

# HIGHWOODS PROPERTIES INC

## FORM 10-Q (Quarterly Report)

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Address	3100 SMOKETREE CT STE 600 RALEIGH, North Carolina 27604
Telephone	919-872-4924
CIK	0000921082
Industry	Real Estate Operations
Sector	Services
Fiscal Year	12/31

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# SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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## FORM 10-Q

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

For the quarterly period ended September 30, 2002

*Commission file number: 001-13100*

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## HIGHWOODS PROPERTIES, INC.

(Exact name of registrant as specified in its charter)

Maryland  
(State or other jurisdiction of  
incorporation or organization)

56-1871668  
(I.R.S. Employer  
Identification Number)

**3100 Smoketree Court, Suite 600, Raleigh, N.C.**  
(Address of principal executive office)

27604  
(Zip Code)

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

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

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The Company has only one class of common stock, par value \$.01 per share, with 53,387,085 shares outstanding as of October 31, 2002.

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# HIGHWOODS PROPERTIES, INC.

## QUARTERLY REPORT FOR THE PERIOD ENDED SEPTEMBER 30, 2002

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## **PART I -- FINANCIAL INFORMATION**

### **Item 1. Financial Statements**

We refer to (1) Highwoods Properties, Inc. as the "Company," (2) Highwoods Realty Limited Partnership as the "Operating Partnership," (3) the Company's common stock as "Common Stock" and (4) the Operating Partnership's common partnership interests as "Common Units."

The information furnished in the accompanying balance sheets, statements of income, statements of stockholders' equity and statements of cash flows reflect all adjustments (consisting of normal recurring accruals) that are, in our opinion, necessary for a fair presentation of the aforementioned financial statements for the interim period.

The aforementioned financial statements should be read in conjunction with the notes to consolidated financial statements and Management's Discussion and Analysis of Financial Condition and Results of Operations included herein and in our 2001 Annual Report on Form 10-K.

**HIGHWOODS PROPERTIES, INC.**  
**Consolidated Balance Sheets**  
(\$ in thousands)

	SEPTEMBER 30, 2002	DECEMBER 31, 2001
	----- (Unaudited)	-----
<b>ASSETS</b>		
Real estate assets, at cost:		
Land and improvements.....	\$ 428,852	\$ 420,922
Buildings and tenant improvements.....	2,890,638	2,827,825
Development in process.....	40,018	108,122
Land held for development.....	174,002	153,468
Furniture, fixtures and equipment.....	20,479	19,398
	-----	-----
	3,553,989	3,529,735
Less - accumulated depreciation.....	(448,994)	(374,623)
	-----	-----
Net real estate assets.....	3,104,995	3,155,112
Property held for sale.....	139,972	212,590
Cash and cash equivalents.....	13,998	576
Restricted cash.....	2,702	5,685
Accounts receivable, net.....	18,327	23,659
Advances to related parties.....	971	788
Notes receivable.....	31,914	43,761
Accrued straight-line rents receivable.....	50,191	49,078
Investment in unconsolidated affiliates.....	80,825	83,393
Other assets:		
Deferred leasing costs.....	106,821	95,761
Deferred financing costs.....	25,964	26,121
Prepaid expenses and other.....	13,400	10,461
	-----	-----
	146,185	132,343
Less - accumulated amortization.....	(71,125)	(58,699)
	-----	-----
Other assets, net.....	75,060	73,644
	-----	-----
Total Assets.....	\$ 3,518,955	\$ 3,648,286
	=====	=====
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Mortgages and notes payable.....	\$ 1,626,362	\$ 1,719,230
Accounts payable, accrued expenses and other liabilities.....	131,087	120,235
	-----	-----
Total Liabilities.....	1,757,449	1,839,465
Minority interest.....	191,114	203,181
<b>STOCKHOLDERS' EQUITY:</b>		
Preferred stock, \$.01 par value, 50,000,000 authorized shares:		
8 5/8% Series A Cumulative Redeemable Preferred Shares (liquidation preference \$1,000 per share), 104,945 shares issued and outstanding at September 30, 2002 and December 31, 2001.....	104,945	104,945
8% Series B Cumulative Redeemable Preferred Shares (liquidation preference \$25 per share), 6,900,000 shares issued and outstanding at September 30, 2002 and December 31, 2001.....	172,500	172,500
8% Series D Cumulative Redeemable Preferred Shares (liquidation preference \$250 per share), 400,000 shares issued and outstanding at September 30, 2002 and December 31, 2001.....	100,000	100,000
Common stock, \$.01 par value, 200,000,000 authorized shares; 53,387,085 and 52,891,822 shares issued and outstanding at September 30, 2002 and December 31, 2001, respectively.....	534	529
Additional paid-in capital.....	1,389,595	1,376,546
Distributions in excess of net earnings.....	(182,719)	(135,878)
Accumulated other comprehensive loss.....	(10,418)	(9,441)
Deferred compensation--restricted stock.....	(4,045)	(3,561)
	-----	-----
Total Stockholders' Equity.....	1,570,392	1,605,640
	-----	-----
Total Liabilities and Stockholders' Equity.....	\$ 3,518,955	\$ 3,648,286
	=====	=====

See accompanying notes to consolidated financial statements.

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

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	2002	2001	2002	2001
Rental revenue.....	\$ 117,369	\$ 119,544	\$ 351,043	\$ 361,745
OPERATING EXPENSES:				
Rental property.....	37,051	35,765	109,224	107,038
Depreciation and amortization.....	31,522	27,879	91,840	83,958
Interest expense:				
Contractual.....	27,522	26,381	80,673	80,955
Amortization of deferred financing costs.....	347	324	1,027	1,664
	27,869	26,705	81,700	82,619
General and administrative.....	4,147	4,784	14,858	15,447
OTHER INCOME/(EXPENSES):				
Interest and other income.....	2,829	5,070	8,912	20,438
Equity in earnings of unconsolidated affiliates.....	1,259	3,241	6,298	5,666
Nonrecurring litigation reserve.....	(2,700)	--	(2,700)	--
Nonrecurring compensation expense.....	(3,700)	--	(3,700)	--
	(2,312)	8,311	8,810	26,104
Income before gain on disposition of land and depreciable assets, minority interest, discontinued operations and extraordinary item.....	14,468	32,722	62,231	98,787
Gain on disposition of land and depreciable assets.....	3,599	3,357	12,045	16,098
Income before minority interest, discontinued operations and extraordinary item.....	18,067	36,079	74,276	114,885
Minority interest.....	(2,216)	(4,476)	(8,977)	(13,997)
Income from continuing operations.....	15,851	31,603	65,299	100,888
DISCONTINUED OPERATIONS:				
Income from discontinued operations, net of minority interest.....	1,741	2,386	5,918	8,157
Loss on sale of discontinued operations, net of minority interest.....	(3,280)	--	(1,394)	--
	(1,539)	2,386	4,524	8,157
Net income before extraordinary item.....	14,312	33,989	69,823	109,045
Extraordinary item--loss on early extinguishment of debt....	(378)	--	(378)	(518)
Net income.....	13,934	33,989	69,445	108,527
Dividends on preferred stock.....	(7,713)	(7,713)	(23,139)	(23,787)
Net income available for common shareholders.....	\$ 6,221	\$ 26,276	\$ 46,306	\$ 84,740
NET INCOME PER COMMON SHARE--BASIC:				
Income from continuing operations.....	\$ 0.16	\$ 0.45	\$ 0.79	\$ 1.41
Income/(loss) from discontinued operations.....	\$ (0.03)	\$ 0.04	\$ 0.09	\$ 0.15
Extraordinary item--loss on early extinguishment of debt.	\$ (0.01)	\$ --	\$ (0.01)	\$ (0.01)
Net income.....	\$ 0.12	\$ 0.49	\$ 0.87	\$ 1.55
Weighted average shares outstanding--basic.....	53,388	53,748	53,171	54,680
NET INCOME PER COMMON SHARE--DILUTED:				
Income from continuing operations.....	\$ 0.16	\$ 0.45	\$ 0.79	\$ 1.40
Income/(loss) from discontinued operations.....	\$ (0.03)	\$ 0.04	\$ 0.08	\$ 0.15
Extraordinary item--loss on early extinguishment of debt.	\$ (0.01)	\$ --	\$ (0.01)	\$ (0.01)
Net income.....	\$ 0.12	\$ 0.49	\$ 0.86	\$ 1.54
Weighted average shares outstanding--diluted.....	53,604	54,169	53,544	55,074
Distributions declared per common share.....	0.585	0.585	1.76	1.73



# HIGHWOODS PROPERTIES, INC.

## Consolidated Statements of Stockholders' Equity For the Nine Months Ended September 30, 2002

(Unaudited and \$ in thousands, except for number of common shares)

	NUMBER OF COMMON SHARES	COMMON STOCK	SERIES A PREFERRED	SERIES B PREFERRED	SERIES D PREFERRED	ADDITIONAL PAID-IN CAPITAL	DEFERRED COMPEN- SATION	ACCUMULATED OTHER COMPRE- HENSIVE LOSS	DISTRIBUTIONS IN EXCESS OF NET EARNINGS	TOTAL
Balance at December 31, 2001	52,891,822	529	\$ 104,945	\$172,500	\$ 100,000	\$1,376,546	\$(3,561)	\$( 9,441)	\$(135,878)	\$1,605,640
Issuance of Common Stock	235,625	2	-	-	-	5,324	-	-	-	5,326
Conversion of Common Units to Common Stock	257,121	3	-	-	-	7,471	-	-	-	7,474
Common Stock Dividends	-	-	-	-	-	-	-	-	(93,147)	(93,147)
Preferred Stock Dividends	-	-	-	-	-	-	-	-	(23,139)	(23,139)
Issuance of restricted stock	49,124	-	-	-	-	1,428	(1,428)	-	-	-
Amortization of deferred compensation	-	-	-	-	-	-	944	-	-	944
Retirement of Common Stock	(46,607)	-	-	-	-	(1,174)	-	-	-	(1,174)
Net Income	-	-	-	-	-	-	-	-	69,445	69,445
Other comprehensive loss	-	-	-	-	-	-	-	(977)	-	(977)
Balance at September 30, 2002	53,387,085	534	\$ 104,945	\$172,500	\$ 100,000	\$1,389,595	\$(4,045)	\$(10,418)	\$(182,719)	\$1,570,392

See accompanying notes to consolidated financial statements.



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

	NINE MONTHS ENDED SEPTEMBER 30,	
	2002	2001
<b>OPERATING ACTIVITIES:</b>		
Net income.....	\$ 69,445	\$ 108,527
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization.....	95,761	89,490
Amortization of deferred compensation.....	944	755
Minority interest.....	9,593	15,166
Equity in earnings of unconsolidated affiliates.....	(6,298)	(5,666)
Gain on disposition of land and depreciable assets.....	(10,468)	(16,098)
Write off of accrued straight line rent.....	3,110	--
Loss on early extinguishment of debt.....	378	518
Transition adjustment upon adoption of FASB 133.....	--	556
Loss on ineffective portion of derivative instruments.....	--	428
Changes in operating assets and liabilities.....	8,708	(17,426)
Net cash provided by operating activities.....	171,173	176,250
<b>INVESTING ACTIVITIES:</b>		
Additions to real estate assets and deferred leasing costs.....	(98,856)	(202,879)
Proceeds from disposition of real estate assets.....	164,403	157,000
Repayment of advances to subsidiaries.....	--	27,560
Distributions from unconsolidated affiliates.....	7,409	6,866
Investments in notes receivable.....	11,847	26,878
Other investing activities.....	476	1,352
Net cash provided by investing activities.....	85,279	16,777
<b>FINANCING ACTIVITIES:</b>		
Distributions paid on common stock and common units.....	(105,825)	(107,611)
Dividends paid on preferred stock.....	(23,139)	(23,787)
Payment of prepayment penalties.....	(378)	(518)
Borrowings on mortgages and notes payable.....	34,942	12,780
Repayments on mortgages and notes payable.....	(75,305)	(100,187)
Borrowings on revolving loans.....	255,500	349,000
Repayments on revolving loans.....	(332,500)	(220,000)
Net proceeds from the sale of common stock.....	5,326	817
Net change in deferred financing costs.....	1,725	155
Repurchase of stock and units.....	(3,376)	(155,308)
Net cash used in financing activities.....	(243,030)	(244,659)
Net increase/(decrease) in cash and cash equivalents.....	13,422	(51,632)
Cash and cash equivalents at beginning of the period.....	576	104,780
Cash and cash equivalents at end of the period.....	\$ 13,998	\$ 53,148
	=====	=====
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>		
Cash paid for interest.....	\$ 81,724	\$ 83,972
	=====	=====

See accompanying notes to consolidated financial statements.

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

Supplemental disclosure of non-cash investing and financing activities:

The following table summarizes the net assets contributed by the holders of Common Units in the Operating Partnership, the net assets acquired subject to mortgage notes payable and other non-cash equity transactions:

	NINE MONTHS ENDED SEPTEMBER 30,	
	2002	2001
Assets:		
Notes receivable.....	\$ --	\$ 675
Accounts receivable.....	154	--
Cash and cash equivalents.....	729	6,880
Rental property and equipment, net.....	37,098	58,012
Investment in unconsolidated affiliates.....	(1,174)	--
	-----	-----
	36,807	65,567
	=====	=====
Liabilities:		
Mortgages and notes payable.....	24,495	58,545
Accounts payable, accrued expenses and other liabilities.....	14,163	7,241
	-----	-----
	38,658	65,786
	=====	=====
Equity:.....	(1,851)	(219)
	=====	=====

See accompanying notes to consolidated financial statements.

# HIGHWOODS PROPERTIES, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2002  
(Unaudited)

### 1. DESCRIPTION OF THE COMPANY

Highwoods Properties, Inc. (the "Company") is a self-administered and self-managed real estate investment trust ("REIT") that operates in the southeastern and midwestern United States. The Company's wholly-owned assets include: 502 in-service office, industrial and retail properties; 213 apartment units; 1,251 acres of undeveloped land suitable for future development; and an additional eight properties under development.

The Company conducts substantially all of its activities through, and substantially all of its interests in the properties are held directly or indirectly by, Highwoods Realty Limited Partnership (the "Operating Partnership"). The Company is the sole general partner of the Operating Partnership. At September 30, 2002, the Company owned 88.3% of the common partnership interests ("Common Units") in the Operating Partnership. Limited partners (including certain officers and directors of the Company) own the remaining Common Units. Holders of Common Units may redeem them for the cash value of one share of the Company's common stock, \$.01 par value (the "Common Stock"), or, at the Company's option, one share of Common Stock.

When a Common Unit holder redeems a Common Unit for a share of Common Stock or cash, the minority interest will be reduced and the Company's share in the Operating Partnership will be increased. The Common Units owned by the Company are not redeemable for cash.

### 2. BASIS OF PRESENTATION

The consolidated financial statements include the accounts of the Company and the Operating Partnership and their majority-controlled affiliates. All significant intercompany balances and transactions have been eliminated in the consolidated financial statements. For a more complete discussion of our critical accounting policies, see also "Management's Discussion and Analysis of Financial Condition and Results of Operations - Critical Accounting Policies".

The extraordinary loss represents the write-off of loan origination fees and prepayment penalties paid on the early extinguishment of debt, net of the minority interest.

The Company has elected and expects to continue to qualify as a REIT under Sections 856 through 860 of the Internal Revenue Code of 1986, as amended. Therefore, no provision has been made for income taxes related to REIT taxable income to be distributed to stockholders.

Minority interest in the Company represents Common Units in the Operating Partnership owned by various individuals and entities other than the Company. Per share information is calculated using the weighted average number of shares outstanding (including common share equivalents). In addition, minority interest includes equity of consolidated real estate partnerships, which are owned by various individuals and entities and not the Company.

Certain amounts in the September 30, 2001 and December 31, 2001 financial statements have been reclassified to conform to the September 30, 2002 presentation. These reclassifications had no material effect on net income or stockholders' equity as previously reported.

The accompanying financial information has not been audited, but in the opinion of management, all adjustments (consisting of normal recurring accruals) necessary for a fair presentation of our financial position, results of operations and cash flows have been made. For further information, refer to the financial statements and notes thereto included in our 2001 Annual Report on Form 10-K.

**HIGHWOODS PROPERTIES, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued**

**2. BASIS OF PRESENTATION - Continued**

Non-recurring litigation reserve was \$2.7 million for the three months ended September 30, 2002, and was a result of an accrual of \$2.7 million to increase our reserves for the probable and estimated losses related to various legal proceedings arising in the ordinary course of business and from previously completed mergers and acquisitions.

Non-recurring compensation was \$3.7 million for the three months ended September 30, 2002, and was related to the exercise of options that occurred during the first and second quarters of 2002. When an option holder elected to exercise options, in lieu of issuing new shares upon exercise of the option and then repurchasing shares on the open market, we settled the option exercise by paying the option holder the net difference in cash between the strike price and the market value of the underlying shares. Such exercises were previously recorded as adjustments to stockholders' equity. However, the effect of such exercises should have been recorded as compensation expense under FASB Interpretation No. 44 (Accounting For Certain Transactions Involving Stock Options, An Interpretation of APB Opinion No. 25). Had we issued the shares to the option holder, received the cash for the strike price and then repurchased the shares in the market, we would not record any compensation expense. Management believes the impact of this non-recurring charge has had no material effect on net income or stockholders' equity during the first six months of 2002 as previously reported. In addition, management believes the impact of APB 25 would not have had a material effect on financial statements for prior periods. Commencing during the third quarter of 2002, we discontinued the practice of settling option exercises by paying the option holder the net difference in cash between the strike price and the market value of the underlying shares. In the event we decide to repurchase shares after an option exercise, we will require the option holder to pay the cash for the strike price and then separately repurchase a corresponding number of shares in the market under our stock repurchase program.

**HIGHWOODS PROPERTIES, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued**

**3. SEGMENT INFORMATION**

Our sole business is the acquisition, development and operation of rental real estate properties. We operate office, industrial and retail properties and apartment units. There are no material inter-segment transactions.

Our chief operating decision maker ("CDM") assesses and measures operating results based upon property level net operating income. The operating results for the individual assets within each property type have been aggregated since the CDM evaluates operating results and allocates resources on a property-by-property basis within the various property types.

Further, all operations are within the United States and no tenant comprises more than 10% of consolidated revenues. The following table summarizes the rental income, net operating income and total assets for each reportable segment for the three and nine months ended September 30, 2002 and 2001 (\$ in thousands):

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	2002	2001	2002	2001
RENTAL INCOME (A):				
Office segment	\$ 96,409	\$ 96,142	\$ 287,627	\$ 291,021
Industrial segment	10,529	11,623	31,893	35,137
Retail segment	10,083	8,970	30,380	27,325
Apartment segment	348	2,809	1,143	8,262
Total rental income	\$ 117,369	\$ 119,544	\$ 351,043	\$ 361,745
NET OPERATING INCOME (A):				
Office segment	\$ 64,308	\$ 66,560	\$ 193,924	\$ 202,748
Industrial segment	8,372	9,612	25,985	29,450
Retail segment	7,494	6,077	21,442	18,252
Apartment segment	144	1,530	468	4,257
Total Net Operating Income	\$ 80,318	\$ 83,779	\$ 241,819	\$ 254,707
RECONCILIATION TO INCOME BEFORE GAIN ON DISPOSITION OF LAND AND DEPRECIABLE ASSETS, MINORITY INTEREST, DISCONTINUED OPERATIONS AND EXTRAORDINARY ITEM:				
Equity in earnings of unconsolidated affiliates	\$ 1,259	\$ 3,241	\$ 6,298	5,666
Interest and other income	2,829	5,070	8,912	20,438
Nonrecurring litigation reserve	(2,700)	--	(2,700)	--
Nonrecurring compensation expense	(3,700)	--	(3,700)	--
Interest expense	(27,869)	(26,705)	(81,700)	(82,619)
General and administrative expenses	(4,147)	(4,784)	(14,858)	(15,447)
Depreciation and amortization	(31,522)	(27,879)	(91,840)	(83,958)
Income before gain on disposition of land and depreciable assets, minority interest, discontinued operations and extraordinary item	\$ 14,468	\$ 32,722	\$ 62,231	\$ 98,787
TOTAL ASSETS:				
Office segment	\$ 2,725,012	\$ 2,781,068	\$ 2,725,012	\$ 2,781,068
Industrial segment	326,578	334,796	326,578	334,796
Retail segment	285,373	274,581	285,373	274,581
Apartment segment	12,218	11,285	12,218	11,285
Corporate and other	169,774	223,796	169,774	223,796
Total Assets	\$ 3,518,955	\$ 3,625,526	\$ 3,518,955	\$ 3,625,526

(A) Net of discontinued operations.

**HIGHWOODS PROPERTIES, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued**

**4. INVESTMENTS IN UNCONSOLIDATED AFFILIATES**

During the past several years, we have formed various joint ventures with unrelated investors. We have retained minority equity interests ranging from 12.50% to 50.00% in these joint ventures. As required by GAAP, we have accounted for our joint venture activity using the equity method of accounting, as we do not control these joint ventures. As a result, the assets and liabilities of our joint ventures are not included on our balance sheet.

On June 26, 2002, we acquired our joint venture partner's interest in MG-HIW Rocky Point, LLC, which owned Harborview Plaza, to bring our ownership interest in that entity to 100.0%. At that time, we consolidated the assets and liabilities, and recorded income and expenses on a consolidated basis. The net income related to this joint venture until the date of purchase is included in 'Total net income' in the table below.

On September 11, 2002, we contributed Harborview Plaza to SF-HIW Harborview Plaza, LP, a newly formed limited partnership, in exchange for a 20.0% limited partnership interest. The assets, liabilities and net income from the SF-HIW Harborview Plaza, LP are included in the table below.

As of September 30, 2002, our joint ventures have approximately \$593.4 million of outstanding debt. All of the joint venture debt is non-recourse to us except (1) in the case of customary exceptions pertaining to such matters as misuse of funds, environmental conditions and material misrepresentations and

(2) with respect to \$2.5 million of construction debt related to the MG-HIW Metrowest II, LLC, which has been guaranteed by us subject to a pro rata indemnity from our joint venture partner. Our partner in SF-HIW Harborview Plaza, LP has the right to put its 80% equity interest in the partnership to us for cash at anytime during the one year period commencing on September 11, 2014. The value of the equity interest will be determined based upon the then fair market value of SF-HIW Harborview Plaza, LP's assets and liabilities. Selected financial data for our unconsolidated affiliates for the nine months ended September 30, 2002 and 2001 is presented below (\$ in thousands):

	OWNERSHIP PERCENTAGE	
	2002	2001
Board of Trade Investment Company.....	49.00%	49.00%
Dallas County Partners I, LP.....	50.00	50.00
Dallas County Partners II, LP.....	50.00	50.00
Dallas County Partners III, LP.....	50.00	50.00
Fountain Three.....	50.00	50.00
Kessinger/Hunter, LLC.....	30.00	30.00
4600 Madison Associates, LP.....	12.50	12.50
Highwoods DLF 98/29, LP.....	22.81	22.81
Highwoods DLF 97/26 DLF 99/32, LP.....	42.93	42.93
RRHWoods, LLC.....	50.00	50.00
Highwoods-Markel Associates, LLC.....	50.00	50.00
MG-HIW, LLC.....	20.00	20.00
MG-HIW Peachtree Corners, LLC.....	50.00	50.00
MG-HIW Rocky Point, LLC.....	--	50.00
MG-HIW Metrowest I, LLC.....	50.00	50.00
MG-HIW Metrowest II, LLC.....	50.00	50.00
Concourse Center Associates, LLC.....	50.00	--
Plaza Colonnade, LLC.....	50.00	--
SF-HIW Harborview Plaza, LP.....	20.00	--

  

	SEPTEMBER 30, 2002	SEPTEMBER 30, 2001
Total assets.....	\$ 924,155	\$ 903,458
Total debt.....	593,359	568,625
Total liabilities.....	617,781	601,072

  

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	2002	2001	2002	2001
Total net income.....	\$ 5,055	\$ 9,558	\$ 22,058	\$ 19,392

**HIGHWOODS PROPERTIES, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued**

**5. DERIVATIVE FINANCIAL INSTRUMENTS**

On January 1, 2001, we adopted Financial Accounting Standards Board Statement (SFAS) No. 133/138, "Accounting for Derivative Instruments and Hedging Activities," as amended. This Statement requires us to recognize all derivatives on the balance sheet at fair value. Derivatives that are not hedges must be adjusted to fair value through income. If the derivative is a hedge, depending on the nature of the hedge, changes in the fair value of the derivative will either be offset against the change in fair value of the hedged assets, liabilities or firm commitments through earnings, or recognized in Accumulated Other Comprehensive Loss ("AOCL") until the hedged item is recognized in earnings. The ineffective portion of a derivative's change in fair value is recognized in earnings. In connection with the adoption of SFAS 133/138 in January 2001, we recorded a net transition adjustment of \$555,962 of unrealized loss in interest and other income and a net transition adjustment of \$125,000 in AOCL. Adoption of the standard also resulted in our recognizing \$127,000 of derivative instrument liabilities and a reclassification of approximately \$10.6 million of deferred financing costs from past cashflow hedging relationships from other assets to AOCL.

Our interest rate risk management objective is to limit the impact of interest rate changes on earnings and cashflows and to lower overall borrowing costs. To achieve these objectives, we enter into interest rate hedge contracts such as collars, swaps, caps and treasury lock agreements in order to mitigate our interest rate risk with respect to various debt instruments. We do not hold these derivatives for trading or speculative purposes.

On the date that we enter into a derivative contract, we designate the derivative as (1) a hedge of the variability of cash flows that are to be received or paid in connection with a recognized liability (a "cash flow" hedge), or (2) an instrument that is held as a non-hedge derivative. Changes in the fair value of highly effective cash flow hedges, to the extent that the hedge is effective, are recorded in AOCL, until earnings are affected by the hedged transaction (i.e. until periodic settlements of a variable-rate liability are recorded in earnings). Any hedge ineffectiveness (which represents the amount by which the changes in the fair value of the derivative exceed the variability in the cash flows of the transaction) is recorded in current-period earnings. Changes in the fair value of non-hedging instruments are reported in current-period earnings.

We formally document all relationships between hedging instruments and hedged items, as well as the risk-management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives that are designated as cash flow hedges to (1) specific assets and liabilities on the balance sheet or (2) forecasted transactions. We also assess and document, both at the hedging instrument's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in cash flows associated with the hedged items. When we determine that a derivative is not (or has ceased to be) highly effective as a hedge, we discontinue hedge accounting prospectively.

During the nine months ended September 30, 2002, we had an interest rate swap and an interest rate collar each mature, resulting in a debit to interest rate derivative liability and an offsetting credit to AOCL of \$411,000.

As of September 30, 2002, we have two \$24.0 million treasury lock agreements related to an anticipated five-year fixed rate financing with two financial counterparties, which effectively lock the five-year treasury rate at 3.72%. These treasury lock agreements are designated as cashflow hedges and the effective portion of the cumulative loss on the derivative instruments was \$2.5 million at September 30, 2002 and is being reported as a component of AOCL in stockholders' equity. These costs will be recognized into earnings in the same period or periods during which the hedged transaction affects earnings (as the underlying debt is paid down).

Derivative liabilities totaling approximately \$2.5 million related to our treasury lock agreements, with a notional amount of \$48.0 million, are recorded in accounts payable, accrued expenses and other liabilities in the Consolidated Balance Sheets at September 30, 2002. The fair value of our interest rate swap, cap and collar agreements was \$(2.5) million at September 30, 2002.

**HIGHWOODS PROPERTIES, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued**

**5. DERIVATIVE FINANCIAL INSTRUMENTS - Continued**

At September 30, 2002, approximately \$7.9 million of deferred financing costs from past cash flow hedging instruments remain in AOCL. These costs will be recognized into earnings as the underlying debt is repaid. We expect that the portion of the cumulative loss recorded in AOCL at September 30, 2002 associated with the derivative instruments, which will be recognized within the next 12 months, will be approximately \$1.6 million.

**6. OTHER COMPREHENSIVE INCOME/(LOSS)**

Other comprehensive income/(loss) represents net income plus the results of certain non-stockholders' equity changes not reflected in the Consolidated Statements of Income. The components of other comprehensive income/(loss) are as follows (\$ in thousands):

	NINE MONTHS ENDED 2002	SEPTEMBER 30, 2001
Net Income.....	\$ 69,445	\$ 108,527
Accumulated other comprehensive income/(loss):		
Unrealized derivative losses on cashflow hedges.....	(2,134)	(514)
Reclassification of past hedging relationships.....	--	(10,597)
Amortization of past hedging relationships.....	1,157	1,175
	-----	-----
Total other comprehensive loss .....	(977)	(9,936)
	-----	-----
Total comprehensive income.....	\$ 68,468	\$ 98,591
	=====	=====

**7. DISCONTINUED OPERATIONS AND THE IMPAIRMENT OF LONG-LIVED ASSETS**

As of January 1, 2002, we adopted Financial Accounting Standards Board Statement No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," ("SFAS 144") and the appropriate amounts are disclosed separately under income from discontinued operations on the consolidated income statement. Below represents the income statement and net carrying value of the properties sold and held for sale at September 30, 2002 (which account for 2,148,446 rentable square feet and 88 units) as a result of our capital recycling program and included in income from discontinued operations for the three and nine months ended September 30, 2002 and 2001 (in thousands):

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	2002	2001	2002	2001
Total revenue	\$ 5,460	\$ 6,286	\$ 16,669	\$ 19,125
Rental operating expenses	(1,985)	(1,932)	(5,831)	(5,931)
Depreciation and amortization	(1,305)	(1,624)	(3,921)	(3,868)
Interest Expense	(200)	--	(200)	--
	-----	-----	-----	-----
Income before loss on disposition of depreciable assets and minority interest	1,970	2,730	6,717	9,326
Loss on disposition of depreciable assets	(3,712)	--	(1,577)	--
	-----	-----	-----	-----
Income/(loss) before minority interest	(1,742)	2,730	5,140	9,326
Minority interest	203	(344)	(616)	(1,169)
	-----	-----	-----	-----
Income/(loss) from discontinued operations	\$ (1,539)	\$ 2,386	\$ 4,524	\$ 8,157
	=====	=====	=====	=====
Net carrying value	\$ 123,350	\$ 153,297	\$ 123,350	\$ 153,297
	=====	=====	=====	=====

In addition, in accordance with SFAS 144, we have determined that as of September 30, 2002, the carrying value of three office properties held will not be recovered from their projected undiscounted future operating cash flows. We have recognized a \$4.5 million impairment loss, which is included in the gain on the sale of land and depreciable assets in the consolidated statements of income for the three and nine months ended September 30, 2002.



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

The following discussion should be read in conjunction with all of the financial statements appearing elsewhere in the report and is based primarily on the consolidated financial statements of the Company.

### DISCLOSURE REGARDING FORWARD-LOOKING STATEMENTS

Some of the information in this Quarterly Report on Form 10-Q may contain forward-looking statements. Such statements include, in particular, statements about our plans, strategies and prospects under this section and under the heading "Business". You can identify forward-looking statements by our use of forward-looking terminology such as "may," "will," "expect," "anticipate," "estimate," "continue" or other 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:

- . speculative development activity by our competitors in our existing markets could result in an excessive supply of office, industrial and retail properties relative to tenant demand;
- . the financial condition of our tenants could deteriorate;
- . the costs of our development projects could exceed our original estimates;
- . we may not be able to complete development, acquisition, reinvestment, disposition or joint venture projects as quickly or on as favorable terms as anticipated;
- . we may not be able to lease or re-lease space quickly or on as favorable terms as old leases;
- . we may have incorrectly assessed the environmental condition of our properties;
- . an unexpected increase in interest rates would increase our debt service costs;
- . we may not be able to continue to meet our long-term liquidity requirements on favorable terms;
- . we could lose key executive officers; and
- . our southeastern and midwestern markets may suffer additional declines in economic growth or may not recover as fully or as quickly as expected.

This list of risks and uncertainties, however, is not intended to be exhaustive. You should also review the other cautionary statements we make in "Business - Risk Factors" set forth in our 2001 Annual Report.

Given these uncertainties, we caution you not to place undue reliance on forward-looking statements. We undertake no obligation to publicly release the results of any revisions to these forward-looking statements that may be made to reflect any future events or circumstances, or to reflect the occurrence of unanticipated events.

### OVERVIEW

We are a self-administered and self-managed equity REIT that began operations through a predecessor in 1978. Since the Company's initial public offering in 1994, we have evolved into one of the largest owners and operators of suburban office, industrial and retail properties in the southeastern and midwestern United States. At September 30, 2002, we:

- . owned 502 in-service office, industrial and retail properties, encompassing approximately 38.0 million rentable square feet;
- . owned an interest (50.0% or less) in 78 in-service office and industrial properties, encompassing

approximately 7.7 million rentable square feet and 418 apartment units;

. owned 1,251 acres (and have agreed to purchase an additional eight acres over the next year) of undeveloped land suitable for future development;

. owned eight development properties, encompassing approximately 824,000 rentable square feet; and

. owned an interest (50.0% or less) in one development property, encompassing 285,000 rentable square feet.

The following summarizes our capital recycling program since the beginning of 2000:

	NINE MONTHS ENDED September 30, 2002	YEAR ENDED 2001	YEAR ENDED 2000
	-----	-----	-----
OFFICE, INDUSTRIAL AND RETAIL PROPERTIES (rentable square feet in thousands)			
Dispositions (1).....	(856)	(268)	(4,743)
Contributions to Joint Ventures (1).....	(205)	(118)	(2,199)
Developments Placed In-Service.....	1,614	1,351	3,480
Acquisitions.....	205	72	669
	-----	-----	-----
Net Change in Wholly-owned In-Service Properties.....	758	1,037	(2,793)
	=====	=====	=====
APARTMENT PROPERTIES (in units)			
Dispositions.....	--	(1,672)	--
	=====	=====	=====

(1) Excludes wholly-owned development projects sold or contributed to joint ventures.

In addition to the above property activity, we repurchased \$3.4 million, \$147.4 million and \$100.2 million of Common Stock and Common Units during 2002, 2001 and 2000, respectively, and \$18.5 million of Preferred Stock during 2001. This represents aggregate repurchases of \$269.5 million of Common Stock, Common Units and Preferred Stock since January 1, 2000.

The Company conducts substantially all of its activities through, and substantially all of its interests in the properties are held directly or indirectly by, the Operating Partnership. The Company is the sole general partner of the Operating Partnership. At September 30, 2002, the Company owned 88.3% of the Common Units in the Operating Partnership.

## CRITICAL ACCOUNTING POLICIES

Our discussion and analysis of financial condition and results of operations is based upon our Consolidated Financial Statements contained elsewhere in this Quarterly Report. Our Consolidated Financial Statements include the accounts of the Company and the Operating Partnership and their majority-controlled affiliates. For a discussion of our accounting policies with respect to our investments in joint ventures, see "Investments in Joint Ventures". The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses for the reporting period. Actual results could differ from our estimates.

The estimates used in the preparation of our Consolidated Financial Statements are more fully described in Note (1) to our audited Consolidated Financial Statements for the year ended December 31, 2001, included in our 2001 Form 10-K. However, certain of our significant accounting policies are considered critical accounting policies due to the increased level of assumptions used or estimates made in determining their impact on our Consolidated Financial Statements presented for any interim period. Management has reviewed our critical accounting policies and estimates with the audit committee of the Company's board of directors.

We consider our critical accounting policies to be those used in the determination of the reported amounts and

disclosure related to the following:

- . Impairment of long-lived assets;
- . Allowance for doubtful accounts;
- . Capitalized costs;
- . Fair value of derivative instruments;
- . Rental revenue; and
- . Investments in joint ventures.

**Impairment of long-lived assets.** Real estate and leasehold improvements are classified as long-lived assets held for sale or as long-lived assets to be held and used. In accordance with Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," we record assets held for sale at the lower of the carrying amount or fair value less cost to sell. The impairment loss is the amount by which the carrying amount exceeds the fair value less cost to sell. With respect to assets classified as held and used, we periodically review these assets to determine whether our carrying amount will be recovered from their undiscounted future operating cash flows and we recognize an impairment loss to the extent we believe the carrying amount is not recoverable. Our determination of future operating cash flows requires us to make assumptions related to future rental rates, tenant concessions, operating expenditures, property taxes and capital improvements. If our assumptions prove incorrect and our estimates of future operating cash flows are materially overstated, we could be required to recognize future impairment losses on our properties.

**Allowance for doubtful accounts.** Accounts receivable are reduced by an allowance for amounts that may become uncollectible in the future. Our receivable balance is comprised primarily of rents and operating cost recoveries due from tenants as well as accrued rental rate increases to be received over the life of the existing leases. We regularly evaluate the adequacy of our allowance for doubtful accounts considering such factors as the credit quality of our tenants, delinquency of payment, historical trends and current economic conditions. Actual results may differ from these estimates under different assumptions or conditions. If our assumptions regarding the collectibility of accounts receivables prove incorrect, we could experience write-offs of accounts receivable or accrued straight-line rents receivable in excess of our allowance for doubtful accounts.

**Capitalized costs.** Expenditures directly related to both the development of real estate assets and the leasing of properties are included in net real estate assets and are stated at cost in the consolidated balance sheets. The development expenditures include pre-construction costs essential to the development of properties, development and construction costs, interest costs, real estate taxes, salaries and other costs incurred during the period of development. The leasing expenditures include all general and administrative costs, including salaries incurred in connection with successfully securing leases on the properties. Estimated costs related to unsuccessful leases are expensed as incurred. If our assumptions regarding the successful efforts of development and leasing are incorrect, the resulting adjustments could impact earnings.

**Fair value of derivative instruments.** In the normal course of business, we are exposed to the effect of interest rate changes. We limit our exposure by following established risk management policies and procedures including the use of derivatives. To mitigate our exposure to unexpected changes in interest rates, derivatives are used primarily to hedge against rate movements on our related debt. We are required to recognize all derivatives as either assets or liabilities in the consolidated balance sheets and to measure those instruments at fair value. Changes in fair value will affect either stockholders' equity or net income depending on whether the derivative instrument qualifies as a hedge for accounting purposes.

To determine the fair value of derivative instruments, we use a variety of methods and assumptions that are based on market conditions and risks existing at each balance sheet date. For the majority of financial instruments, including most derivatives, standard market conventions and techniques such as discounted cash flow analysis, option pricing modes, replacement cost and termination cost are used to determine fair value. All methods of assessing fair value result in a general approximation of value, and such value may never actually be realized.

Rental revenue. Rental revenue is comprised of base rent, including termination fees, recoveries from tenants and parking and other income. In accordance with GAAP, base rental revenue is recognized on a straight-line basis over the terms of the respective leases. This means that, with respect to a particular lease, actual amounts billed in accordance with the lease during any given period may be higher or lower than the amount of rental revenue recognized for the period. Accrued straight-line rents receivable represents the amount by which straight-line rental revenue exceeds rents currently billed in accordance with lease agreements. Recoveries from tenants represent reimbursements for certain costs as provided in the lease agreements. These costs generally include real estate taxes, utilities, insurance, common area maintenance and other recoverable costs.

Investments in joint ventures. Our investments in unconsolidated affiliates consist of one corporation, nine limited liability companies, four limited partnerships and two general partnerships. We account for our investments in unconsolidated affiliates under the equity method of accounting as we exercise significant influence, but do not control these entities. Our unconsolidated corporation is controlled by an unrelated third party that owns more than 50% of the outstanding voting stock. We have a 50% or less ownership interest in the unconsolidated limited liability companies and, under the terms of the various operating agreements, do not have any participating rights. We have a 50% or less ownership interest in the unconsolidated limited partnerships and general partnerships. Although we have an interest in two unconsolidated general partnerships and are the general partner in three of the unconsolidated limited partnerships, under the terms of the various partnership agreements, we do not have control of the major operating and financial policies of these unconsolidated partnerships.

These investments are initially recorded at cost, as investments in unconsolidated affiliates, and are subsequently adjusted for equity in earnings and cash contributions and distributions. Any difference between the carrying amount of these investments on our balance sheet and the underlying equity in net assets is amortized as an adjustment to equity in earnings of unconsolidated affiliates over the life of the property, generally 40 years.

From time to time, we contribute real estate assets to an unconsolidated joint venture in exchange for a combination of cash and an equity interest in the venture. We record a partial gain on the contribution of the real estate assets to the extent of the third party investor's interest and record a deferred gain to the extent of our continuing interest in the unconsolidated joint venture.

In connection with the MG-HIW, LLC joint venture, we have guaranteed Miller Global, our partner who has an 80.0% interest in the joint venture, a minimum internal rate of return on \$50.0 million of their equity. If the minimum internal rate of return is not achieved upon the sale of the assets or winding up of the joint venture, Miller Global would receive a disproportionately greater interest of the cash proceeds related to the assets subject to the internal rate of return guarantee. Based upon the current and forecasted operating performance of the assets and our estimate of the residual value of the subject assets, the estimated internal rate of return for Miller Global with respect to their equity is not less than the minimum required return. As a result, we do not currently expect that our interest in the joint venture will be adjusted upon the sale of the subject assets or the winding up of the joint venture as a result of the internal rate of return guarantee. However, if our assumptions and estimates prove incorrect, Miller Global could receive a greater interest of the cash proceeds from any such sale or winding up.

## RESULTS OF OPERATIONS

The following table sets forth information regarding our results of operations for the three and nine months ended September 30, 2002 and 2001 (\$ in millions):

	THREE MONTHS ENDED SEPTEMBER 30,			NINE MONTHS ENDED SEPTEMBER 30,		
	2002	2001	\$ Change	2002	2001	\$ Change
Rental revenue .....	\$ 117.4	\$ 119.5	\$ (2.1)	\$ 351.0	\$ 361.7	\$ (10.7)
Operating expenses:						
Rental property.....	37.1	35.8	1.3	109.2	107.0	2.2
Depreciation and amortization.....	31.5	27.9	3.6	91.8	84.0	7.8
Interest expense:						
Contractual.....	27.5	26.4	1.1	80.7	80.9	(0.2)
Amortization of deferred financing costs.....	0.4	0.3	0.1	1.0	1.7	(0.7)
	27.9	26.7	1.2	81.7	82.6	(0.9)
General and administrative.....	4.1	4.7	(0.6)	14.9	15.4	(0.5)
Other Income/(Expenses):						
Interest and other income.....	2.8	5.1	(2.3)	8.9	20.4	(11.5)
Equity in earnings of unconsolidated affiliates...	1.3	3.2	(1.9)	6.3	5.7	0.6
Nonrecurring litigation reserve.....	(2.7)	--	(2.7)	(2.7)	--	(2.7)
Nonrecurring compensation expense.....	(3.7)	--	(3.7)	(3.7)	--	(3.7)
	(2.3)	8.3	(10.6)	8.8	26.1	(17.3)
Income before gain on disposition of land and depreciable assets, minority interest, discontinued operations and extraordinary item	14.5	32.7	(18.2)	62.2	98.8	(36.6)
Gain on disposition of land and depreciable assets	3.6	3.4	0.2	12.1	16.1	(4.0)
Income before minority interest, discontinued operations and extraordinary item.....	18.1	36.1	(18.0)	74.3	114.9	(40.6)
Minority interest.....	(2.2)	(4.5)	2.3	(9.0)	(14.0)	5.0
Income from continuing operations.....	15.9	31.6	(15.7)	65.3	100.9	(35.6)
Discontinued operations:						
Income from discontinued operations, net of minority interest.....	1.7	2.4	(0.7)	5.9	8.1	(2.2)
Loss on sale of discontinued operations, net of minority interest.....	(3.3)	--	(3.3)	(1.4)	--	(1.4)
	(1.6)	2.4	(4.0)	4.5	8.1	(3.6)
Net income before extraordinary item.....	14.3	34.0	(19.7)	69.8	109.0	(39.2)
Extraordinary item -- loss on early extinguishment of debt.....	(0.4)	--	(0.4)	(0.4)	(0.5)	0.1
Net income.....	13.9	34.0	(20.1)	69.4	108.5	(39.1)
Dividends on preferred stock.....	(7.7)	(7.7)	--	(23.1)	(23.8)	0.7
Net income available for common shareholders.....	\$ 6.2	\$ 26.3	\$ (20.1)	\$ 46.3	\$ 84.7	\$ (38.4)
	=====	=====	=====	=====	=====	=====

Three Months Ended September 30, 2002. Revenues from rental operations decreased \$2.1 million, or 1.8%, to \$117.4 million for the three months ended September 30, 2002 from \$119.5 million for the three months ended September 30, 2001. The decrease was primarily due to a decrease in the average occupancy rates from 92.7% in the third quarter of 2001 to 86.3% in the third quarter of 2002. Slightly offsetting the decrease was an increase in rental revenues as a result of an increase in our property portfolio in 2002 as a result of our capital recycling program, which included 1.6 million rentable square feet of properties that were placed in service during 2002. Our in-service wholly-owned portfolio increased from 36.9 million rentable square feet at September 30, 2001 to 38.0 million rentable square feet at September 30, 2002.

Same property rental revenue, recorded in accordance with GAAP, generated from the 475 in-service properties wholly-owned on January 1, 2001, decreased \$4.2 million, or 3.6%, for the three months ended September 30, 2002, compared to the three months ended September 30, 2001. Same store straight-line rent decreased \$1.1 million as a result of lower occupancy with fewer new leases recording straight-line rent and the impact from straight-lining of

rents on existing tenants discussed generally in our critical accounting policies. Same store rental revenues excluding straight-line rent and termination fees decreased \$4.2 million, or 3.7%. This decrease is a result of lower same store average occupancy, which declined from 92.5% in the third quarter of 2001 to 86.8% in the third quarter of 2002.

During the three months ended September 30, 2002, 242 second generation leases representing 1.5 million square feet of office, industrial and retail space were executed at an average rate per square foot, which was 9.3% lower than the average rate per square foot on the previous leases.

Rental operating expenses (real estate taxes, utilities, insurance, repairs and maintenance and other property-related expenses) increased \$1.3 million, or 3.6%, to \$37.1 million for the three months ended September 30, 2002 from \$35.8 million for the three months ended September 30, 2001. This increase was primarily a result of increases in real estate taxes, primarily due to higher property tax assessments, utilities and small increases in various other rental expenses in the third quarter of 2002, offset by lower occupancy relative to variable operating expenses. Rental operating expenses as a percentage of related rental revenues increased to 31.6% for the three months ended September 30, 2002 from 30.0% for the three months ended September 30, 2001. The increase was primarily due to an increase in rental operating expenses related to the increase in real estate taxes and a decrease in rental revenues related to lower average occupancy during the three months ended September 30, 2002.

Same property rental property expenses, which are the expenses of the 475 in-service properties wholly-owned on January 1, 2001, increased \$456,000, or 1.3%, for the three months ended September 30, 2002, compared to the three months ended September 30, 2001. This increase was primarily a result of increases in real estate taxes, primarily due to higher property tax assessments, utilities and small increases in various other rental expense accounts in the third quarter of 2002.

Depreciation and amortization for the three months ended September 30, 2002 and 2001 totaled \$31.5 million and \$27.9 million, respectively. The increase of \$3.6 million, or 12.9%, was due to an increase in the amortization of leasing commissions and tenant improvements and an increase in depreciation expense related to buildings placed in service during 2001 and 2002, partly offset by a decrease in the depreciation expense as a result of dispositions during 2002 and 2001.

Interest expense increased \$1.2 million, or 4.5%, to \$27.9 million for the three months ended September 30, 2002 from \$26.7 million for the three months ended September 30, 2001. The increase was attributable to a decrease in capitalized interest during the three months ended September 30, 2002, offset by a decrease in weighted average interest rates during the three months ended September 30, 2002. Interest expense for the three months ended September 30, 2002 and 2001 included \$347,000 and \$324,000, respectively, of amortization of deferred financing costs. Capitalized interest for the three months ended September 30, 2002 and 2001 was \$1.7 million and \$4.0 million, respectively.

General and administrative expenses as a percentage of rental revenue, interest and other income, and equity in earnings of unconsolidated affiliates was 3.4% in the third quarter of 2002 and 3.7% in the third quarter of 2001. The increase is primarily due to a non-recurring increase in management fee expense related to certain executives that provide management services to the Operating Partnership. These executives are employees of the Company, which is the managing general partner of the Operating Partnership.

Interest and other income decreased \$2.3 million, or 45.1%, to \$2.8 million for the three months ended September 30, 2002 from \$5.1 million for the three months ended September 30, 2001. The decrease primarily resulted from a decrease in development fee income and a decrease in interest income in the three months ended September 30, 2002 due to the collection of notes receivable during 2001 and 2002.

Equity in earnings of unconsolidated affiliates decreased \$1.9 million, or 59.4%, to \$1.3 million for the three months ended September 30, 2002 from \$3.2 million for the three months ended September 30, 2001. The decrease was attributable to an accrual made in 2001 by the Iowa joint ventures to reflect reimbursements for real estate taxes paid in 2001 and years prior. In 2002, these payments have been accounted for when they have been received.

Non-recurring litigation reserve was \$2.7 million for the three months ended September 30, 2002, and was a result of an accrual of \$2.7 million to increase our reserves for the probable and estimated losses related to various legal proceedings arising in the ordinary course of business and from previously completed mergers and acquisitions.

Non-recurring compensation was \$3.7 million for the three months ended September 30, 2002, and was related to the exercise of options that occurred during the first and second quarters of 2002. When an option holder elected to exercise options, in lieu of issuing new shares upon exercise of the option and then repurchasing shares on the open market, we settled the option exercise by paying the option holder the net difference in cash between the strike price and the market value of the underlying shares. Such exercises were previously recorded as adjustments to stockholders' equity. However, the effect of such exercises should have been recorded as compensation expense under FASB Interpretation No. 44 (Accounting For Certain Transactions Involving Stock Options, An Interpretation of APB Opinion No. 25). Had we issued the shares to the option holder, received the cash for the strike price and then repurchased the shares in the market, we would not record any compensation expense. Management believes the impact of this non-recurring charge has had no material effect on net income or stockholders' equity during the first six months of 2002 as previously reported. In addition, management believes the impact of APB 25 would not have had a material effect on financial statements for prior periods. Commencing during the third quarter of 2002, we discontinued the practice of settling option exercises by paying the option holder the net difference in cash between the strike price and the market value of the underlying shares. In the event we decide to repurchase shares after an option exercise, we will require the option holder to pay the cash for the strike price and then separately repurchase a corresponding number of shares in the market under our stock repurchase program.

Income before gain on disposition of land and depreciable assets, minority interest, discontinued operations and extraordinary item equaled \$14.5 million and \$32.7 million for the quarters ended September 30, 2002 and 2001, respectively. The Company's net income allocated to minority interest totaled \$2.2 million and \$4.5 million for the quarters ended September 30, 2002 and 2001, respectively. The Company recorded \$7.7 million in preferred stock dividends for each of the quarters ended September 30, 2002 and 2001, respectively.

Gain on disposition of land and depreciable assets increased \$242,000, or 5.9%, to \$3.6 million for the quarter ended September 30, 2002 from \$3.4 million for the quarter ended September 30, 2001. In the third quarter of 2001, the majority of the gain was comprised of a gain of approximately \$4.1 million related to the disposition of 512 apartment units, partly offset by a loss of approximately \$126,000 related to the disposition of 579,515 rentable square feet of office properties and by a loss of approximately \$538,000 related to the disposition of 77 acres of land. In the third quarter of 2002, the gain primarily consisted of \$2.7 million of additional gain that resulted from the sale of a building during the second quarter of 2002 that had not been entirely recorded during that period due to an error in the consolidation process and a gain of approximately \$741,000 related to the disposition of 25 acres of land.

Income from discontinued operations, net of minority interest, decreased from \$2.4 million for the three months ended September 30, 2001 to \$1.7 million for the three months ended September 30, 2002. The decrease was a result of the decrease in income from discontinued operations for properties sold during 2002.

Loss on sale of discontinued operations, net of minority interest, was \$3.3 million during the three months ended September 30, 2002, which represented an impairment charge related to two properties held for sale at September 30, 2002.

Nine Months Ended September 30, 2002. Revenues from rental operations decreased \$10.7 million, or 3.0%, to \$351.0 million for the nine months ended September 30, 2002 from \$361.7 million for the nine months ended September 30, 2001. The decrease was primarily due to a decrease in the average occupancy rates from 93.4% for the nine months ended September 30, 2001 to 87.5% for the nine months ended September 30, 2002. In addition, we wrote off approximately \$3.1 million of accrued straight-line rent receivables from WorldCom and its affiliates during the second quarter of 2002. Our in-service wholly-owned portfolio increased from 36.9 million rentable square feet at September 30, 2001 to 38.0 million rentable square feet at September 30, 2002.

Same property rental revenue, recorded in accordance with GAAP, generated from the 475 wholly-owned in-service properties on January 1, 2001, decreased \$13.9 million for the nine months ended September 30, 2002 compared to the nine months ended September 30, 2001. Same store straight-line rent decreased \$6.3 million as a result of the \$3.1 million write-off of bankrupt tenant WorldCom's accrued straight-line rent receivable, lower occupancy with fewer new leases recording straight-line rent and the impact from straight lining of rents on existing tenants discussed generally in our critical accounting policies. Same store revenues excluding straight-line rent and termination fees decreased \$9.5 million, or 2.8%. This decrease is a result of lower same store average occupancy, which declined from 93.2% in the first nine months of 2001 to 87.7% in the first nine months of 2002.

During the nine months ended September 30, 2002, 586 second generation leases representing 4.0 million square feet of office, industrial and retail space were executed at an average rate per square foot which was 4.8% lower than the average rate per square foot on the previous leases.

Rental operating expenses (real estate taxes, utilities, insurance, repairs and maintenance and other property-related expenses) increased \$2.2 million, or 2.1%, to \$109.2 million for the nine months ended September 30, 2002 from \$107.0 million for the nine months ended September 30, 2001. The increase was primarily a result of an increase in real estate taxes in the first nine months of 2002, primarily due to higher property tax assessments, utilities and small increases in various other rental expenses in 2002, offset by lower occupancy relative to variable operating expenses. Rental operating expenses as a percentage of related rental revenues increased to 31.1% for the nine months ended September 30, 2002 from 29.6% for the nine months ended September 30, 2001. The increase was primarily due to an increase in rental operating expenses related to the increase in real estate taxes and a decrease in rental revenues related to lower average occupancy during the nine months ended September 30, 2002.

Same property rental property expenses, which are the expenses of the 475 in-service properties wholly-owned on January 1, 2001, remained consistent for the nine months ended September 30, 2002, compared to the nine months ended September 30, 2001.

Depreciation and amortization for the nine months ended September 30, 2002 and 2001 totaled \$91.8 million and \$84.0 million, respectively. The increase of \$7.8 million, or 9.3%, was due to an increase in the amortization of leasing commissions and tenant improvements and an increase in depreciation expense related to buildings placed in service during 2001 and 2002, partly offset by a decrease in the depreciation expense as a result of dispositions during 2002 and 2001.

Interest expense decreased \$919,000, or 1.1%, to \$81.7 million for the nine months ended September 30, 2002 from \$82.6 million for the nine months ended September 30, 2001. The decrease was primarily attributable to the decrease in the weighted average interest rates for the nine months ended September 30, 2002, partly offset by an increase in the average outstanding debt for the nine months ended September 30, 2002 and a decrease in capitalized interest during the nine months ended September 30, 2002. Interest expense for the nine months ended September 30, 2002 and 2001 included \$1.0 million and \$1.7 million, respectively, of amortization of deferred financing costs. The decrease in amortization of deferred financing costs from September 30, 2001 to September 30, 2002 was related to loan fees which were amortized fully during 2001. Capitalized interest for the nine months ended September 30, 2002 and 2001 was \$8.3 million and \$11.0 million, respectively.

General and administrative expenses as a percentage of rental revenue, interest and other income, and equity in earnings of unconsolidated affiliates was 4.1% and 4.0% in the first nine months of 2002 and 2001, respectively. The increase is primarily due to a non-recurring increase in management fee expense related to certain executives that provide management services to the Operating Partnership. These executives are employees of the Company, which is the managing general partner of the Operating Partnership. The increase is partly offset by a decrease in revenue due to lower average occupancy during the nine months ended September 30, 2002 and 2001.

Interest and other income decreased \$11.5 million, or 56.4%, to \$8.9 million for the nine months ended September 30, 2002 from \$20.4 million for the nine months ended September 30, 2001. The decrease primarily resulted from a decrease in leasing and development fee income in the nine months ended September 30, 2002 and a decrease in interest income in the nine months ended September 30, 2002 due to lower average cash balances (during 2001, we had higher cash balances as a result of proceeds from dispositions related to our capital recycling program that were ultimately used in our stock repurchase program) and the collection of notes receivable during 2001 and 2002.

Equity in earnings of unconsolidated affiliates increased \$632,000, or 10.5%, to \$6.3 million for the nine months ended September 30, 2002 from \$5.7 million for the nine months ended September 30, 2001. The increase was primarily a result of earnings from certain joint ventures formed with unrelated investors in 2002.

Non-recurring litigation reserve was \$2.7 million for the nine months ended September 30, 2002, and was a result of an accrual of \$2.7 million to increase our reserves for the probable and estimated losses related to various legal proceedings arising in the ordinary course of business and from previously completed mergers and acquisitions.

Non-recurring compensation was \$3.7 million for the nine months ended September 30, 2002, and was related to the exercise of options that occurred during the first and second quarters of 2002. When an option holder elected



to exercise options, in lieu of issuing new shares upon exercise of the option and then repurchasing shares on the open market, we settled the option exercise by paying the option holder the net difference in cash between the strike price and the market value of the underlying shares. Such exercises were previously recorded as adjustments to stockholders' equity. However, the effect of such exercises should have been recorded as compensation expense under FASB Interpretation No. 44 (Accounting For Certain Transactions Involving Stock Options, An Interpretation of APB Opinion No. 25). Had we issued the shares to the option holder, received the cash for the strike price and then repurchased the shares in the market, we would not have been required to record any compensation expense. Management believes the impact of this non-recurring charge has had no material effect on net income or stockholders' equity during the first six months of 2002 as previously reported. In addition, management believes the impact of APB 25 would not have had a material effect on financial statements for prior periods. Commencing during the third quarter of 2002, we discontinued the practice of settling option exercises by paying the option holder the net difference in cash between the strike price and the market value of the underlying shares. In the event we decide to repurchase shares after an option exercise, we will require the option holder to pay the cash for the strike price and then separately repurchase a corresponding number of shares in the market under our stock repurchase program.

Income before gain on disposition of land and depreciable assets, minority interest, discontinued operations and extraordinary item equaled \$62.2 million and \$98.8 million for the nine months ended September 30, 2002 and 2001, respectively. The Company's net income allocated to minority interest totaled \$9.0 million and \$14.0 million for the nine months ended September 30, 2002 and 2001, respectively. The Company recorded \$23.1 million and \$23.8 million in preferred stock dividends for each of the nine months ended September 30, 2002 and 2001, respectively. The decrease was a result of the \$18.5 million repurchase by the Company of its preferred stock during 2001.

Gain on disposition of land and depreciable assets decreased \$4.0 million, or 24.8%, to \$12.1 million for the nine months ended September 30, 2002 from \$16.1 million for the nine months ended September 30, 2001. In the first nine months of 2001, the majority of the gain was comprised of a gain of approximately \$15.6 million related to the disposition of 1,672 apartment units and a gain of approximately \$1.0 million related to the disposition of 160 acres of land, partly offset by a loss of approximately \$508,000 related to the disposition of 795,331 rentable square feet of office properties. In the first nine months of 2002, the majority of the gain was comprised of a gain of approximately \$14.8 million related to the disposition of 533,263 rentable square feet of office properties and a gain of approximately \$6.5 million related to the disposition of 78 acres of land and other non-revenue producing assets, partly offset by an impairment loss of approximately \$9.1 million.

Income from discontinued operations, net of minority interest, decreased from \$8.2 million for the nine months ended September 30, 2001 to \$5.9 million for the nine months ended September 30, 2002. The decrease was a result of the decrease in income from discontinued operations for properties sold during 2002.

Loss on sale of discontinued operations, net of minority interest, was \$1.4 million for the nine months ended September 30, 2002. This amount was comprised of an impairment charge of \$4.0 million related to properties held for sale at September 30, 2002 offset by gains in aggregate of approximately \$2.6 million related to the disposition of 331,747 rentable square feet.

## LIQUIDITY AND CAPITAL RESOURCES

Statement of Cash Flows. The following table sets forth the changes in the Company's cash flows from the first nine months of 2001 as compared to the first nine months of 2002 (\$ in thousands):

	NINE MONTHS ENDED SEPTEMBER 30,		
	2002	2001	CHANGE
Cash Provided By Operating Activities	\$ 171,173	\$ 176,250	\$ (5,077)
Cash Provided By Investing Activities	85,279	16,777	68,502
Cash Used in Financing Activities	(243,030)	(244,659)	1,629

The decrease in cash provided by operating activities was primarily the result of (1) a decrease in average occupancy rates for our wholly-owned portfolio; (2) our capital recycling program; and (3) a decrease in interest income and development and leasing income in the first nine months of 2002. In addition, the level of net cash provided by operating activities is also affected by the timing of receipt of revenues and payment of expenses.

The increase in cash provided by investing activities was primarily a result of a decrease of \$104.0 million in additions to real estate assets in the first nine months of 2002, partly offset by a decrease of \$15.0 million in the investments in notes receivable from the first nine months of 2001 to the first nine months of 2002 and a decrease in the collection of advances from subsidiaries of \$27.6 million from the first nine months of 2001 to the first nine months of 2002.

The decrease in cash used in financing activities was primarily a result of a decrease of \$151.9 million in the repurchase of Common Stock and Common Units from the first nine months of 2001 to the first nine months of 2002, a decrease of \$2.4 million in distributions paid on Common Stock, Common Units and Preferred Stock during 2002 and an increase in net proceeds from the sale of Common Stock of \$4.5 million during 2002. These decreases were partially offset by an increase in repayments of \$87.6 million and a decrease in borrowings of \$71.3 million on the unsecured revolving loan, mortgages and notes payable during 2002.

Capitalization. Based on our total market capitalization of \$3.42 billion at September 30, 2002 (at the September 30, 2002 stock price of \$23.40 and assuming the redemption for shares of Common Stock of the 7.0 million Common Units of minority interest in the Operating Partnership), our debt represented approximately 47.6% of our total market capitalization. Our total indebtedness at September 30, 2002 was \$1.62 billion and was comprised of \$523.4 million of secured indebtedness with a weighted average interest rate of 7.9% and \$1.1 billion of unsecured indebtedness with a weighted average interest rate of 6.5%. We do not intend to reserve funds to retire existing secured or unsecured debt upon maturity. For a more complete discussion of our long-term liquidity needs, see "Current and Future Cash Needs."

The following table sets forth the maturity schedule of our mortgages and notes payable as of September 30, 2002 (\$ in thousands):

	TOTAL	WITHIN 1 YEAR	WITHIN 2-3 YEARS	WITHIN 4-5 YEARS	WITHIN 6 OR MORE YEARS
Fixed Rate Debt:					
Unsecured:					
MOPPRS (1).....	\$ 125,000	\$ -	\$ -	\$ -	\$ 125,000
Put Option Notes (2).....	100,000	-	-	-	100,000
Notes.....	706,500	-	246,500	110,000	350,000
Secured:					
Mortgages and loans payable.....	517,859	10,044	90,467	90,461	326,887
Total Fixed Rate Debt.....	1,449,359	10,044	336,967	200,461	901,887
Variable Rate Debt:					
Unsecured:					
Term Loan.....	20,000	-	20,000	-	-
Revolving Loan.....	151,500	-	151,500	-	-
Secured:					
Revolving Loan.....	1,129	1,129	-	-	-
Mortgage loan payable.....	4,374	247	538	3,589	-
Total Variable Rate Debt.....	177,003	1,376	172,038	3,589	-
Total Mortgages and Notes payable.....	\$ 1,626,362	\$ 11,420	\$ 509,005	\$ 204,050	\$ 901,887

(1) On February 2, 1998, the Operating Partnership sold \$125.0 million of MandatOry Par Put Remarketed Securities ("MOPPRS") due February 1, 2013. The MOPPRS bear an interest rate of 6.835% from the date of issuance through January 31, 2003. After January 31, 2003, the interest rate to maturity on the MOPPRS will be 5.715% plus the applicable spread determined as of January 31, 2003. In connection with the initial issuance of the MOPPRS, a counter party was granted a remarketing option to purchase the MOPPRS from the holders thereof on January 31, 2003 at 100.0% of the principal amount. If the counter party elects not to exercise this option, the Operating Partnership would be required to repurchase the MOPPRS from the holders on January 31, 2003 at 100.0% of the principal amount plus accrued and unpaid interest.

(2) On June 24, 1997, a trust formed by the Operating Partnership sold \$100.0 million of Exercisable Put Option Securities due June 15, 2004 ("X-POS"), which represent fractional undivided beneficial interests in the trust. The assets of the trust consist

of, among other things, \$100.0 million of Exercisable Put Option Notes due June 15, 2011 (the "Put Option Notes"), issued by the Operating Partnership. The Put Option Notes bear an interest rate of 7.19% from the date of issuance through June 15, 2004. After June 15, 2004, the interest rate to maturity on the Put Option Notes will be 6.39% plus the applicable spread determined as of June 15, 2004. In connection with the initial issuance of the Put Option Notes, a counter party was granted an option to purchase the Put Option Notes from the trust on June 15, 2004 at 100.0% of the principal amount. If the counter party elects not to exercise this option, the Operating Partnership would be required to repurchase the Put Option Notes from the Trust on June 15, 2004 at 100.0% of the principal amount plus accrued and unpaid interest.

The mortgage and loans payable and the secured revolving loan were secured by real estate assets with an aggregate carrying value of \$907.3 million at September 30, 2002.

The Operating Partnership's unsecured notes of \$931.5 million bear interest rates ranging from 6.8% to 8.1%, with interest payable semi-annually in arrears. The premium and discount related to the issuance of the unsecured notes is being amortized over the life of the respective notes as an adjustment to interest expense. All of the unsecured notes, except for the MOPPRS and Put Option Notes, are redeemable at any time prior to maturity at our option, subject to certain conditions including the payment of make-whole amounts.

We currently have a \$300.0 million unsecured revolving loan (with \$151.5 million outstanding at September 30, 2002) that matures in December 2003 and a \$55.2 million secured revolving loan (with \$1.1 million outstanding at September 30, 2002) that matures in March 2003. Our unsecured revolving loan also includes a \$150.0 million competitive sub-facility. Depending upon the corporate credit ratings assigned to us from time to time by the various rating agencies, our unsecured revolving loan bears variable rate interest at a spread above LIBOR ranging from 0.70% to 1.55% and our secured revolving loan bears variable rate interest at a spread above LIBOR ranging from 0.55% to 1.50%. We currently have a credit rating of BBB- assigned by Standard & Poor's, a credit rating of BBB- assigned by Fitch Inc. and a credit rating of Baa2 assigned by Moody's Investor Service. As a result, interest currently accrues on borrowings under our unsecured revolving loan at an average rate of LIBOR plus 95 basis points and under our secured revolving loan at an average rate of LIBOR plus 85 basis points. In addition, we are currently required to pay an annual facility fee equal to .20% of the total commitment under the unsecured revolving loan.

The terms of each of our revolving loans and indenture that governs our outstanding notes require us to comply with various operating and financial covenants and performance ratios. We are currently in compliance with all such requirements.

**Joint Ventures.** During the past several years, we have formed various joint ventures with unrelated investors. We have retained minority equity interests ranging from 12.5% to 50.0% in these joint ventures. As required by GAAP, we have accounted for our joint venture activity using the equity method of accounting, as we do not control these joint ventures. As a result, the assets and liabilities of our joint ventures are not included on our balance sheet. As of September 30, 2002, our joint ventures have approximately \$593.4 million of outstanding debt. All of the joint venture debt is non-recourse to us except (1) in the case of customary exceptions pertaining to such matters as misuse of funds, environmental conditions and material misrepresentations and (2) with respect to \$2.5 million of construction debt related to the MG-HIW Metrowest II, LLC, which has been guaranteed by us subject to a pro rata indemnity from our joint venture partner. Our partner in SF-HIW Harborview Plaza, LP has the right to put its 80% equity interest in the partnership to us in cash at anytime during the one year period commencing on September 11, 2014. The value of the equity interest will be determined based upon the then fair market value of SF-HIW Harborview Plaza, LP's assets and liabilities.

**Interest Rate Hedging Activities.** To meet in part our long-term liquidity requirements, we borrow funds at a combination of fixed and variable rates. Borrowings under our two revolving loans bear interest at variable rates. Our long-term debt, which consists of long-term financings and the unsecured issuance of debt securities, typically bears interest at fixed rates. In addition, we have assumed fixed rate and variable rate debt in connection with acquiring properties. Our interest rate risk management objective is to limit the impact of interest rate changes on earnings and cash flows and to lower our overall borrowing costs. To achieve these objectives, from time to time we enter into interest rate hedge contracts such as collars, swaps, caps and treasury lock agreements in order to mitigate our interest rate risk with respect to various debt instruments. As of September 30, 2002, we have two \$24.0 million treasury lock agreements related to an anticipated five-year fixed rate financing with two financial counterparties, which effectively lock the five-year treasury rate at 3.72%. We do not hold or issue these derivative contracts for trading or speculative purposes.

The interest rate on all of our variable rate debt is adjusted at one- and three-month intervals, subject to settlements under these contracts. We also enter into treasury lock agreements from time to time in order to limit our exposure to an increase in interest rates with respect to future debt offerings. Net payments made to counterparties under interest rate hedge contracts were \$415,051 during the nine months ended September 30, 2002 and were recorded as additional interest expense.

**Current and Future Cash Needs.** Historically, rental revenue has been the principal source of funds to meet our short-term liquidity requirements, which primarily consist of operating expenses, debt service, stockholder distributions and ordinary course capital expenditures. In addition, construction management, maintenance, leasing and management fees have provided sources of cash flow. We presently have no plans for major capital improvements to the existing properties except for the \$3.2 million renovation of Tampa Bay Park and the \$7.9 million general and non-recurring renovations at Country Club Plaza. In addition, we could incur tenant improvements and lease commissions related to any releasing of space currently leased by WorldCom and US Air (see "Recent Developments") and the redevelopment of the EPA site in Research Commons.

In addition to the requirements discussed above, our short-term (within the next 12 months) liquidity requirements also include the funding of approximately \$15.2 million of our existing development activity and first generation tenant improvements and lease commissions on properties placed in service that are not fully leased. See "Business - Development Activity." We expect to fund our short-term liquidity requirements through a combination of working capital, cash flows from operations and the following:

- . borrowings under our unsecured revolving loan (up to \$149.0 million of availability as of November 8, 2002);
- . borrowings under our secured revolving loan (up to \$55.2 million of availability as of November 8, 2002);
- . the selective disposition of non-core assets;
- . the sale or contribution of some of our wholly-owned properties, development projects and development land to strategic joint ventures to be formed with unrelated investors, which will have the net effect of generating additional capital through such sale or contributions; and
- . the issuance of secured debt (at September 30, 2002, we had \$2.8 billion of unencumbered real estate assets at cost).

Our long-term liquidity needs generally include the funding of existing and future development activity, selective asset acquisitions and the retirement of mortgage debt, amounts outstanding under the two revolving loans and long-term unsecured debt. We remain committed to maintaining a flexible capital structure. Accordingly, we expect to meet our long-term liquidity needs through a combination of (1) the issuance by the Operating Partnership of additional unsecured debt securities, (2) the issuance of additional equity securities by the Company and the Operating Partnership as well as (3) the sources described above with respect to our short-term liquidity. We expect to use such sources to meet our long-term liquidity requirements either through direct payments or repayment of borrowings under the unsecured revolving loan. We do not intend to reserve funds to retire existing secured or unsecured indebtedness upon maturity. Instead, we will seek to refinance such debt at maturity or retire such debt through the issuance of equity or debt securities.

We anticipate that our available cash and cash equivalents and cash flows from operating activities, with cash available from borrowings and other sources, will be adequate to meet our capital and liquidity needs in both the short and long term. However, if these sources of funds are insufficient or unavailable, the Company's ability to make the expected distributions to stockholders discussed below and satisfy other cash payments may be adversely affected.

**Distributions to Stockholders.** To maintain its qualification as a REIT, the Company must distribute to stockholders at least 90.0% of REIT taxable income. The Company expects to use its cash flow from operating activities for distributions to stockholders and for payment of recurring, non-incremental revenue-generating

expenditures. The following factors will affect cash flows from operating activities and, accordingly, influence the decisions of the board of directors regarding distributions: (1) debt service requirements after taking into account the repayment and restructuring of certain indebtedness; (2) scheduled increases in base rents of existing leases; (3) changes in rents attributable to the renewal of existing leases or replacement leases; (4) changes in occupancy rates at existing properties and procurement of leases for newly acquired or developed properties; and (5) operating expenses and capital replacement needs.

**Share and Unit Repurchase Program.** On April 25, 2001, we announced that the Company's Board of Directors authorized the repurchase of up to an additional 5.0 million shares of Common Stock and Common Units. As of October 29, 2002, under the new repurchase program, the Company had repurchased 1.4 million shares of Common Stock and Common Units at a weighted average purchase price of \$24.59 per share and a total purchase price of \$34.6 million. In determining whether or not to repurchase additional capital stock, we will consider, among other factors, the effect of repurchases on our liquidity and the price of our Common Stock.

**Disposition and Joint Venture Activity.** As part of our ongoing capital recycling program, during the nine months ended September 30, 2002, we sold 856,000 rentable square feet of office properties and 101.7 acres of development land for gross proceeds of \$164.4 million. At September 30, 2002, we had 1,610,575 square feet of office properties and 112.8 acres of land under letter of intent or contract for sale in various transactions with a carrying value of \$140.0 million. These transactions are subject to customary closing conditions, including due diligence and documentation, and are expected to close during the fourth quarter of 2002. However, we can provide no assurance that all or parts of these transactions will be consummated. During the third quarter, we recorded a \$3.8 million impairment reserve related to two properties and two land parcels that we expect to sell.

On June 26, 2002, we acquired our joint venture partner's interest in MG-HIW Rocky Point, LLC, which owned Harborview Plaza, to bring our ownership interest in that entity to 100.0%. At that time, we consolidated the assets and liabilities, and recorded income and expenses on a consolidated basis.

On September 11, 2002, we contributed Harborview Plaza to SF-HIW Harborview Plaza, LP, a newly formed limited partnership, in exchange for a 20.0% limited partnership interest.

## **RECENT DEVELOPMENTS**

**WorldCom Bankruptcy.** On July 21, 2002, WorldCom filed a voluntary petition with the United States Bankruptcy Court seeking relief under Chapter 11 of the United States Bankruptcy Code. We currently have 13 leases encompassing 982,921 square feet in eight locations with WorldCom and its affiliates, including four leases encompassing 828,467 square feet in four locations with Intermedia Communications, with an average remaining lease term of 7.8 years. Based on September 2002 rental revenue, our annualized rental revenue from these leases is \$17.4 million, or approximately 3.7% of our total annualized rental revenue. Approximately 185,000 square feet of the space leased by Intermedia has not yet been upfitted or occupied and we estimate that a substantial portion of the remaining Intermedia space currently appears to be significantly under-utilized. During the third quarter of 2002, WorldCom rejected one lease encompassing 3,601 square feet that was due to expire in July 2003. As a result of this rejection, we will file a proof of claim totaling approximately \$65,000, which represents the total amount of future rental payments remaining on the lease term.

In addition, our joint venture with Miller Global ("MG-HIW, LLC") has 11 leases encompassing 38,624 square feet in four locations with WorldCom and its affiliates, including three leases encompassing 4,703 square feet in two locations with Intermedia Communications, with lease expirations ranging from 2002 to 2007. We have a 20.0% ownership in this joint venture and, based on September 2002 rental revenue, our proportionate share of the annualized rental revenue generated from these leases is \$197,165.

Approximately 81.5% of the annualized rental revenue related to our leases with WorldCom and its affiliates, including our pro rata share of the annualized rental revenue related to MG-HIW, LLC, is derived from properties in Tampa. The remainder of this revenue is derived from properties in Greenville, South Carolina, Richmond, Raleigh, Orlando and Nashville. WorldCom and its affiliates are current on base rental payments through November 30, 2002. Since June 30, 2002, we have recorded rental revenue from WorldCom and its affiliates on a cash basis, rather than on a straight-line basis.

Due to the inherent uncertainties of the bankruptcy process, we are not able to predict the impact of WorldCom's bankruptcy on its leasing and occupancy of our properties or on our financial condition and results of operations.

**U.S. Airways Bankruptcy.** On August 11, 2002, US Airways Group Inc. filed a voluntary petition with the United States Bankruptcy Court seeking relief under Chapter 11 of the United States Bankruptcy Code. We currently have seven leases encompassing 414,059 square feet with US Airways and its affiliates with an average

remaining lease term of 5.1 years as of September 30, 2002. Based on September 2002 rental revenue, our annualized rental revenue from these leases is \$6.9 million, or approximately 1.5% of our total annualized rental revenue. Approximately 55,000 square feet of space is currently being sub-leased by US Airways to a third party and we estimate that the balance of the space is approximately 75 percent utilized by US Airways as a reservation call center and for certain revenue accounting and information technology functions. All of the 414,059 square feet of space is located in Winston-Salem, North Carolina.

US Airways is current on base rental payments through November 30, 2002, except for pre-petition rent in the amount of \$185,428 from August 1, 2002 up to the date of the US Airways bankruptcy filing, which was August 11, 2002. We have an accrued straight line rent receivable from US Airways in the amount of \$500,508 as of September 30, 2002.

Due to the inherent uncertainties of the bankruptcy process, we are not able to predict the impact of US Airways' bankruptcy on its leasing and occupancy of our properties or on our financial condition and results of operations.

## **IMPACT OF RECENTLY ISSUED ACCOUNTING STANDARDS**

In October 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment of Disposal of Long-Lived Assets," which addresses financial accounting and reporting for the impairment of disposal of long-lived assets. This standard harmonizes the accounting for impaired assets and resolves some of the implementation issues as originally described in SFAS No. 121. We adopted SFAS No. 144 in the first quarter of 2002. Income from discontinued operations, net of minority interest and the gain/(loss) on sale of discontinued operations, net of minority interest, for properties meeting the criteria in accordance with SFAS No. 144 are reflected in the consolidated statements of income as discontinued operations for all periods presented.

In April, 2002, the FASB issued SFAS No. 145, "Rescission of FASB Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13 and Technical Corrections", which rescinds Statement No. 4, which required all gains and losses from extinguishment of debt to be aggregated, and if material, classified as an extraordinary item, net of related income tax effect. The provisions of SFAS No. 145 related to the rescission of Statement No. 4 are effective for financial statements issued for fiscal years after May 15, 2002. We will adopt SFAS No. 145 in the fourth quarter of 2002. We do not anticipate that the adoption of this statement will have a material effect on our results of operations.

## **FUNDS FROM OPERATIONS AND CASH AVAILABLE FOR DISTRIBUTIONS**

We consider funds from operations ("FFO") to be a useful financial performance measure of the operating performance of an equity REIT because, together with net income and cash flows, FFO provides investors with an additional basis to evaluate the ability of a REIT to incur and service debt and to fund acquisitions and other capital expenditures. FFO does not represent net income or cash flows from operating, investing or financing activities as defined by GAAP. It should not be considered as an alternative to net income as an indicator of our operating performance or to cash flows as a measure of liquidity. FFO does not measure whether cash flow is sufficient to fund all cash needs, including principal amortization, capital improvements and distributions to stockholders. Further, FFO as disclosed by other REITs may not be comparable to our calculation of FFO, as described below. FFO and cash available for distributions should not be considered as alternatives to net income as an indication of our performance or to cash flows as a measure of liquidity.

FFO equals income from continuing operations before minority interest (computed in accordance with GAAP) excluding gains (or losses) from debt restructuring and sales of depreciable property and dividends paid to preferred shareholders, plus depreciation and amortization. In addition, FFO includes both recurring and non-recurring operating results and income/(loss) from discontinued operations. As a result, non-recurring items that are not defined as "extraordinary" under GAAP are reflected in the calculation of FFO.

Cash available for distribution is defined as funds from operations increased by the amortization of deferred financing activities and reduced by rental income from straight-line rents and non-revenue enhancing capital expenditures for building improvements and tenant improvements and lease commissions related to second generation space.

FFO and cash available for distribution for the three and nine month periods ended September 30, 2002 and 2001 are summarized in the following table (in thousands):

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	2002	2001	2002	2001
<b>FUNDS FROM OPERATIONS:</b>				
Income before gain on disposition of land and depreciable assets, minority interest, discontinued operations and extraordinary item.....	\$ 14,468	\$ 32,722	\$ 62,231	\$ 98,787
Add/(Deduct):				
Dividends to preferred shareholders.....	(7,713)	(7,713)	(23,139)	(23,787)
Prepayment penalties - unconsolidated sub.....	325	--	325	--
Transition adjustment upon adoption of FAS 133.....	--	--	--	556
Income from discontinued operations.....	1,970	2,730	6,715	9,326
(Loss)/gain on disposition of land.....	741	(538)	6,498	1,025
Depreciation and amortization.....	32,827	29,503	95,761	87,826
Depreciation on unconsolidated affiliates.....	2,432	1,911	7,065	5,815
Funds from operations.....	45,050	58,615	155,456	179,548
<b>CASH AVAILABLE FOR DISTRIBUTION:</b>				
Add/(Deduct):				
Rental income from straight-line rents.....	(1,222)	(2,701)	(2,540)	(8,947)
Non-recurring compensation expense.....	3,700	--	3,700	--
Non-recurring litigation reserve.....	2,700	--	2,700	--
Amortization of deferred financing costs.....	347	324	1,027	1,664
Non-incremental revenue generating capital expenditures (1):				
Building improvements paid.....	(1,740)	(2,872)	(4,861)	(5,959)
Second generation tenant improvements paid.....	(5,824)	(4,834)	(12,735)	(12,610)
Second generation lease commissions paid.....	(3,694)	(2,867)	(9,353)	(11,195)
Cash available for distribution.....	\$ 39,317	\$ 45,665	\$133,394	\$ 142,501
Weighted average shares/units outstanding - basic (2)....	60,436	61,363	60,357	62,333
Weighted average shares/units outstanding - diluted (2)...	60,653	61,783	60,730	62,727
<b>DIVIDEND PAYOUT RATIOS:</b>				
Funds from operations.....	78.8%	61.7%	68.6%	60.3%
Cash available for distribution.....	90.2%	79.1%	79.9%	75.9%

(1) Amounts represent cash expenditures.

(2) Assumes redemption of Common Units for shares of Common Stock. Minority interest Common Unit holders and the stockholders of the Company share equally on a per Common Unit and per share basis; therefore, the per share information is unaffected by conversion.

## PROPERTY INFORMATION

The following table sets forth certain information with respect to our wholly owned in-service and development properties (excluding apartment units) as of September 30, 2002 and 2001:

	SEPTEMBER 30, 2002		SEPTEMBER 30, 2001	
	RENTABLE SQUARE FEET	PERCENT LEASED/ PRE-LEASED	RENTABLE SQUARE FEET	PERCENT LEASED/ PRE-LEASED
IN-SERVICE:				
Office	25,861,000	86.3%	24,829,000	92.9%
Industrial	10,468,000	86.2%	10,396,000	92.3%
Retail (1)	1,650,000	95.4%	1,628,000	95.1%
Total or Weighted Average	37,979,000	86.7%	36,853,000	92.7%
	=====	=====	=====	=====
DEVELOPMENT:				
Completed--Not Stabilized				
Office	568,000	17.3%	1,188,000	62.1%
Industrial	136,000	29.0%	184,000	37.2%
Retail	20,000	90.0%	--	--
Total or Weighted Average	724,000	21.5%	1,372,000	58.8%
	=====	=====	=====	=====
In Process				
Office (2)	100,000	42.0%	1,285,000	52.5%
Industrial (2)	60,000	20.0%	258,000	47.3%
Retail	--	--	20,000	90.0%
Total or Weighted Average	160,000	33.8%	1,563,000	52.1%
	=====	=====	=====	=====
TOTAL:				
Office	26,529,000		27,302,000	
Industrial	10,664,000		10,838,000	
Retail (1)	1,670,000		1,648,000	
Total or Weighted Average	38,863,000		39,788,000	
	=====		=====	
SAME STORE:				
Office	23,408,000	87.7%	21,076,000	92.7%
Industrial	10,041,000	86.3%	9,694,000	91.7%
Retail (1)	1,650,000	95.4%	1,450,000	95.0%
Total or Weighted Average	35,099,000	87.2%	32,220,000	92.5%
	=====	=====	=====	=====

(1) Excludes Kansas City's basement space.

(2) Includes projects that we have an option to purchase.



The following table sets forth information concerning the 20 largest customers of our wholly-owned properties as of September 30, 2002 (\$ in thousands):

TENANT	NUMBER OF LEASES	RENTAL SQUARE FEET	ANNUALIZED RENTAL REVENUE(1)	PERCENT OF TOTAL ANNUALIZED RENTAL REVENUE(1)	AVERAGE REMAINING LEASE TERM IN YEARS
-----	-----	-----	-----	-----	-----
Intermedia Communications/ WorldCom (2).....	13	982,921	\$ 17,396	3.70%	7.8
AT&T.....	10	854,992	14,046	2.99	5.4
Federal Government.....	59	688,320	13,664	2.91	5.0
Capital One Services.....	6	587,188	10,208	2.17	5.9
Caterpillar Financial Services.....	1	300,901	7,899	1.68	12.4
PricewaterhouseCoopers.....	7	307,158	7,038	1.50	7.4
US Air.....	7	414,059	6,909	1.47	5.1
State of Georgia.....	10	356,993	6,783	1.44	6.3
Sara Lee.....	9	1,198,534	4,523	0.96	2.7
Bell South.....	11	212,011	4,396	0.93	1.6
IBM.....	5	203,802	4,260	0.91	3.0
Northern Telecom, Inc.....	1	246,000	3,235	0.69	5.4
Lockton Companies, Inc.....	1	127,485	3,117	0.66	12.4
Bank of America.....	23	152,017	2,998	0.64	2.6
Volvo.....	5	214,783	2,979	0.63	6.8
International Paper Co.....	10	121,174	2,887	0.61	0.3
Hartford Insurance.....	6	134,021	2,886	0.61	3.5
Business Telecom, Inc.....	4	145,497	2,832	0.60	2.5
T-Mobile USA, Inc.....	3	120,561	2,808	0.60	3.7
Ford Motor Company.....	2	129,158	2,661	0.57	7.2
---	---	---	---	---	---
Total.....	193	7,497,575	\$123,525	26.27%	5.9
===	===	=====	=====	=====	=====

(1) Annualized Rental Revenue is September 2002 rental revenue (base rent plus operating expense pass throughs) multiplied by 12.

(2) Since June 30, 2002, we have recorded rental revenue from WorldCom and its affiliates on a cash basis, rather than on a straight-line basis.

As of September 30, 2002, we were developing six suburban office properties, two industrial properties and one retail property totaling 884,000 rentable square feet of office and industrial space. The following table summarizes these development projects. In addition to the properties described in this table, we are developing with a joint venture partner one additional property totaling 285,000 rentable square feet. At September 30, 2002, this one development project had an aggregate anticipated total investment of \$69.0 million and was 59.0% pre-leased.

## IN-PROCESS

PROPERTY -----	MARKET -----	ANTICIPATED		INVESTMENT AT 09/30/02 -----	PRE-LEASING PERCENTAGE(1) -----	ESTIMATED COMPLETION -----	ESTIMATED STABILIZATION(2) -----
		RENTABLE SQUARE FEET -----	TOTAL INVESTMENT -----				
(\$ in thousands)							
OFFICE: 801 Raleigh Corporate Center	Research Triangle	100,000	\$ 12,016	\$ 9,050	42%	4Q02	2Q04
		-----	-----	-----	----		
In-Process Office Total or Weighted Average		100,000	\$ 12,016	\$ 9,050	42%		
		=====	=====	=====	=====		
INDUSTRIAL: Tradeport V (3)	Atlanta	60,000	\$ 2,913	\$ 1,420	20%	4Q02	4Q03
		-----	-----	-----	----		
In-Process Industrial Total or Weighted Average		60,000	\$ 2,913	\$ 1,420	20%		
		=====	=====	=====	=====		
Total or Weighted Average of all In-Process Development Projects		160,000	\$ 14,929	\$10,470	34%		
		=====	=====	=====	=====		

(1) Letters of intent comprise 4.5% of the total pre-leasing percentage.

(2) We generally consider a development project to be stabilized upon the earlier of the first date such project is at least 95% occupied or one year from the date of completion.

(3) We are developing this property for a third party and own an option to purchase.

**COMPLETED--NOT STABILIZED (3)**

PROPERTY -----	MARKET -----	ANTICIPATED		INVESTMENT AT 09/30/02 -----	PRE-LEASING PERCENTAGE(1) -----	ESTIMATED COMPLETION -----	ESTIMATED STABILIZATION(2) -----
		RENTABLE SQUARE FEET -----	TOTAL INVESTMENT -----				
(\$ in thousands)							
OFFICE:							
Seven Springs I	Nashville	131,000	\$ 15,556	\$ 13,048	12%	1Q02	1Q03
1501 Highwoods Boulevard	Piedmont Triad	98,000	11,290	10,156	4	4Q01	1Q03
Centre Green Four	Research Triangle	100,000	11,764	9,613	0	4Q01	2Q03
GlenLake I	Research Triangle	158,000	22,417	19,457	40	4Q01	2Q03
Shadow Creek II	Memphis	81,000	8,750	7,110	19	4Q01	4Q03
		-----	-----	-----	----		
Completed-Not Stabilized Office Total or Weighted Average		568,000 =====	\$ 69,777 =====	\$ 59,384 =====	17% =====		
Industrial:							
Newpoint IV	Atlanta	136,000	\$ 5,288	\$ 4,875	29%	4Q01	1Q03
		-----	-----	-----	----		
Completed-Not Stabilized Industrial Total or Weighted Average		136,000 =====	\$ 5,288 =====	\$ 4,875 =====	29% =====		
Retail:							
Granada Shops	Kansas City	20,000	\$ 5,020	\$ 4,120	90%	4Q01	2Q03
		-----	-----	-----	----		
Completed-Not Stabilized Retail Total or Weighted Average		20,000 =====	\$ 5,020 =====	\$ 4,120 =====	90% =====		
Total or Weighted Average of all Completed- Not Stabilized Development Projects		724,000 =====	\$ 80,085 =====	\$ 68,379 =====	22% =====		
Total or Weighted Average of all Development Projects		884,000 =====	\$ 95,014 =====	\$ 78,849 =====	24% =====		

(1) Letters of intent comprise 4.5% of the total pre-leasing percentage.

(2) We generally consider a development project to be stabilized upon the earlier of the first date such project is at least 95% occupied or one year from the date of completion.

(3) These properties contributed an aggregate of \$61,000 in Net Operating Income (Property Revenue - Property Expense) in the third quarter of 2002.

## DEVELOPMENT ANALYSIS

	RENTABLE SQUARE FEET -----	ANTICIPATED TOTAL INVESTMENT -----	PRE-LEASING PERCENTAGE (1) -----
	(\$ in thousands)		
Summary by Estimated Stabilization Date:			
First Quarter 2003.....	365,000	\$ 32,134	15%
Second Quarter 2003.....	278,000	39,201	29%
Fourth Quarter 2003.....	141,000	11,663	19%
Second Quarter 2004.....	100,000	12,016	42%
	-----	-----	---
Total or Weighted Average.....	884,000	\$ 95,014	24%
	=====	=====	===
Summary by Market:			
Atlanta.....	196,000	\$ 8,201	26%
Kansas City.....	20,000	5,020	90%
Memphis.....	81,000	8,750	19%
Nashville.....	131,000	15,556	12%
Piedmont Triad.....	98,000	11,290	4%
Research Triangle.....	358,000	46,197	29%
	-----	-----	---
Total or Weighted Average.....	884,000	\$ 95,014	24%
	=====	=====	===
Build-to-Suit.....	--	\$ --	--%
Multi-Tenant.....	884,000	95,014	24%
	-----	-----	---
Total or Weighted Average.....	884,000	\$ 95,014	24%
	=====	=====	===
	AVERAGE RENTABLE SQUARE FEET -----	AVERAGE ANTICIPATED TOTAL INVESTMENT -----	AVERAGE PRE-LEASING (1) -----
	(\$ in thousands)		
Average Per Property By Type:			
Office.....	111,333	\$ 13,632	21%
Industrial.....	98,000	4,101	26%
Retail.....	20,000	5,020	90%
	-----	-----	---
Weighted Average.....	98,222	\$ 10,557	24%
	=====	=====	===

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(1) Letters of intent comprise 4.5% of the total pre-leasing percentage.

The following table sets forth certain information about leasing activities at our wholly owned in-service properties (excluding apartment units) for the three months ended September 30, June 30 and March 31, 2002 and December 31, 2001.

	OFFICE LEASING STATISTICS THREE MONTHS ENDED				
	9/30/02	6/30/02	3/31/02	12/31/01	AVERAGE
NET EFFECTIVE RENTS RELATED TO RE-LEASED SPACE:					
Number of lease transactions (signed leases)...	184	162	110	116	143
Rentable square footage leased.....	882,115	874,467	417,102	437,454	652,785
Average per rentable square foot over the lease term:					
Base rent.....	\$ 17.26	\$ 16.86	\$ 16.83	\$ 17.85	\$ 17.20
Tenant improvements.....	(1.06)	(0.86)	(0.98)	(1.19)	(1.02)
Leasing commissions.....	(0.60)	(0.56)	(0.78)	(0.97)	(0.73)
Rent concessions.....	(0.22)	(0.14)	(0.15)	(0.11)	(0.16)
Effective rent.....	\$ 15.38	\$ 15.30	\$ 14.92	\$ 15.58	\$ 15.29
Expense stop(1).....	(5.54)	(5.17)	(5.17)	(4.50)	(5.10)
Equivalent effective net rent.....	\$ 9.84	\$ 10.13	\$ 9.75	\$ 11.08	\$ 10.20
Average term in years.....	3.6	4.1	4.1	4.6	4.1
CAPITAL EXPENDITURES RELATED TO RE-LEASED SPACE:					
Tenant Improvements:					
Total dollars committed under signed leases.....	\$ 4,396,259	\$ 3,481,988	\$ 2,031,231	\$ 2,647,115	\$ 3,139,148
Rentable square feet.....	882,115	874,467	417,102	437,454	652,785
Per rentable square foot.....	\$ 4.98	\$ 3.98	\$ 4.87	\$ 6.05	\$ 4.81
Leasing Commissions:					
Total dollars committed under signed leases.....	\$ 1,352,691	\$ 1,272,854	\$ 984,220	\$ 1,277,523	\$ 1,221,822
Rentable square feet.....	882,115	874,467	417,102	437,454	652,785
Per rentable square foot.....	\$ 1.53	\$ 1.46	\$ 2.36	\$ 2.92	\$ 1.87
Total:					
Total dollars committed under signed leases.....	\$ 5,748,950	\$ 4,754,842	\$ 3,015,450	\$ 3,924,637	\$ 4,360,970
Rentable square feet.....	882,115	874,467	417,102	437,454	652,785
Per rentable square foot.....	\$ 6.52	\$ 5.44	\$ 7.23	\$ 8.97	\$ 6.68

(1) "Expense stop" represents operating expenses (generally including taxes, utilities, routine building expense and common area maintenance) for which we will not be reimbursed by our tenants.

INDUSTRIAL LEASING STATISTICS THREE MONTHS ENDED					
	9/30/02	6/30/02	3/31/02	12/31/01	Average
NET EFFECTIVE RENTS RELATED TO RE-LEASED SPACE:					
Number of lease transactions (signed leases)...	45	32	15	31	31
Rentable square footage leased.....	593,188	1,005,765	78,844	894,865	643,166
Average per rentable square foot over the lease term:					
Base rent.....	\$ 4.37	\$ 3.58	\$ 6.95	\$ 3.52	\$ 4.61
Tenant improvements.....	(0.23)	(0.29)	(1.10)	(0.24)	(0.47)
Leasing commissions.....	(0.14)	(0.14)	(0.21)	(0.10)	(0.15)
Rent concessions.....	(0.02)	(0.03)	--	--	(0.01)
Effective rent.....	\$ 3.98	\$ 3.12	\$ 5.64	\$ 3.18	\$ 3.98
Expense stop (1).....	(0.39)	(0.09)	(0.72)	(0.18)	(0.35)
Equivalent effective net rent.....	\$ 3.59	\$ 3.03	\$ 4.92	\$ 3.00	\$ 3.63
Average term in years.....	1.6	6.3	4.1	2.2	3.6
CAPITAL EXPENDITURES RELATED TO RE-LEASED SPACE:					
Tenant Improvements:					
Total dollars committed under signed leases .....	\$ 522,115	\$ 2,088,547	\$ 386,263	\$ 661,591	\$ 914,629
Rentable square feet.....	593,188	1,005,765	78,844	894,865	643,166
Per rentable square foot.....	\$ 0.88	\$ 2.08	\$ 4.90	\$ 0.74	\$ 1.42
Leasing Commissions:					
Total dollars committed under signed leases .....	\$ 141,694	\$ 797,939	\$ 44,100	\$ 257,010	\$ 310,186
Rentable square feet.....	593,188	1,005,765	78,844	894,865	643,166
Per rentable square foot.....	\$ 0.24	\$ 0.79	\$ 0.56	\$ 0.29	\$ 0.48
Total:					
Total dollars committed under signed leases .....	\$ 663,809	\$ 2,886,486	\$ 430,363	\$ 918,601	\$ 1,224,815
Rentable square feet.....	593,188	1,005,765	78,844	894,865	643,166
Per rentable square foot.....	\$ 1.12	\$ 2.87	\$ 5.46	\$ 1.03	\$ 1.90

(1) "Expense stop" represents operating expenses (generally including taxes, utilities, routine building expense and common area maintenance) for which we will not be reimbursed by our tenants.

RETAIL LEASING STATISTICS THREE MONTHS ENDED					
	9/30/02	6/30/02	3/31/02	12/31/01	AVERAGE
Net Effective Rents Related to Re-Leased Space:					
Number of lease transactions (signed leases)...	13	13	12	12	13
Rentable square footage leased.....	28,267	52,527	59,649	26,019	41,616
Average per rentable square foot over the lease term:					
Base rent.....	\$ 20.14	\$ 18.15	\$ 25.66	\$ 15.75	\$ 19.93
Tenant improvements.....	(0.60)	(1.83)	(1.87)	(0.63)	(1.23)
Leasing commissions.....	(0.88)	(0.65)	(0.35)	(0.82)	(0.68)
Rent concessions.....	--	(0.03)	(0.02)	--	(0.01)
Effective rent.....	\$ 18.66	\$ 15.64	\$ 23.42	\$ 14.30	\$ 18.01
Expense stop (1).....	--	(1.02)	--	--	(0.26)
Equivalent effective net rent.....	\$ 18.66	\$ 14.62	\$ 23.42	\$ 14.30	\$ 17.75
Average term in years.....	5.6	7.0	6.5	6.7	6.4
Capital Expenditures Related to Re-leased Space:					
Tenant Improvements:					
Total dollars committed under signed leases .....	\$ 121,500	\$ 1,077,825	\$ 738,605	\$ 148,860	\$ 521,698
Rentable square feet.....	28,267	52,527	59,649	26,019	41,616
Per rentable square foot.....	\$ 4.30	\$ 20.52	\$ 12.38	\$ 5.72	\$ 12.54
Leasing Commissions:					
Total dollars committed under signed leases .....	\$ 91,405	\$ 151,268	\$ 61,981	\$ 73,314	\$ 94,492
Rentable square feet.....	28,267	52,527	59,649	26,019	41,616
Per rentable square foot.....	\$ 3.23	\$ 2.88	\$ 1.04	\$ 2.82	\$ 2.27
Total:					
Total dollars committed under signed leases .....	\$ 212,905	\$ 1,229,093	\$ 800,586	\$ 222,174	\$ 616,189
Rentable square feet.....	28,267	52,527	59,649	26,019	41,616
Per rentable square foot.....	\$ 7.53	\$ 23.40	\$ 13.42	\$ 8.54	\$ 14.81

(1) "Expense stop" represents operating expenses (generally including taxes, utilities, routine building expense and common area maintenance) for which we will not be reimbursed by our tenants.

The following tables set forth scheduled lease expirations at our wholly owned in-service properties (excluding apartment units) as of September 30, 2002, assuming no tenant exercises renewal options.

#### OFFICE PROPERTIES:

LEASE EXPIRING	NUMBER OF LEASES EXPIRING	RENTABLE SQUARE FEET SUBJECT TO EXPIRING LEASES	PERCENTAGE OF LEASED SQUARE FOOTAGE REPRESENTED BY EXPIRING LEASES	ANNUAL RENTS UNDER EXPIRING LEASES (1)	AVERAGE ANNUAL RENTAL RATE PER SQUARE FOOT FOR EXPIRATIONS	PERCENTAGE OF LEASED RENTS REPRESENTED BY EXPIRING LEASES
-----	-----	-----	-----	-----	-----	-----
				(\$ in thousands)		
2002 (2)	319	1,173,528	5.2%	\$ 20,902	\$17.81	5.4%
2003	569	3,385,788	15.1%	58,098	17.16	14.8%
2004	502	2,896,061	12.9%	52,267	18.05	13.4%
2005	502	3,285,499	14.8%	56,914	17.32	14.6%
2006	308	2,793,578	12.5%	50,559	18.10	13.0%
2007	191	1,825,640	8.2%	29,390	16.10	7.5%
2008	94	1,919,826	8.6%	30,470	15.87	7.8%
2009	30	768,022	3.4%	13,288	17.30	3.4%
2010	41	1,418,672	6.3%	26,152	18.43	6.7%
2011	38	1,155,693	5.2%	22,322	19.31	5.7%
Thereafter	126	1,751,987	7.8%	29,993	17.12	7.7%
	-----	-----	-----	-----	-----	-----
	2,720	22,374,294	100.0%	\$390,355	\$17.45	100.0%
	=====	=====	=====	=====	=====	=====

#### INDUSTRIAL PROPERTIES:

LEASE EXPIRING	NUMBER OF LEASES EXPIRING	RENTABLE SQUARE FEET SUBJECT TO EXPIRING LEASES	PERCENTAGE OF LEASED SQUARE FOOTAGE REPRESENTED BY EXPIRING LEASES	ANNUAL RENTS UNDER EXPIRING LEASES (1)	AVERAGE ANNUAL RENTAL RATE PER SQUARE FOOT FOR EXPIRATIONS	PERCENTAGE OF LEASED RENTS REPRESENTED BY EXPIRING LEASES
-----	-----	-----	-----	-----	-----	-----
				(\$ in thousands)		
2002 (3)	70	955,002	10.5%	\$ 4,047	\$ 4.24	9.8%
2003	95	1,135,693	12.5%	5,922	5.21	14.3%
2004	97	2,522,192	27.8%	9,687	3.84	23.5%
2005	66	1,109,012	12.2%	5,622	5.07	13.6%
2006	35	744,758	8.2%	4,160	5.59	10.1%
2007	27	1,311,658	14.4%	5,542	4.23	13.4%
2008	7	214,340	2.4%	1,441	6.72	3.5%
2009	8	318,813	3.5%	2,361	7.41	5.7%
2010	3	46,508	0.5%	348	7.48	0.8%
2011	2	35,475	0.4%	178	5.02	0.4%
Thereafter	20	691,120	7.6%	2,031	2.94	4.9%
	-----	-----	-----	-----	-----	-----
	430	9,084,571	100.0%	\$ 41,339	\$ 4.55	100.0%
	=====	=====	=====	=====	=====	=====

(1) Annual Rents Under Expiring Leases are September 2002 rental revenue (base rent plus operating expense pass-throughs) multiplied by 12.

(2) Includes 137,000 square feet of leases that are a month-to-month basis, or 0.5% of total annualized revenue. (3) Includes 160,000 square feet of leases that are a month-to-month basis, or 0.2% of total annualized revenue.



## RETAIL PROPERTIES:

LEASE EXPIRING	NUMBER OF LEASES EXPIRING	RENTABLE SQUARE FEET SUBJECT TO EXPIRING LEASES	PERCENTAGE OF LEASED SQUARE FOOTAGE REPRESENTED BY EXPIRING LEASES	ANNUAL RENTS UNDER EXPIRING LEASES (1)	AVERAGE ANNUAL RENTAL RATE PER SQUARE FOOT FOR EXPIRATIONS	PERCENTAGE OF LEASED RENTS REPRESENTED BY EXPIRING LEASES
-----	-----	-----	-----	-----	-----	-----
				(\$ in thousands)		
2002 (2)	26	79,423	5.0%	\$ 1,427	\$17.97	3.7%
2003	35	87,076	5.5%	2,094	24.05	5.4%
2004	42	211,027	13.4%	2,824	13.38	7.3%
2005	40	93,849	5.9%	2,748	29.28	7.1%
2006	38	111,064	7.0%	2,784	25.07	7.2%
2007	35	128,631	8.1%	2,451	19.05	6.3%
2008	25	124,318	7.8%	4,309	34.66	11.2%
2009	21	168,355	10.6%	3,304	19.63	8.6%
2010	18	97,372	6.1%	2,872	29.50	7.4%
2011	19	108,418	6.8%	2,584	23.83	6.7%
Thereafter	28	378,565	23.8%	11,241	29.69	29.1%
	----	-----	-----	-----	-----	-----
	327	1,588,098	100.0%	\$ 38,638	\$24.33	100.0%
	=====	=====	=====	=====	=====	=====

## TOTAL:

LEASE EXPIRING	NUMBER OF LEASES EXPIRING	RENTABLE SQUARE FEET SUBJECT TO EXPIRING LEASES	PERCENTAGE OF LEASED SQUARE FOOTAGE REPRESENTED BY EXPIRING LEASES	ANNUAL RENTS UNDER EXPIRING LEASES (1)	AVERAGE ANNUAL RENTAL RATE PER SQUARE FOOT FOR EXPIRATIONS	PERCENTAGE OF LEASED RENTS REPRESENTED BY EXPIRING LEASES
-----	-----	-----	-----	-----	-----	-----
				(\$ in thousands)		
2002 (3)	415	2,207,953	6.7%	\$ 26,376	\$11.95	5.6%
2003	699	4,608,557	14.0%	66,114	14.35	14.2%
2004	641	5,629,280	17.1%	64,778	11.51	13.8%
2005	608	4,488,360	13.6%	65,284	14.55	13.9%
2006	381	3,649,400	11.0%	57,503	15.76	12.2%
2007	253	3,265,929	9.9%	37,383	11.45	7.9%
2008	126	2,258,484	6.8%	36,220	16.04	7.7%
2009	59	1,255,190	3.8%	18,953	15.10	4.0%
2010	62	1,562,552	4.7%	29,372	18.80	6.2%
2011	59	1,299,586	3.9%	25,084	19.30	5.3%
Thereafter	174	2,821,672	8.5%	43,265	15.33	9.2%
	----	-----	-----	-----	-----	-----
	3,477	33,046,963	100.0%	\$470,332	\$14.23	100.0%
	=====	=====	=====	=====	=====	=====

(1) Annual Rents Under Expiring Leases are September 2002 rental revenue (base rent plus operating expense pass-throughs) multiplied by 12.

(2) Includes 36,000 square feet of leases that are a month-to-month basis, or 0.1% of total annualized revenue. (3) Includes 333,000 square feet of leases that are a month-to-month basis, or 0.7% of total annualized revenue.

## INFLATION

In the last five years, inflation has not had a significant impact on us because of the relatively low inflation rate in our geographic areas of operation. Most of the leases require the tenants to pay their share of increases in operating expenses, including common area maintenance, real estate taxes and insurance, thereby reducing our exposure to inflation.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The effects of potential changes in interest rates are discussed below. Our market risk discussion includes "forward-looking statements" and represents an estimate of possible changes in fair value or future earnings that would occur assuming hypothetical future movements in interest rates. These disclosures are not precise indicators of expected future losses, but only indicators of reasonably possible losses. As a result, actual future results may differ materially from those presented. See "Management's Discussion and Analysis of Financial Condition and Results of Operations--Liquidity and Capital Resources" for a description of our accounting policies and other information related to these financial instruments.

To meet in part our long-term liquidity requirements, we borrow funds at a combination of fixed and variable rates. Borrowings under our revolving loans bear interest at variable rates. Our long-term debt, which consists of long-term financings and the issuance of debt securities, typically bears interest at fixed rates. In addition, we have assumed fixed rate and variable rate debt in connection with acquiring properties. Our interest rate risk management objective is to limit the impact of interest rate changes on earnings and cash flows and to lower our overall borrowing costs. To achieve these objectives, from time to time we enter into interest rate hedge contracts such as collars, swaps, caps and treasury lock agreements in order to mitigate our interest rate risk with respect to various debt instruments. As of September 30, 2002, we have two \$24.0 million treasury lock agreements related to an anticipated five-year fixed rate financing with two financial counterparties, which effectively lock the five-year treasury rate at 3.72%. If interest rates increase by 100 basis points, the aggregate fair market value of these interest rate hedge contracts as of September 30, 2002 would increase by approximately \$2.3 million. If interest rates decrease by 100 basis points, the aggregate fair market value of these interest rate hedge contracts as of September 30, 2002 would decrease by approximately \$2.4 million. We do not hold or issue these derivative contracts for trading or speculative purposes.

As of September 30, 2002, we had approximately \$177.0 million of variable rate debt outstanding that was not protected by interest rate hedge contracts. If the weighted average interest rate on this variable rate debt is 100 basis points higher or lower during the 12 months ended September 30, 2003, our interest expense would be increased or decreased approximately \$1.8 million. In addition, as of September 30, 2002, our share of the joint venture variable rate debt is \$69.6 million, and is not protected by interest rate hedge contracts. If the weighted average interest rate on this variable rate debt is 100 basis points higher or lower during the 12 months ended September 30, 2003, equity in earnings of unconsolidated affiliates would be increased or decreased by approximately \$697,000.

### **ITEM 4. CONTROLS AND PROCEDURES**

We 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. These disclosure controls and procedures are further designed to ensure that such information is accumulated and communicated to our management, including our chief executive officer and chief financial officer, to allow timely decisions regarding required disclosure.

Based on the most recent evaluation, which was completed at September 30, 2002, our chief executive officer and chief financial officer believe that our disclosure controls and procedures are effective. There have been no significant changes in our internal controls or in other factors that could significantly affect the internal controls subsequent to the date we completed our evaluation.

## PART II--OTHER INFORMATION

### ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

#### (a) Exhibits

Exhibit No. Description

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99.1	Statement of Chief Executive Officer of Highwoods Properties Inc.
99.2	Statement of Chief Financial Officer of Highwoods Properties Inc.

#### (b) Reports on Form 8-K

We filed a Current Report on Form 8-K, dated August 15, 2002, reporting under Item 5 certain matters related to the bankruptcy of US Airways Group, Inc.

## SIGNATURES

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

### HIGHWOODS PROPERTIES, INC.

By:                     /s/ RONALD P. GIBSON                      
                    Ronald P. Gibson  
                    President and Chief Executive Officer

By:                     /s/ CARMAN J. LIUZZO                      
                    Carman J. Liuzzo  
                    Chief Financial Officer  
                    (Principal Accounting Officer)

Date: November 14, 2002

## CERTIFICATION

I, Ronald P. Gibson, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Highwoods Properties Inc.;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
  - (a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - (b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - (c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - (a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

*Date: November 14, 2002*

*/s/ RONALD P. GIBSON*

-----  
*Ronald P. Gibson*  
*President and Chief Executive Officer*

## CERTIFICATION

I, Carman J. Liuzzo, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Highwoods Properties Inc.;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
  - (a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - (b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - (c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - (a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

*Date: November 14, 2002*

*/s/ CARMAN J. LIUZZO*

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*Carman J. Liuzzo*  
*Vice President and Chief Financial Officer*

**Exhibit 99.1**

**Statement of Chief Executive Officer OF  
HIGHWOODS PROPERTIES, INC.**

In connection with the Quarterly Report of Highwoods Properties, Inc. (the "Company") on Form 10-Q for the period ended September 30, 2002 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Ronald P. Gibson, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. ss. 1350, as adopted pursuant to ss. 906 of the Sarbanes-Oxley Act of 2002, that:

- 1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- 2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

*/s/ RONALD P. GIBSON*

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*Ronald P. Gibson  
President and Chief Executive Officer  
November 14, 2002*

**STATEMENT OF CHIEF FINANCIAL OFFICER OF  
HIGHWOODS PROPERTIES, INC.**

In connection with the Quarterly Report of Highwoods Properties, Inc. (the "Company") on Form 10-Q for the period ended September 30, 2002 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Carman J. Liuzzo, Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. ss. 1350, as adopted pursuant to ss. 906 of the Sarbanes-Oxley Act of 2002, that:

- 1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- 2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ CARMAN J. LIUZZO

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Carman J. Liuzzo  
Vice President and Chief Financial Officer  
November 14, 2002

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**End of Filing**

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