2,188	2,114	4,521	4,254
Memphis, TN	5,845	5,467	11,951	11,215
Nashville, TN	9,842	9,376	19,504	17,989
Orlando, FL	1,432	1,285	2,849	2,449
Piedmont Triad, NC	3,221	3,455	6,457	7,049
Pittsburgh, PA	4,630	—	8,911	—
Raleigh, NC	14,301	14,285	28,169	27,473
Richmond, VA	8,541	8,238	16,431	16,080
Tampa, FL	10,818	10,565	21,668	20,672
Total Office Segment	73,305	64,834	145,484	126,777
Industrial:				
Atlanta, GA	2,763	3,004	5,653	5,837
Piedmont Triad, NC	2,310	2,109	4,599	4,328
Total Industrial Segment	5,073	5,113	10,252	10,165
Retail:				
Kansas City, MO	5,327	4,836	10,865	10,115
Total Retail Segment	5,327	4,836	10,865	10,115
Total Net Operating Income	83,705	74,783	166,601	147,057
Reconciliation to income from continuing operations before disposition of property and condominiums and equity in earnings of unconsolidated affiliates:				
Depreciation and amortization	(40,276)	(32,684)	(78,105)	(65,621)
General and administrative expense	(8,959)	(8,041)	(18,694)	(15,685)
Interest expense	(24,495)	(23,907)	(49,297)	(47,450)
Other income	764	1,875	2,994	3,748
Income from continuing operations before disposition of property and condominiums and equity in earnings of unconsolidated affiliates	$10,739	$12,026	$23,499	$22,049

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(1) Net of discontinued operations.

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15. Subsequent Events

In early July 2012, the Company issued 451,300 shares of Common Stock from sales in the second quarter of 2012 under our equity sales agreements at an average gross sales price of $33.52 per share raising net proceeds, after sales commissions and expenses, of $14.9 million.

On July 13, 2012, we acquired two medical office properties in Greensboro, NC for $16.4 million. The transaction included the issuance of approximately 77,000 Common Units. We expect to expense approximately $0.1 million of costs related to this acquisition.

On July 13, 2012, we sold five non-core office buildings in Nashville, TN for $41.0 million. We expect to record gain on disposition of discontinued operations of $6.8 million related to this disposition.

On July 25, 2012, we sold three GSA-leased buildings in Jackson, MS and Atlanta, GA for $86.5 million. We expect to record gain on disposition of discontinued operations of $14.0 million related to this disposition.

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

The Company is a fully integrated, self-administered and self-managed equity REIT that provides leasing, management, development, construction and other customer-related services for our properties and for third parties. The Company conducts virtually all of its activities through the Operating Partnership. The Operating Partnership is managed by the Company, its sole general partner. At June 30, 2012, we owned or had an interest in 338 in-service office, industrial and retail properties, encompassing approximately 34.6 million square feet, which includes one office property under development encompassing 203,000 square feet and a 12.5% interest in a 261,000 square foot office property directly owned by the Company (not included in the Operating Partnership's Consolidated Financial Statements); nine for-sale residential condominiums and a 215-unit rental residential property under development. We are based in Raleigh, North Carolina, and our properties and development land are located in Florida, Georgia, Mississippi, Missouri, North Carolina, Pennsylvania, South Carolina, Tennessee and Virginia. Additional information about us can be found on our website at www.highwoods.com. Information on our website is not part of this Quarterly Report.

You should read the following discussion and analysis in conjunction with the accompanying Consolidated Financial Statements and related notes contained elsewhere in this Quarterly Report.

Disclosure Regarding Forward-Looking Statements

Some of the information in this Quarterly Report may contain forward-looking statements. Such statements include, in particular, statements about our plans, strategies and prospects under this section. You can identify forward-looking statements by our use of forward-looking terminology such as "may," "will," "expect," "anticipate," "estimate," "continue" or similar words. Although we believe that our plans, intentions and expectations reflected in or suggested by such forward-looking statements are reasonable, we cannot assure you that our plans, intentions or expectations will be achieved. When considering such forward-looking statements, you should keep in mind the following important factors that could cause our actual results to differ materially from those contained in any forward-looking statement:

- the financial condition of our customers could deteriorate;
- we may not be able to lease or release second generation space, defined as previously occupied space that becomes available for lease, quickly or on as favorable terms as old leases;
- we may not be able to lease our newly constructed buildings as quickly or on as favorable terms as originally anticipated;
- we may not be able to complete development, acquisition, reinvestment, disposition or joint venture projects as quickly or on as favorable terms as anticipated;
- development activity by our competitors in our existing markets could result in an excessive supply of office, industrial and retail properties relative to customer demand;
- our markets may suffer declines in economic growth;
- unanticipated increases in interest rates could increase our debt service costs;
- unanticipated increases in operating expenses could negatively impact our operating results;

- we may not be able to meet our liquidity requirements or obtain capital on favorable terms to fund our working capital needs and growth initiatives or to repay or refinance outstanding debt upon maturity; and

- the Company could lose key executive officers.

This list of risks and uncertainties, however, is not intended to be exhaustive. You should also review the other cautionary statements we make in “Item 1A. Business – Risk Factors” set forth in our 2011 Annual Report on Form 10-K. Given these uncertainties, you should not place undue reliance on forward-looking statements. We undertake no obligation to publicly release the results of any revisions to these forward-looking statements to reflect any future events or circumstances or to reflect the occurrence of unanticipated events.

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Executive Summary

Our Strategic Plan focuses on:

- owning high-quality, differentiated real estate assets in the better submarkets in our core markets;
- improving the operating results of our existing properties through concentrated leasing, asset management, cost control and customer service efforts;
- developing and acquiring office properties in key infill submarkets that improve the overall quality of our portfolio and generate attractive returns over the long-term for our stockholders;
- selectively disposing of properties no longer considered to be core assets primarily due to location, age, quality and overall strategic fit; and
- maintaining a conservative, flexible balance sheet with ample liquidity to meet our funding needs and growth prospects.

While we own and operate a limited number of industrial, retail and residential properties, our operating results depend heavily on successfully leasing and operating our office properties. Economic growth and employment levels in our core markets are and will continue to be important determinative factors in predicting our future operating results.

The key components affecting our rental and other revenues are average occupancy, rental rates, new developments placed in service, acquisitions and dispositions. Average occupancy generally increases during times of improving economic growth, as our ability to lease space outpaces vacancies that occur upon the expirations of existing leases. Average occupancy generally declines during times of slower economic growth, when new vacancies tend to outpace our ability to lease space. Asset acquisitions, dispositions and new developments placed in service directly impact our rental revenues and could impact our average occupancy, depending upon the occupancy rate of the properties that are acquired, sold or placed in service. A further indicator of the predictability of future revenues is the expected lease expiration schedule of our portfolio. As a result, in addition to seeking to increase our average occupancy by leasing current vacant space, we also must concentrate our leasing efforts on renewing leases on expiring space.

Whether or not our rental revenue tracks average occupancy proportionally depends upon whether rents under new leases signed are higher or lower than the rents under the previous leases. Annualized rental revenues from second generation leases signed during any particular year are generally less than 15% of our total annual rental revenues. During the second quarter of 2012, we leased 0.6 million square feet of second generation office space, defined as space previously occupied under our ownership that becomes available for lease or acquired vacant space, with a weighted average term of 4.4 years. On average, tenant improvements for such leases were $10.29 per square foot, lease commissions were $2.65 per square foot and rent concessions were $2.65 per square foot. Annualized GAAP rents under such office leases were $21.71 per square foot, or 2.6% higher than under previous leases.

We strive to maintain a diverse, stable and creditworthy customer base. We have an internal guideline whereby customers that account for more than 3% of our revenues are periodically reviewed with the Company's Board of Directors. Currently, no customer accounts for more than 3% of our revenues other than the Federal Government, which accounts for 9.0% of our revenues, as of June 30, 2012. After the disposition of three GSA-leased buildings on July 25, 2012, the Federal Government accounts for 7.0% of our revenues.

Our expenses primarily consist of rental property expenses, depreciation and amortization, general and administrative expenses and interest expense. From time to time, expenses also include impairments of assets held for use. Rental property expenses are expenses associated with our ownership and operation of rental properties and include expenses that vary somewhat proportionately to occupancy levels, such as common area maintenance and utilities, and expenses that do not vary based on occupancy, such as property taxes and insurance. Depreciation and amortization is a non-cash expense associated with the ownership of real property and generally remains relatively consistent each year, unless we buy, place in service or sell assets, since we depreciate our properties and related building and tenant improvement assets on a straight-line basis over a fixed life. General and administrative expenses, net of amounts capitalized, consist primarily of management and employee salaries and other personnel costs, corporate overhead and long-term incentive compensation.

We intend to maintain a conservative and flexible balance sheet that allows us to capitalize on favorable development and acquisition opportunities as they arise. As of June 30, 2012, our mortgages and notes payable represented 44.9% of the undepreciated book value of our assets. We expect this ratio to remain under 50% during the remainder of 2012.

Results of Operations

Three Months Ended June 30, 2012 and 2011

Rental and Other Revenues

Rental and other revenues from continuing operations were $16.1 million, or 14.0%, higher in the second quarter of 2012 as compared to 2011 primarily due to the acquisitions of office properties in Pittsburgh, PA and Atlanta, GA in the third quarter of 2011 and an office property in Raleigh, NC in the second quarter of 2012, which collectively accounted for $12.5 million of the increase. In addition, same property revenues were $3.5 million higher in the second quarter of 2012 as compared to 2011 primarily due to an increase in same property average occupancy and annualized GAAP rents per square foot from 89.9% and $18.54 in the second quarter of 2011 to 91.4% and $18.82 in the second quarter of 2012, respectively, higher operating expense recoveries due to higher operating expenses, higher net termination fees due to an early termination at an office property in Atlanta, GA and lower bad debts. We expect rental and other revenues for the remainder of 2012, adjusted for any discontinued operations and additional acquisition activity, to be higher compared to the same period in 2011 primarily due to the contribution of acquisitions made in the third quarter of 2011, partly offset by slightly lower average occupancy in our same property portfolio as a result of the early termination discussed above.

Operating Expenses

Rental property and other expenses were $7.2 million, or 17.9%, higher in the second quarter of 2012 as compared to 2011 primarily due to recent acquisitions, which accounted for $5.5 million of the increase. In addition, same property operating expenses were $1.6 million higher in the second quarter of 2012 as compared to 2011 primarily due to higher repairs and maintenance, utilities and insurance costs, partly offset by lower real estate taxes. We expect rental property and other expenses for the remainder of 2012, adjusted for any discontinued operations and additional acquisition activity, to be higher compared to the same period in 2011 primarily due to the contribution of acquisitions made in the third quarter of 2011.

Operating margin, defined as rental and other revenues less rental property and other expenses expressed as a percentage of rental and other revenues, was lower at 64.0% in the second quarter of 2012, as compared to 65.2% in the second quarter of 2011. Operating margin is expected to be similar for the remainder of 2012 as compared to the same period in 2011.

Depreciation and amortization was $7.6 million, or 23.2%, higher in the second quarter of 2012 as compared to 2011 primarily due to recent acquisitions, which accounted for $5.4 million of the increase. In addition, same property depreciation and amortization was $1.9 million higher in the second quarter of 2012 as compared to 2011 primarily due to an early termination. We expect depreciation expense for the remainder of 2012, adjusted for any discontinued operations and additional acquisition activity, to be higher compared to the same period in 2011 primarily due to the contribution of acquisitions made in the third quarter of 2011.

General and administrative expenses were $0.9 million, or 11.6%, higher in the second quarter of 2012 as compared to 2011 primarily due to higher salaries and incentive compensation. We expect general and administrative expenses for the remainder of 2012, adjusted for additional acquisition activity, to decrease over the same period in 2011 due to lower dead deal and acquisition costs.

Other Income

Other income was $1.1 million lower in the second quarter of 2012 as compared to 2011 primarily due to a loss on debt extinguishment of outstanding bonds in 2012.

Interest Expense

Interest expense was $0.6 million, or 2.5%, higher in the second quarter of 2012 as compared to 2011 primarily due to higher average debt balances from recent acquisitions, offset by lower average interest rates and financing obligation interest expense. We anticipate interest expense will increase for the remainder of 2012 as compared to the same period in 2011 due to the full year impact of higher average debt balances from acquisitions, partly offset by lower average interest rates on our outstanding borrowings and lower financing obligation interest expense in 2012.

Net Gains on Disposition of Discontinued Operations

Net gains on disposition of discontinued operations were $1.4 million higher in the second quarter of 2012 as compared to 2011 due to the disposition of an office property in Pinellas County, FL in the second quarter of 2012.

Dividends on Preferred Stock and Excess of Preferred Stock Redemption/Repurchase Cost Over Carrying Value

Dividends on Preferred Stock were $1.0 million lower in the second quarter of 2012 as compared to 2011 and excess of Preferred Stock redemption/repurchase cost over carrying value was $1.9 million lower in the second quarter of 2012 as compared to 2011 due to the redemption of all remaining Series B Preferred Shares in the second quarter of 2011.

Six Months Ended June 30, 2012 and 2011

Rental and Other Revenues

Rental and other revenues from continuing operations were $31.8 million, or 14.0%, higher in the first six months of 2012 as compared to the same period in 2011 primarily due to the acquisitions of office properties in Pittsburgh, PA and Atlanta, GA in the third quarter of 2011 and an office property in Raleigh, NC in the second quarter of 2012, which accounted for $24.6 million of the increase. Same property revenues were $6.7 million higher in the first six months of 2012 as compared to the same period in 2011 primarily due to an increase in same property average occupancy and annualized GAAP rents per square foot from 90.1% and $18.38 in the first six months of 2011 to 91.1% and $18.73 in the first six months of 2012, higher operating expense recoveries and higher net termination fees.

Operating Expenses

Rental property and other expenses were $12.5 million, or 15.6%, higher in the first six months of 2012 as compared to the same period in 2011 primarily due to recent acquisitions, which accounted for $11.5 million of the increase. Same property operating expenses were $0.7 million higher in the first six months of 2012 as compared to the same period in 2011 primarily due to higher repairs and maintenance costs, offset by lower utilities from the mild winter in 2012 and lower real estate taxes.

Operating margin, defined as rental and other revenues less rental property and other expenses expressed as a percentage of rental and other revenues, was lower at 64.3% in the first six months of 2012, as compared to 64.8% in the first six months of 2011.

Depreciation and amortization was $12.5 million, or 19.0%, higher in the first six months of 2012 as compared to the same period in 2011 primarily due to recent acquisitions, which accounted for $10.1 million of the increase. In addition, same property depreciation and amortization was $2.2 million higher in the first six months of 2012 as compared to the same period in 2011 primarily due to an early termination.

General and administrative expenses were $2.8 million, or 17.8%, higher in the first six months of 2012 as compared to the same period in 2011 primarily due to higher salaries and incentive compensation.

Interest Expense

Interest expense was $1.8 million, or 3.9%, higher in the first six months of 2012 as compared to the same period in 2011 primarily due to higher average debt balances from recent acquisitions, offset by lower average interest rates and financing obligation interest expense.

Equity in Earnings of Unconsolidated Affiliates

Equity in earnings of unconsolidated affiliates was $1.5 million lower in the first six months of 2012 as compared to the same period in 2011 primarily due to our share of impairment of real estate assets on two office properties in our DLF I joint venture.

Net Gains on Disposition of Discontinued Operations

Net gains on disposition of discontinued operations were $6.5 million higher in the first six months of 2012 as compared to the same period in 2011 due to the disposition of 96 rental residential units in Kansas City, MO in the first quarter of 2012 and an office property in Pinellas County, FL in the second quarter of 2012.

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Dividends on Preferred Stock and Excess of Preferred Stock Redemption/Repurchase Cost Over Carrying Value

Dividends on Preferred Stock were $2.0 million lower in the first six months of 2012 as compared to the same period in 2011 and excess of Preferred Stock redemption/repurchase cost over carrying value was $1.9 million lower in the first six months of 2012 as compared to the same period in 2011 due to the redemption of all remaining Series B Preferred Shares in the second quarter of 2011.

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Liquidity and Capital Resources

Overview

Our goal is to maintain a conservative and flexible balance sheet with access to multiple sources of debt and equity capital and sufficient availability under our revolving credit facility. We generally use rents received from customers to fund our operating expenses, capital expenditures and distributions. To fund property acquisitions, development activity or building renovations and repay debt upon maturity, we may use current cash balances, sell assets, obtain new debt and/or issue equity. Our debt generally consists of mortgage debt, unsecured debt securities and borrowings under our revolving credit facility.

Statements of Cash Flows

We report and analyze our cash flows based on operating activities, investing activities and financing activities. The following table sets forth the changes in the Company’s cash flows ($ in thousands):

	Six Months Ended June 30,		
	2012	2011	Change
Net Cash Provided By Operating Activities	$93,328	$87,595	$5,733
Net Cash Used In Investing Activities	(39,024)	(78,913)	39,889
Net Cash Used In Financing Activities	(58,965)	(13,649)	(45,316)
Total Cash Flows	$(4,661)	$(4,967)	$306

In calculating net cash related to operating activities, depreciation and amortization, which are non-cash expenses, are added back to net income. As a result, we have historically generated a positive amount of cash from operating activities. From period to period, cash flow from operations depends primarily upon changes in our net income, as discussed more fully above under “Results of Operations,” changes in receivables and payables, and net additions or decreases in our overall portfolio, which affect the amount of depreciation and amortization expense.

Net cash related to investing activities generally relates to capitalized costs incurred for leasing and major building improvements and our acquisition, development, disposition and joint venture capital activity. During periods of significant net acquisition and/or development activity, our cash used in such investing activities will generally exceed cash provided by investing activities, which typically consists of cash received upon the sale of properties and distributions of capital from our joint ventures.

Net cash related to financing activities generally relates to distributions, incurrence and repayment of debt, and issuances, repurchases or redemptions of Common Stock, Common Units and Preferred Stock. As discussed previously, we use a significant amount of our cash to fund distributions. Whether or not we have increases in the outstanding balances of debt during a period depends generally upon the net effect of our acquisition, disposition, development and joint venture activity. We generally use our revolving credit facility for working capital purposes, which means that during any given period, in order to minimize interest expense, we may record significant repayments and borrowings under our revolving credit facility.

The change in net cash related to operating activities in the first six months of 2012 as compared to the same period in 2011 was primarily due to net operating income from acquisitions made in the third quarter of 2011, partly offset by the timing of real estate tax payments.

The change in net cash related to investing activities in the first six months of 2012 as compared to the same period in 2011 was primarily due to a loan to an unconsolidated affiliate in the second quarter of 2011 and higher net proceeds from the disposition of real estate assets in the first six months of 2012, partly offset by higher capital expenditures in the first six months of 2012 related to recent acquisitions.

The change in net cash related to financing activities in the first six months of 2012 as compared to the same period in 2011 was primarily due to higher net repayments of borrowings in the first six months of 2012, partly offset by higher proceeds from the issuance of Common Stock in the first six months of 2012 and the repurchase of Preferred Stock in the second quarter of 2011.

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Capitalization

The following table sets forth the Company’s capitalization (in thousands, except per share amounts):

	June 30, 2012	December 31, 2011
Mortgages and notes payable, at recorded book value	$1,823,128	$ 1,903,213
Financing obligations	$30,822	$ 31,444
Preferred Stock, at liquidation value	$29,077	$ 29,077
Common Stock outstanding	75,619	72,648
Common Units outstanding (not owned by the Company)	3,711	3,730
Per share stock price at period end	$33.65	$ 29.67
Market value of Common Stock and Common Units	$2,669,455	$ 2,266,135
Total market capitalization	$4,552,482	$ 4,229,869

At June 30, 2012, our mortgages and notes payable represented 40.0% of our total market capitalization and consisted of $743.5 million of secured indebtedness with a weighted average interest rate of 5.50% and $1,079.6 million of unsecured indebtedness with a weighted average interest rate of 4.77%. The secured indebtedness was collateralized by real estate assets with an aggregate undepreciated book value of $1,237.7 million.

Current and Future Cash Needs

Rental and other revenues are our principal source of funds to meet our short-term liquidity requirements. Other sources of funds for short-term liquidity needs include available working capital and borrowings under our existing revolving credit facility, which had $446.8 million of availability at July 19, 2012. Our short-term liquidity requirements primarily consist of operating expenses, interest and principal amortization on our debt, dividends and distributions and capital expenditures, including building improvement costs, tenant improvement costs and lease commissions. Building improvements are capital costs to maintain existing buildings not typically related to a specific customer. Tenant improvements are the costs required to customize space for the specific needs of customers. We anticipate that our available cash and cash equivalents and cash provided by operating activities, together with cash available from borrowings under our revolving credit facility, will be adequate to meet our short-term liquidity requirements.

Our long-term liquidity uses generally consist of the retirement or refinancing of debt upon maturity (including mortgage debt, our revolving and construction credit facilities, term loans and other unsecured debt), funding of existing and new building development or land infrastructure projects and funding acquisitions of buildings and development land. Additionally, we may, from time to time, retire some or all of our remaining outstanding Preferred Stock and/or unsecured debt securities through redemptions, open market repurchases, privately negotiated acquisitions or otherwise.

We expect to meet our long-term liquidity needs through a combination of:

- cash flow from operating activities;

- borrowings under our revolving credit facility;

- the issuance of unsecured debt;

- the issuance of secured debt;
- the issuance of equity securities by the Company or the Operating Partnership; and
- the disposition of non-core assets.

Recent Acquisition and Disposition Activity

During the second quarter of 2012, we acquired a 178,300 square foot office property in Cary, NC from our DLF I joint venture for an agreed upon value of $26.0 million.

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During the second quarter of 2012, we sold a non-core office property in Pinellas County, FL for gross proceeds of $9.5 million. We recorded gain on disposition of discontinued operations of $1.4 million related to this disposition.

On July 13, 2012, we acquired two medical office properties in Greensboro, NC for $16.4 million. The transaction included the issuance of approximately 77,000 Common Units. We expect to expense approximately $0.1 million of costs related to this acquisition. In addition, we expect to acquire a third related medical office property in Greensboro, NC for an additional $13.4 million in the third quarter of 2012. This purchase price will include the assumption of secured debt recorded at fair value of $7.9 million, with an estimated effective interest rate of 3.5%, including amortization of deferred financing costs. This assumed debt is scheduled to mature in August 2014.

On July 13, 2012, we sold five non-core office buildings in Nashville, TN for $41.0 million. We expect to record gain on disposition of discontinued operations of $6.8 million related to this disposition.

On July 25, 2012, we sold three GSA-leased buildings in Jackson, MS and Atlanta, GA for $86.5 million. We expect to record gain on disposition of discontinued operations of $14.0 million related to this disposition.

Recent Financing Activity

We have entered into separate ATM Equity Offering$_{SM}$ Sales Agreements (the “Sales Agreements”) with each of Merrill Lynch, Pierce, Fenner & Smith Incorporated, Mitsubishi UFJ Securities (USA), Inc., Morgan Keegan & Company, Inc. and RBC Capital Markets, LLC (each, an “Agent” and, together, the “Agents”). Under the terms of the Sales Agreements, the Company may offer and sell shares of its Common Stock from time to time through the Agents, acting as agents of the Company or as principals. Sales of the shares, if any, may be made by means of ordinary brokers' transactions on the New York Stock Exchange or otherwise at market prices prevailing at the time of sale, at prices related to prevailing market prices or at negotiated prices or as otherwise agreed with any of the Agents. Subject to the terms and conditions of each Sales Agreement, each Agent will use its commercially reasonable efforts to sell on the Company's behalf any shares to be offered by the Company under that Sales Agreement. During the second quarter of 2012, the Company issued 1,836,976 shares of Common Stock under these agreements at an average gross sales price of $33.72 per share raising net proceeds, after sales commissions and expenses, of $61.0 million. We paid an aggregate of $0.9 million in sales commissions to Merrill Lynch, Pierce, Fenner & Smith Incorporated and Mitsubishi UFJ Securities (USA), Inc. during the second quarter of 2012. In early July 2012, the Company issued 451,300 shares of Common Stock from sales in the first quarter of 2012 under these agreements at an average gross sales price of $33.52 per share raising net proceeds, after sales commissions and expenses, of $14.9 million. We paid $0.2 million in sales commissions to Mitsubishi UFJ Securities (USA), Inc. during July 2012.

Our $475.0 million unsecured revolving credit facility is scheduled to mature on July 27, 2015 and includes an accordion feature that allows for an additional $75.0 million of borrowing capacity subject to additional lender commitments. Assuming no defaults have occurred, we have an option to extend the maturity for an additional year. The interest rate at our current credit ratings is LIBOR plus 150 basis points and the annual facility fee is 35 basis points. The interest rate and facility fee are based on the higher of the publicly announced ratings from Moody's Investors Service or Standard & Poor's Ratings Services. We use our revolving credit facility for working capital purposes and for the short-term funding of our development and acquisition activity and, in certain instances, the repayment of other debt. Continuing ability to borrow under the revolving credit facility allows us to quickly capitalize on strategic opportunities at short-term interest rates. There was $75.5 million and $28.1 million outstanding under our revolving credit facility at June 30, 2012 and July 19, 2012, respectively. At both June 30, 2012 and July 19, 2012, we had $0.1 million of outstanding letters of credit, which reduces the availability on our revolving credit facility. As a result, the unused capacity of our revolving credit facility at June 30, 2012 and July 19, 2012 was $399.4 million and $446.8 million, respectively.

In the second quarter of 2012, we repurchased $12.1 million principal amount of unsecured notes due March 2017 bearing interest of 5.85% for a purchase price of 107.5% of par value. We recorded $1.0 million of loss on debt extinguishment related to this repurchase.

We regularly evaluate the financial condition of the lenders that participate in our credit facilities using publicly available information. Based on this review, we currently expect our lenders, which are major financial institutions, to perform their obligations under our existing facilities.

Covenant Compliance

We are currently in compliance with the covenants and other requirements with respect to our outstanding debt. Although we expect to remain in compliance with these covenants and ratios for at least the next year, depending upon our future operating performance, property and financing transactions and general economic conditions, we cannot assure you that we will continue to be in compliance.

Our revolving credit facility and bank term loans require us to comply with customary operating covenants and various financial requirements. Upon an event of default on the revolving credit facility, the lenders having at least 66.7% of the total commitments under the revolving credit facility can accelerate all borrowings then outstanding, and we could be prohibited from borrowing any further amounts under our revolving credit facility, which would adversely affect our ability to fund our operations.

The Operating Partnership has $379.1 million carrying amount of 2017 bonds outstanding and $200.0 million carrying amount of 2018 bonds outstanding. The indenture that governs these outstanding notes requires us to comply with customary operating covenants and various financial ratios. The trustee or the holders of at least 25.0% in principal amount of either series of bonds can accelerate the principal amount of such series upon written notice of a default that remains uncured after 60 days.

We may not be able to repay, refinance or extend any or all of our debt at maturity or upon any acceleration. If any refinancing is done at higher interest rates, the increased interest expense could adversely affect our cash flow and ability to pay distributions. Any such refinancing could also impose tighter financial ratios and other covenants that restrict our ability to take actions that could otherwise be in our best interest, such as funding new development activity, making opportunistic acquisitions, repurchasing our securities or paying distributions.

Off Balance Sheet Arrangements

In 2011, we provided a $38.3 million interest-only secured loan to our DLF I joint venture that originally was scheduled to mature in March 2012. The loan bears interest at LIBOR plus 500 basis points. The maturity date of the loan has been extended to September 30, 2012. In the second quarter of 2012, we acquired an office property from the joint venture by reducing the balance of the advance due to us from the joint venture joint venture. We deferred our share of the gain recorded by the joint venture related to this transaction. We recorded interest income from this loan in interest and other income of $0.2 million and $0.3 million during the three months ended June 30, 2012 and 2011, respectively, and $0.7 million and $0.3 million during the six months ended June 30, 2012 and 2011, respectively.

In the second quarter of 2012, our DLF II joint venture obtained a $50.0 million, three-year secured mortgage loan from a third party lender, bearing a fixed interest rate of 3.5% on $39.1 million of the loan and a floating interest rate of LIBOR plus 250 basis points on $10.9 million of the loan, which was used by the joint venture to repay a secured loan at maturity to a third party lender.

There were no other significant changes to our off balance sheet arrangements in the three months ended June 30, 2012. For information regarding our off balance sheet arrangements at December 31, 2011, see Note 9 to the Consolidated Financial Statements in our 2011 Annual Report on Form 10-K.

Critical Accounting Estimates

There were no changes made by management to the critical accounting policies in the six months ended June 30, 2012. For a description of our critical accounting estimates, see “Management's Discussion and Analysis of Financial Condition and Results of Operations - Critical Accounting Estimates” in our 2011 Annual Report on Form 10-K.

Non-GAAP Measures - FFO and NOI

The Company believes that Funds from Operations (“FFO”) and FFO per share are beneficial to management and investors and are important indicators of the performance of any equity REIT. Because FFO and FFO per share calculations exclude such factors as depreciation, amortization and impairment of real estate assets and gains or losses from sales of operating real estate assets, which can vary among owners of identical assets in similar conditions based on historical cost accounting and useful life estimates, they facilitate comparisons of operating performance between periods and between other REITs. Management believes that historical cost accounting for real estate assets in accordance with GAAP implicitly assumes that the value of real estate assets diminishes predictably over time. Since real estate values have historically risen or fallen with market conditions, many industry investors and analysts have considered the presentation of operating results for real estate companies that use historical cost accounting to be insufficient on a stand-alone basis. As a result, management believes that the use of FFO and FFO per share, together with the required GAAP presentations, provides a more complete understanding of the Company's performance relative to its competitors and a more informed and appropriate basis on which to make decisions involving operating, financing and investing activities.

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FFO and FFO per share are non-GAAP financial measures and therefore do not represent net income or net income per share as defined by GAAP. Net income and net income per share as defined by GAAP are the most relevant measures in determining the Company's operating performance because FFO and FFO per share include adjustments that investors may deem subjective, such as adding back expenses such as depreciation, amortization and impairment. Furthermore, FFO per share does not depict the amount that accrues directly to the stockholders' benefit. Accordingly, FFO and FFO per share should never be considered as alternatives to net income or net income per share as indicators of the Company's operating performance.

The Company's presentation of FFO is consistent with FFO as defined by the National Association of Real Estate Investment Trusts ("NAREIT"), which is calculated as follows:

- Net income/(loss) computed in accordance with GAAP;
- Less net income attributable to noncontrolling interests in consolidated affiliates;
- Plus depreciation and amortization of depreciable operating properties;
- Less gains, or plus losses, from sales of depreciable operating properties, plus impairments on depreciable operating properties and excluding items that are classified as extraordinary items under GAAP;
- Plus or minus our proportionate share of adjustments, including depreciation and amortization of depreciable operating properties, for unconsolidated partnerships and joint ventures (to reflect funds from operations on the same basis); and
- Plus or minus adjustments for depreciation and amortization and gains/(losses) on sales of depreciable operating properties, plus impairments on depreciable operating properties, and noncontrolling interests in consolidated affiliates related to discontinued operations.

In calculating FFO, the Company excludes net income attributable to noncontrolling interests in the Operating Partnership, which the Company believes is consistent with standard industry practice for REITs that operate through an UPREIT structure. The Company believes that it is important to present FFO on an as-converted basis since all of the Common Units not owned by the Company are redeemable on a one-for-one basis for shares of its Common Stock.

The following table sets forth the Company's FFO and FFO per share ($ in thousands, except per share amounts):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Funds from operations:				
Net income	$14,498	$14,434	$32,830	$26,877
Net (income) attributable to noncontrolling interests in consolidated affiliates	(223)	(182)	(407)	(305)
Depreciation and amortization of real estate assets	39,854	32,225	77,141	64,728
Unconsolidated affiliates:				
Depreciation and amortization of real estate assets	1,675	2,033	3,773	4,126
Impairment of depreciable properties	—	—	1,002	—
Discontinued operations:				

Depreciation and amortization of real estate assets	322	778	1,008	1,653
(Gains) on disposition of depreciable properties	(1,385)	—	(6,519)	—
Funds from operations	54,741	49,288	108,828	97,079
Dividends on Preferred Stock	(627)	(1,622)	(1,254)	(3,299)
Excess of Preferred Stock redemption/repurchase cost over carrying value	—	(1,895)	—	(1,895)
Funds from operations available for common stockholders	$54,114	$45,771	$107,574	$91,885
Funds from operations available for common stockholders per share	$0.69	$0.60	$1.39	$1.21
Weighted average shares outstanding (1)	78,521	76,197	77,601	75,987

(1) Includes assumed conversion of all potentially dilutive Common Stock equivalents.

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In addition, the Company believes net operating income from continuing operations ("NOI") and same property NOI are useful supplemental measures of the Company's property operating performance because such metrics provide a performance measure of the revenues and expenses directly involved in owning real estate assets and provides a perspective not immediately apparent from net income or FFO. The Company defines NOI as rental and other revenues from continuing operations, less rental property and other expenses from continuing operations. The Company defines cash NOI as NOI less straight line rent and lease termination fees. Other REITs may use different methodologies to calculate NOI and same property NOI.

Our same property portfolio currently consists of 287 in-service office, industrial and retail properties encompassing 26.4 million square feet that were wholly owned during the entirety of the periods presented (from January 1, 2011 to June 30, 2012). In our most recent prior periodic report, our 2011 Annual Report, our same property portfolio consisted of 289 in-service office, industrial and retail properties encompassing 26.2 million square feet that were wholly owned during the entirety of the periods presented therein (from January 1, 2010 to December 31, 2011). The change in our same property portfolio was due to the addition of one office property encompassing 0.3 million square feet acquired during 2010 and three newly developed office properties encompassing 0.5 million square feet placed in service during 2010, offset by the removal of six office properties encompassing 0.6 million square feet qualifying for discontinued operations during 2012.

Rental and other revenues related to properties not in our same property portfolio were $17.3 million and $4.8 million for the three months ended June 30, 2012 and 2011, respectively, and $33.8 million and $8.7 million for the six months ended June 30, 2012 and 2011, respectively. Rental property and other expenses related to properties not in our same property portfolio were $8.3 million and $2.6 million for the three months ended June 30, 2012 and 2011, respectively, and $16.8 million and $5.0 million for the six months ended June 30, 2012 and 2011, respectively.

The following table sets forth the Company's NOI and same property NOI:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Income from continuing operations before disposition of property and condominiums and equity in earnings of unconsolidated affiliates	$10,739	$12,026	$23,499	$22,049
Other (income)	(764)	(1,875)	(2,994)	(3,748)
Interest expense	24,495	23,907	49,297	47,450
General and administrative expense	8,900	7,978	18,573	15,771
Depreciation and amortization expense	40,276	32,684	78,105	65,621
Net operating income from continuing operations	83,646	74,720	166,480	147,143
Less – non same property and other net operating income	9,080	2,075	17,003	3,649
Total same property net operating income from continuing operations	$74,566	$72,645	$149,477	$143,494
Rental and other revenues	$130,735	$114,651	$258,768	$226,981
Rental property and other expenses	47,089	39,931	92,288	79,838
Total net operating income from continuing operations	83,646	74,720	166,480	147,143
Less – non same property and other net operating income	9,080	2,075	17,003	3,649
Total same property net operating income from continuing operations	$74,566	$72,645	$149,477	$143,494
Total same property net operating income from continuing operations	$74,566	$72,645	$149,477	$143,494
Less – straight line rent and lease termination fees	3,535	2,851	7,458	6,364
Same property cash net operating income from continuing operations	$71,031	$69,794	$142,019	$137,130

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

For information regarding our market risk as of March 31, 2012, see "Quantitative and Qualitative Disclosures About Market Risk" in our Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2012.

ITEM 4. CONTROLS AND PROCEDURES

SEC rules require us to maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our annual and periodic reports filed with the SEC is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. The Company's CEO and CFO have concluded that the disclosure controls and procedures of the Company and the Operating Partnership were each effective at the end of the period covered by this Quarterly Report.

SEC rules also require us to establish and maintain internal control over financial reporting designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepting accounting principles. There were no changes in internal control over financial reporting during the three months ended June 30, 2012 that materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. There were also no changes in internal control over financial reporting during the three months ended June 30, 2012 that materially affected, or are reasonably likely to materially affect, the Operating Partnership's internal control over financial reporting.

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PART II

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITES AND USE OF PROCEEDS

During the second quarter of 2012, the Company issued an aggregate of 16,366 shares of Common Stock to holders of Common Units in the Operating Partnership upon the redemption of a like number of Common Units in private offerings exempt from the registration requirements pursuant to Section 4(2) of the Securities Act. Each of the holders of Common Units was an accredited investor under Rule 501 of the Securities Act. The resale of such shares was registered by the Company under the Securities Act.

ITEM 5. OTHER EVENTS

As a result of adopting a new accounting pronouncement in the first quarter of 2012, we have presented comprehensive income in a separate financial statement entitled Consolidated Statements of Comprehensive Income. The table below reflects the retrospective application of this new accounting pronouncement, which did not have a material impact on our financial condition or results of operations.

	Year Ended December 31,		
	2011	2010	2009
Comprehensive income/(loss):			
Net income	$47,971	$72,303	$61,694
Other comprehensive income/(loss):			
Unrealized gains/(losses) on tax increment financing bond	234	(177)	293
Unrealized gains/(losses) on cash flow hedges	(2,202)	—	937
Amortization of cash flow hedges	(118)	237	(249)
Sale of cash flow hedge related to disposition of investment in unconsolidated affiliate	—	103	—
Total other comprehensive income/(loss)	(2,086)	163	981
Total comprehensive income	45,885	72,466	62,675
Less-comprehensive (income) attributable to noncontrolling interests	(2,846)	(3,805)	(3,208)
Comprehensive income attributable to the Company	$43,039	$68,661	$59,467

ITEM 6. EXHIBITS

Exhibit Number	Description
12.1	Statement re: Computation of Ratios of the Company
12.2	Statement re: Computation of Ratios of the Operating Partnership
31.1	Certification of CEO Pursuant to Section 302 of the Sarbanes-Oxley Act for the Company
31.2	Certification of CFO Pursuant to Section 302 of the Sarbanes-Oxley Act for the Company
31.3	Certification of CEO Pursuant to Section 302 of the Sarbanes-Oxley Act for the Operating Partnership
31.4	Certification of CFO Pursuant to Section 302 of the Sarbanes-Oxley Act for the Operating Partnership
32.1	Certification of CEO Pursuant to Section 906 of the Sarbanes-Oxley Act for the Company
32.2	Certification of CFO Pursuant to Section 906 of the Sarbanes-Oxley Act for the Company
32.3	Certification of CEO Pursuant to Section 906 of the Sarbanes-Oxley Act for the Operating Partnership
32.4	Certification of CFO Pursuant to Section 906 of the Sarbanes-Oxley Act for the Operating Partnership
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document

101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Extension Labels Linkbase
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, each of the registrants has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Highwoods Properties, Inc.

By: /s/ Terry L. Stevens
Terry L. Stevens
Senior Vice President and Chief Financial Officer

Highwoods Realty Limited Partnership

By: Highwoods Properties, Inc., its sole general partner

By: /s/ Terry L. Stevens
Terry L. Stevens
Senior Vice President and Chief Financial Officer

Date: July 26, 2012