HIGHWOODS PROPERTIES INC
Form 10-Q
October 27, 2011

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

FORM 10-Q

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

For the quarterly period ended September 30, 2011

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

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

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

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

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

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

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

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

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

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

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

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

The Company had 72,579,381 shares of Common Stock outstanding as of October 20, 2011.

HIGHWOODS PROPERTIES, INC.
HIGHWOODS REALTY LIMITED PARTNERSHIP

QUARTERLY REPORT FOR THE PERIOD ENDED SEPTEMBER 30, 2011

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

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

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

Certain information contained herein is presented as of October 20, 2011, the latest practicable date prior to the filing of this Quarterly Report.

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HIGHWOODS PROPERTIES, INC.

Consolidated Balance Sheets

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

	September 30, 2011	December 31, 2010
Assets:		
Real estate assets, at cost:		
Land	$ 368,948	$ 345,088
Buildings and tenant improvements	3,115,149	2,883,092
Development in process	7,576	4,524
Land held for development	106,975	107,101
	3,598,648	3,339,805
Less-accumulated depreciation	(878,702)	(830,153)
Net real estate assets	2,719,946	2,509,652
For-sale residential condominiums	4,995	8,225
Real estate and other assets, net, held for sale	—	13,607
Cash and cash equivalents	11,088	14,206
Restricted cash	23,230	4,399
Accounts receivable, net of allowance of $3,581 and $3,595, respectively	23,443	20,716
Mortgages and notes receivable, net of allowance of $545 and $868, respectively	18,706	19,044
Accrued straight-line rents receivable, net of allowance of $1,366 and $2,209, respectively	102,338	93,178
Investment in and advances to unconsolidated affiliates	99,910	63,607
Deferred financing and leasing costs, net of accumulated amortization of $60,950 and $59,360, respectively	129,311	85,001
Prepaid expenses and other assets	38,940	40,200
Total Assets	$ 3,171,907	$ 2,871,835
Liabilities, Noncontrolling Interests in the Operating Partnership and Equity:		
Mortgages and notes payable	$ 1,893,981	$ 1,522,945
Accounts payable, accrued expenses and other liabilities	127,664	106,716
Financing obligations	32,775	33,114
Total Liabilities	2,054,420	1,662,775
Commitments and contingencies		
Noncontrolling interests in the Operating Partnership	105,995	120,838
Equity:		
Preferred Stock, $.01 par value, 50,000,000 authorized shares;		
8.625% Series A Cumulative Redeemable Preferred Shares (liquidation preference $1,000 per share), 29,077 and 29,092 shares issued and outstanding, respectively	29,077	29,092
8.000% Series B Cumulative Redeemable Preferred Shares (liquidation preference $25 per share), 0 and 2,100,000 shares	—	52,500

issued and outstanding, respectively		
Common Stock, $.01 par value, 200,000,000 authorized shares; 72,579,381 and 71,690,487 shares issued and outstanding, respectively	726	717
Additional paid-in capital	1,807,107	1,766,886
Distributions in excess of net income available for common stockholders	(826,435)	(761,785)
Accumulated other comprehensive loss	(3,606)	(3,648)
Total Stockholders' Equity	1,006,869	1,083,762
Noncontrolling interests in consolidated affiliates	4,623	4,460
Total Equity	1,011,492	1,088,222
Total Liabilities, Noncontrolling Interests in the Operating Partnership and Equity	$ 3,171,907	$ 2,871,835

See accompanying notes to consolidated financial statements.

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HIGHWOODS PROPERTIES, INC.

Consolidated Statements of Income

(Unaudited and in thousands, except per share amounts)

	Three Months Ended September 30, 2011	Three Months Ended September 30, 2010	Nine Months Ended September 30, 2011	Nine Months Ended September 30, 2010
Rental and other revenues	$ 122,086	$ 115,528	$ 354,122	$ 343,796
Operating expenses:				
Rental property and other expenses	46,019	43,339	128,360	122,986
Depreciation and amortization	36,320	34,183	103,467	100,081
Impairment of assets held for use	2,429	—	2,429	—
General and administrative	12,212	8,882	27,983	24,369
Total operating expenses	96,980	86,404	262,239	247,436
Interest expense:				
Contractual	23,356	22,020	68,727	65,527
Amortization of deferred financing costs	806	858	2,448	2,528
Financing obligations	228	460	665	1,330
	24,390	23,338	71,840	69,385
Other income:				
Interest and other income	1,505	1,709	5,277	4,374
Loss on debt extinguishment	—	(85)	(24)	(85)
	1,505	1,624	5,253	4,289
Income from continuing operations before disposition of property, condominiums and investment in unconsolidated affiliates and equity in earnings of unconsolidated affiliates	2,221	7,410	25,296	31,264
Gains on disposition of property	262	19	462	55
Gains/(losses) on for-sale residential condominiums	(476)	54	(322)	407
Gains on disposition of investment in unconsolidated affiliates	2,282	—	2,282	25,330
Equity in earnings of unconsolidated affiliates	1,113	1,018	3,933	2,701
Income from continuing operations	5,402	8,501	31,651	59,757
Discontinued operations:				
Income from discontinued operations	269	272	897	1,233
Net gains/(losses) on disposition of discontinued operations	2,573	—	2,573	(86)
	2,842	272	3,470	1,147
Net income	8,244	8,773	35,121	60,904
Net (income) attributable to noncontrolling interests in the Operating Partnership	(366)	(366)	(1,496)	(2,819)
Net (income)/loss attributable to noncontrolling interests in consolidated affiliates	(249)	148	(554)	(281)
Dividends on Preferred Stock	(627)	(1,677)	(3,926)	(5,031)
	—	—	(1,895)	—

Excess of Preferred Stock redemption/repurchase cost over carrying value								
Net income available for common stockholders	$	7,002	$	6,878	$	27,250	$	52,773
Earnings per Common Share – basic:								
Income from continuing operations available for common stockholders	$	0.06	$	0.10	$	0.33	$	0.72
Income from discontinued operations available for common stockholders		0.04		—		0.05		0.02
Net income available for common stockholders	$	0.10	$	0.10	$	0.38	$	0.74
Weighted average Common Shares outstanding – basic		72,492		71,631		72,176		71,549
Earnings per Common Share – diluted:								
Income from continuing operations available for common stockholders	$	0.06	$	0.10	$	0.33	$	0.72
Income from discontinued operations available for common stockholders		0.04		—		0.05		0.02
Net income available for common stockholders	$	0.10	$	0.10	$	0.38	$	0.74
Weighted average Common Shares outstanding – diluted		76,402		75,638		76,127		75,537
Dividends declared per Common Share	$	0.425	$	0.425	$	1.275	$	1.275
Net income available for common stockholders:								
Income from continuing operations available for common stockholders	$	4,301	$	6,620	$	23,953	$	51,684
Income from discontinued operations available for common stockholders		2,701		258		3,297		1,089
Net income available for common stockholders	$	7,002	$	6,878	$	27,250	$	52,773

See accompanying notes to consolidated financial statements.

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HIGHWOODS PROPERTIES, INC.

Consolidated Statements of Equity

Nine Months Ended September 30, 2011 and 2010

(Unaudited and in thousands, except share amounts)

	Number of Common Shares	Common Stock	Series A Cumulative Redeemable Preferred Shares	Series B Cumulative Redeemable Preferred Shares	Additional Paid-In Capital	Accumulated Other Comprehensive Loss	Non-Controlling Interests in Consolidated Affiliates	Distributions in Excess of Net Income Available for Common Stockholders	Total
Balance at December 31, 2010	71,690,487	$ 717	$ 29,092	$ 52,500	$ 1,766,886	$ (3,648)	$ 4,460	$ (761,785)	$ 1,088,222
Issuances of Common Stock, net	711,234	7	—	—	22,036	—	—	—	22,043
Conversion of Common Units to Common Stock	43,308	—	—	—	1,344	—	—	—	1,344
Dividends on Common Stock	—	—	—	—	—	—	—	(91,900)	(91,900)
Dividends on Preferred Stock	—	—	—	—	—	—	—	(3,926)	(3,926)
Adjustment of noncontrolling interests in the Operating Partnership to fair value	—	—	—	—	10,177	—	—	—	10,177
Distributions to noncontrolling interests in consolidated affiliates	—	—	—	—	—	—	(391)	—	(391)
Issuances of restricted stock, net	134,352	—	—	—	—	—	—	—	—
Redemptions/repurchases of Preferred Stock	—	—	(15)	(52,500)	1,895	—	—	(1,895)	(52,515)
Share-based compensation expense	—	2	—	—	4,769	—	—	—	4,771
Net (income) attributable to noncontrolling interests in the Operating Partnership	—	—	—	—	—	—	—	(1,496)	(1,496)
Net (income) attributable to noncontrolling interests in consolidated affiliates	—	—	—	—	—	—	554	(554)	—
Comprehensive income:									

Net income		—	—	—	—	—	—	35,121	35,121
Other comprehensive income		—	—	—	—	—	42	—	—	42
Total comprehensive income									35,163
Balance at September 30, 2011	72,579,381	$ 726	$ 29,077	$ —	$ 1,807,107	$ (3,606)	$ 4,623	$ (826,435)	$ 1,011,492

	Number of Common Shares	Common Stock	Series A Cumulative Redeemable Preferred Shares	Series B Cumulative Redeemable Preferred Shares	Additional Paid-In Capital	Accumulated Other Comprehensive Loss	Non-Controlling Interests in Consolidated Affiliates	Distributions in Excess of Net Income Available for Common Stockholders	Total
Balance at December 31, 2009	71,285,303	$ 713	$ 29,092	$ 52,500	$ 1,751,398	$ (3,811)	$ 5,183	$ (701,932)	$ 1,133,143
Issuances of Common Stock, net	112,815	1	—	—	2,075	—	—	—	2,076
Conversion of Common Units to Common Stock	93,971	1	—	—	2,957	—	—	—	2,958
Dividends on Common Stock	—	—	—	—	—	—	—	(91,197)	(91,197)
Dividends on Preferred Stock	—	—	—	—	—	—	—	(5,031)	(5,031)
Adjustment of noncontrolling interests in the Operating Partnership to fair value	—	—	—	—	1,480	—	—	—	1,480
Distributions to noncontrolling interests in consolidated affiliates	—	—	—	—	—	—	(506)	—	(506)
Issuances of restricted stock, net	164,143	—	—	—	—	—	—	—	—
Share-based compensation expense	—	2	—	—	5,058	—	—	—	5,060
Net (income) attributable to noncontrolling interests in the Operating Partnership	—	—	—	—	—	—	—	(2,819)	(2,819)
Net (income) attributable to	—	—	—	—	—	—	281	(281)	—

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

See accompanying notes to consolidated financial statements.

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HIGHWOODS PROPERTIES, INC.

Consolidated Statements of Cash Flows

(Unaudited and in thousands)

	Nine Months Ended September 30, 2011	2010
Operating activities:		
Net income	$ 35,121	$ 60,904
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	103,594	100,728
Amortization of lease incentives and acquisition-related intangible assets and liabilities	1,347	807
Share-based compensation expense	4,771	5,060
Allowance for losses on accounts and accrued straight-line rents receivable	1,586	3,605
Amortization of deferred financing costs	2,448	2,528
Amortization of settled cash-flow hedges	(87)	262
Impairment of assets held for use	2,429	—
Loss on debt extinguishment	24	85
Net (gains)/losses on disposition of property	(3,035)	31
(Gains)/losses on for-sale residential condominiums	322	(407)
Gains on disposition of investment in unconsolidated affiliates	(2,282)	(25,330)
Equity in earnings of unconsolidated affiliates	(3,933)	(2,701)
Changes in financing obligations	(339)	103
Distributions of earnings from unconsolidated affiliates	3,400	2,933
Changes in operating assets and liabilities:		
Accounts receivable	(3,493)	(4,689)
Prepaid expenses and other assets	(586)	(195)
Accrued straight-line rents receivable	(9,280)	(8,477)
Accounts payable, accrued expenses and other liabilities	4,118	7,407
Net cash provided by operating activities	136,125	142,654
Investing activities:		
Additions to real estate assets and deferred leasing costs	(150,558)	(66,370)
Net proceeds from disposition of real estate assets	16,530	6,801
Net proceeds from disposition of for-sale residential condominiums	2,770	3,732
Proceeds from disposition of investment in unconsolidated affiliates	4,756	15,000
Distributions of capital from unconsolidated affiliates	1,304	1,591
Repayments of mortgages and notes receivable	338	231
Investment in and advances to unconsolidated affiliates	(39,665)	(907)
Changes in restricted cash and other investing activities	(15,598)	2,396
Net cash used in investing activities	(180,123)	(37,526)
Financing activities:		
Dividends on Common Stock	(91,900)	(91,197)
Redemptions/repurchases of Preferred Stock	(52,515)	—

Dividends on Preferred Stock		(3,926)		(5,031)
Distributions to noncontrolling interests in the Operating Partnership		(4,818)		(4,857)
Distributions to noncontrolling interests in consolidated affiliates		(391)		(506)
Net proceeds from the issuance of Common Stock		22,043		2,076
Borrowings on revolving credit facility		285,400		4,000
Repayments of revolving credit facility		(150,400)		(4,000)
Borrowings on mortgages and notes payable		200,000		10,368
Repayments of mortgages and notes payable		(156,602)		(18,205)
Additions to deferred financing costs and other financing activities		(6,011)		(506)
Net cash provided by/(used in) financing activities		40,880		(107,858)
Net decrease in cash and cash equivalents		(3,118)		(2,730)
Cash and cash equivalents at beginning of the period		14,206		23,699
Cash and cash equivalents at end of the period	$	11,088	$	20,969

See accompanying notes to consolidated financial statements.

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HIGHWOODS PROPERTIES, INC.

Consolidated Statements of Cash Flows – Continued

(Unaudited and in thousands)

Supplemental disclosure of cash flow information:

	Nine Months Ended September 30, 2011	2010
Cash paid for interest, net of amounts capitalized	$ 69,321	$ 66,435

Supplemental disclosure of non-cash investing and financing activities:

	Nine Months Ended September 30, 2011	2010
Conversion of Common Units to Common Stock	$ 1,344	$ 2,958
Change in accrued capital expenditures	$ 3,707	$ 890
Write-off of fully depreciated real estate assets	$ 39,039	$ 34,703
Write-off of fully amortized deferred financing and leasing costs	$ 13,683	$ 11,521
Unrealized gains/(losses) on marketable securities of non-qualified deferred compensation plan	$ (354)	$ 489
Settlement of financing obligation	$ —	$ 4,184
Adjustment of noncontrolling interests in the Operating Partnership to fair value	$ (10,177)	$ (1,480)
Unrealized gain on tax increment financing bond	$ 129	$ 471
Mortgages receivable from seller financing	$ —	$ 17,030
Assumption of mortgages and notes payable related to acquisition activities	$ 192,367	$ 40,306

See accompanying notes to consolidated financial statements.

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements

September 30, 2011

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

(Unaudited)

1. Description of Business and Significant Accounting Policies

Description of Business

The Company is a fully-integrated, self-administered and self-managed equity real estate investment trust ("REIT") that provides leasing, management, development, construction and other customer-related services for its properties and for third parties. The Company conducts virtually all of its activities through the Operating Partnership. At September 30, 2011, the Company and/or the Operating Partnership wholly owned: 302 in-service office, industrial and retail properties, comprising 29.2 million square feet; 96 rental residential units; 18 for-sale residential condominiums; 601 acres of undeveloped land suitable for future development, of which 523 acres are considered core holdings; and an additional office property that is considered completed but not yet stabilized.

The Company is the sole general partner of the Operating Partnership. At September 30, 2011, the Company owned all of the Preferred Units and 72.2 million, or 95.1%, of the Common Units. Limited partners (including one officer and two directors of the Company) own the remaining 3.8 million Common Units. Generally, the Operating Partnership is obligated to redeem each Common Unit at the request of the holder thereof for cash equal to the value of one share of Common Stock, $.01 par value, based on the average of the market price for the 10 trading days immediately preceding the notice date of such redemption provided that the Company, at its option, may elect to acquire any such Common Units presented for redemption for cash or one share of Common Stock. The Common Units owned by the Company are not redeemable. During the nine months ended September 30, 2011, the Company redeemed 43,308 Common Units for a like number of shares of Common Stock.

Common Stock Offering

We have entered into equity sales agreements with various financial institutions to offer and sell, from time to time, shares of our Common Stock by means of ordinary brokers' transactions on the New York Stock Exchange or otherwise at market prices prevailing at the time of sale, at prices related to prevailing market prices or at negotiated prices or as otherwise agreed with any of the institutions. During the third quarter of 2011, we issued 142,000 shares of Common Stock under these agreements at an average price of $34.21 per share raising net proceeds, after sales commissions and expenses, of $4.8 million.

Basis of Presentation

Our Consolidated Financial Statements are prepared in conformity with accounting principles generally accepted in the United States of America ("GAAP"). Our Consolidated Statements of Income for the three and nine months ended September 30, 2010 were revised from previously reported amounts to reflect those properties sold or held for sale which required discontinued operations presentation.

Our Consolidated Financial Statements include the Operating Partnership, wholly owned subsidiaries and those entities in which we have the controlling financial interest. All significant intercompany transactions and accounts have been eliminated. At September 30, 2011 and December 31, 2010, we were not involved with any entities that were determined to be variable interest entities.

The unaudited interim consolidated financial statements and accompanying unaudited consolidated financial information, in the opinion of management, contain all adjustments (including normal recurring accruals) necessary for a fair presentation of our financial position, results of operations and cash flows. We have omitted certain notes and other information from the interim consolidated financial statements presented in this Quarterly Report on Form 10-Q as permitted by SEC rules and regulations. These Consolidated Financial Statements should be read in conjunction with our 2010 Annual Report on Form 10-K.

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

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

1. Description of Business and Significant Accounting Policies - Continued

Use of Estimates

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

Recently Issued Accounting Standards

Beginning with our Quarterly Report on Form 10-Q for the three months ended March 31, 2012, we will be required to enhance our disclosure of assets and liabilities measured at fair value. This includes disclosing any significant transfers between Levels 1 and 2 of the fair value hierarchy, additional quantitative and qualitative information regarding fair value measurements categorized as Level 3 of the fair value hierarchy and the hierarchy classification for items whose fair value is not recorded on our Consolidated Balance Sheets but is disclosed in our Notes to Consolidated Financial Statements. Additionally, we will be required to present comprehensive income on the face of our Consolidated Statements of Income, which previously has been disclosed in our Notes to Consolidated Financial Statements.

2. Real Estate Assets

Acquisitions

In the third quarter of 2011, we acquired a six-building, 1.54 million square foot office complex in Pittsburgh, PA for a purchase price of $188.5 million. The purchase price included the assumption of secured debt recorded at fair value of $124.5 million, with an effective interest rate of 4.27%, including amortization of deferred financing costs. This debt matures in November 2017. We expensed $4.0 million of costs related to this acquisition, which are included in general and administrative expense for the three and nine months ended September 30, 2011.

In the third quarter of 2011, we also acquired a 503,000 square foot office building in Atlanta, GA for a purchase price of $78.3 million. The purchase price included the assumption of secured debt recorded at fair value of $67.9 million, with an effective interest rate of 5.45%, including amortization of deferred financing costs. This debt matures in January 2014. We expensed $0.3 million of costs related to this acquisition, which are included in general and administrative expense for the three and nine months ended September 30, 2011.

The assets acquired and liabilities assumed were recorded at preliminary estimates of fair value as determined by management based on information available at the acquisition date and on current assumptions as to future operations. These estimates are subject to change during the measurement period upon the completion of acquisition accounting, including the finalization of asset valuations. The following table sets forth a summary of the preliminary acquisition purchase price consideration for each major class of assets acquired and liabilities assumed in the acquisitions discussed above:

	Total Purchase Price Consideration
Real estate assets	$ 241,602
Acquisition-related intangible assets (in deferred financing and leasing costs)	39,721
Furniture, fixtures and equipment (in prepaid expenses and other assets)	1,101
Acquisition-related intangible liabilities (in accounts payable, accrued expenses and other liabilities)	(15,627)
Total consideration	$ 266,797

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

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

2. Real Estate Assets - Continued

The following tables set forth our rental and other revenues and net income, adjusted for interest expense and depreciation and amortization related to purchase price allocation, assuming the acquisitions discussed above both occurred as of the beginning of each annual reporting period:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Proforma rental and other revenues	$ 133,669	$ 129,590	$ 393,640	$ 385,400
Proforma net income	$ 7,568	$ 8,180	$ 32,823	$ 59,124
Proforma earnings per share - basic	$ 0.09	$ 0.09	$ 0.34	$ 0.71
Proforma earnings per share - diluted	$ 0.09	$ 0.09	$ 0.34	$ 0.71

Dispositions

During the third quarter of 2011, we sold an office property and adjacent land parcel in one transaction in Winston-Salem, NC for gross proceeds of $15.0 million. We recorded gain on disposition of discontinued operations of $2.6 million and gain on disposition of property of $0.3 million related to the office property and land, respectively, in the third quarter of 2011.

Impairments

We recorded impairment of assets held for use of $2.4 million in the third quarter of 2011 on two office properties located in Orlando, FL due to a change in the assumed timing of future disposition. Impairments can arise from a number of factors; accordingly, there can be no assurances that we will not be required to record additional impairment charges in the future.

3. Mortgages and Notes Receivable

The following table sets forth our mortgages and notes receivable:

	September 30, 2011	December 31, 2010
Seller financing (first mortgages)	$ 17,180	$ 17,180
Less allowance	—	—
	17,180	17,180
Promissory notes	2,071	2,732
Less allowance	(545)	(868)
	1,526	1,864
Mortgages and notes receivable, net	$ 18,706	$ 19,044

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Beginning notes receivable allowance	$ 617	$ 771	$ 868	$ 698
Bad debt expense	—	240	184	328
Write-offs	(1)	(6)	(365)	(11)
Recoveries/other	(71)	(55)	(142)	(65)
Total notes receivable allowance	$ 545	$ 950	$ 545	$ 950

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

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

3. Mortgages and Notes Receivable - Continued

Our mortgages and notes receivable consists primarily of seller financing issued in conjunction with two disposition transactions in the second quarter of 2010. As of September 30, 2011, the contractual payments on both mortgages receivable were current and there were no indications of impairment on the receivables.

4. Investment in and Advances to Unconsolidated Affiliates

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Income Statements:				
Revenues	$ 25,623	$ 26,517	$ 75,619	$ 93,819
Expenses:				
Rental property and other expenses	10,805	12,664	33,576	45,463
Depreciation and amortization	6,759	6,730	19,670	24,108
Interest expense	5,976	6,094	17,841	21,892
Total expenses	23,540	25,488	71,087	91,463
Net income	$ 2,083	$ 1,029	$ 4,532	$ 2,356
Our share of:				
Depreciation and amortization of real estate assets	$ 2,066	$ 2,115	$ 6,192	$ 8,193
Interest expense	$ 1,965	$ 2,190	$ 6,159	$ 8,368
Net income	$ 442	$ 432	$ 2,112	$ 952
Our share of net income	$ 442	$ 432	$ 2,112	$ 952
Purchase accounting and management, leasing and other fees adjustments	671	586	1,821	1,749
Equity in earnings of unconsolidated affiliates	$ 1,113	$ 1,018	$ 3,933	$ 2,701

In the third quarter of 2011, our joint venture partner exercised its option to acquire our 10.0% equity interest in the HIW Development B, LLC joint venture, which recently completed construction of a build-to-suit office property in Charlotte, NC. As a result, we received gross proceeds of $4.8 million and recorded a gain on disposition of investment in unconsolidated affiliate related to this merchant build project of $2.3 million in the third quarter of 2011.

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

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

5. Intangible Assets and Liabilities

The following table sets forth total intangible assets and liabilities, net of accumulated amortization:

	September 30, 2011	December 31, 2010
Assets:		
Deferred financing costs	$ 19,168	$ 16,412
Less accumulated amortization	(6,192)	(7,054)
	12,976	9,358
Deferred leasing costs (including lease incentives and acquisition-related intangible assets)	171,093	127,949
Less accumulated amortization	(54,758)	(52,306)
	116,335	75,643
Deferred financing and leasing costs, net	$ 129,311	$ 85,001
Liabilities (in accounts payable, accrued expenses and other liabilities):		
Acquisition-related intangible liabilities	$ 16,455	$ 658
Less accumulated amortization	(425)	(125)
	$ 16,030	$ 533

The following table sets forth amortization of intangible assets and liabilities:

	Three Months Ended September 30, 2011	Three Months Ended September 30, 2010	Nine Months Ended September 30, 2011	Nine Months Ended September 30, 2010
Amortization of deferred financing costs	$ 806	$ 858	$ 2,448	$ 2,528
Amortization of deferred leasing costs and acquisition-related intangible assets (in depreciation and amortization)	$ 5,188	$ 3,912	$ 13,945	$ 11,495
Amortization of lease incentives (in rental and other revenues)	$ 368	$ 270	$ 1,009	$ 807
Amortization of acquisition-related intangible assets (in rental and other revenues)	$ 240	$ 200	$ 618	$ 318
Amortization of acquisition-related intangible liabilities (in rental and other revenues)	$ (229)	$ (27)	$ (280)	$ (69)

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

	Amortization of Deferred Financing Costs	Amortization of Deferred Leasing Costs and Acquisition-Related Intangible Assets (in Depreciation and Amortization)	Amortization of Lease Incentives (in Rental and Other Revenues)	Amortization of Acquisition-Related Intangible Assets (in Rental and Other Revenues)	Amortization of Acquisition-Related Intangible Liabilities (in Rental and Other Revenues)
October 1, 2011 through December 31, 2011	$ 931	$ 6,263	$ 323	$ 271	$ (141)
2012	3,192	22,604	1,234	1,049	(556)
2013	2,956	17,849	1,080	802	(542)
2014	2,660	13,609	913	505	(467)
2015	2,064	9,950	695	335	(421)
Thereafter	1,173	35,214	2,536	1,103	(13,903)
	$ 12,976	$ 105,489	$ 6,781	$ 4,065	$ (16,030)

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

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

5. Intangible Assets and Liabilities - Continued

The weighted average remaining amortization periods for deferred financing costs, deferred leasing costs and acquisition-related intangible assets (in depreciation and amortization), lease incentives (in rental and other revenues), acquisition-related intangible assets (in rental and other revenues) and acquisition-related intangible liabilities (in rental and other revenues) were 3.9 years, 6.4 years, 8.1 years, 5.8 years and 8.8 years, respectively, as of September 30, 2011.

In connection with the acquisitions of office properties in Atlanta, GA and Pittsburgh, PA in the third quarter of 2011, we recorded $1.6 million of above market lease intangible assets, $38.1 million of in-place lease intangible assets and $15.6 million of below market lease intangible liabilities with weighted average amortization periods of 5.4 years, 6.7 years and 8.8 years, respectively.

6. Mortgages and Notes Payable

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

	September 30, 2011	December 31, 2010
Secured indebtedness	$ 937,846	$ 754,399
Unsecured indebtedness	956,135	768,546
Total mortgages and notes payable	$ 1,893,981	$ 1,522,945

At September 30, 2011, our secured mortgage loans were secured by real estate assets with an aggregate undepreciated book value of $1.5 billion.

In the third quarter of 2011, we obtained a new $475.0 million unsecured revolving credit facility, which replaced our previously existing $400.0 million revolving credit facility. Our new revolving credit facility is originally scheduled to mature on July 27, 2015. Assuming no defaults have occurred, we have an option to extend the maturity for an additional year. The new credit facility includes an accordion feature that allows for an additional $75.0 million of borrowing capacity subject to additional lender commitments. The interest rate on the new facility at our current credit ratings is LIBOR plus 150 basis points and the annual facility fee is 35 basis points. The interest rate and facility fee under the new facility are based on the higher of the publicly announced ratings from Moody’s Investors Service or Standard & Poor’s. The financial and other covenants under the new facility are substantially the same as our previous credit facility. There was $165.0 million and $347.0 million outstanding under our revolving credit facility at September 30, 2011 and October 20, 2011, respectively. At both September 30, 2011 and October 20, 2011, we had $0.2 million of outstanding letters of credit, which reduces the availability on our revolving credit facility. As a result, the unused capacity of our revolving credit facility at September 30, 2011 and October 20, 2011 was $309.8 million and $127.8 million, respectively.

Our secured construction facility, which has $52.1 million outstanding at September 30, 2011, is scheduled to mature on December 20, 2011. Assuming no defaults have occurred, we have the option to extend the maturity date for an additional one-year period. The interest rate is LIBOR plus 85 basis points.

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

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

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

7. Noncontrolling Interests

Noncontrolling Interests in the Operating Partnership

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

	Nine Months Ended September 30,	
	2011	2010
Beginning noncontrolling interests in the Operating Partnership	$ 120,838	$ 129,769
Adjustments of noncontrolling interests in the Operating Partnership to fair value	(10,177)	(1,480)
Conversion of Common Units to Common Stock	(1,344)	(2,958)
Net income attributable to noncontrolling interests in the Operating Partnership	1,496	2,819
Distributions to noncontrolling interests in the Operating Partnership	(4,818)	(4,857)
Total noncontrolling interests in the Operating Partnership	$ 105,995	$ 123,293

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Net income available for common stockholders	$ 7,002	$ 6,878	$ 27,250	$ 52,773
Increase in additional paid in capital from conversion of Common Units to Common Stock	709	—	1,344	2,957
Change in equity from net income available for common stockholders and conversion of Common Units to Common Stock	$ 7,711	$ 6,878	$ 28,594	$ 55,730

Noncontrolling Interests in Consolidated Affiliates

At September 30, 2011, noncontrolling interests in consolidated affiliates relates to our joint venture partner’s 50.0% interest in office properties located in Richmond, VA. Our joint venture partner is an unrelated third party.

8. Disclosure About Fair Value of Financial Instruments

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

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

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

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

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

8. Disclosure About Fair Value of Financial Instruments - Continued

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

We had no Level 2 assets or liabilities at both September 30, 2011 and December 31, 2010.

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

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

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

	September 30, 2011	Level 1	Level 3
Assets:			
Marketable securities of non-qualified deferred compensation plan (in prepaid expenses and other assets)	$ 2,919	$ 2,919	$ —
Tax increment financing bond (in prepaid expenses and other assets)	15,828	—	15,828
Impaired real estate assets	7,772	—	7,772
Total Assets	$ 26,519	$ 2,919	$ 23,600
Noncontrolling Interests in the Operating Partnership	$ 105,995	$ 105,995	$ —
Liability:			
Non-qualified deferred compensation obligation (in accounts payable, accrued expenses and other liabilities)	$ 2,919	$ 2,919	$ —

	December 31, 2010	Level 1	Level 3
Assets:			
	$ 3,479	$ 3,479	$ —

Marketable securities of non-qualified deferred compensation plan (in prepaid expenses and other assets)			
Tax increment financing bond (in prepaid expenses and other assets)	15,699	—	15,699
Total Assets	$ 19,178	$ 3,479	$ 15,699
Noncontrolling Interests in the Operating Partnership	$ 120,838	$ 120,838	$ —
Liability:			
Non-qualified deferred compensation obligation (in accounts payable, accrued expenses and other liabilities)	$ 4,091	$ 4,091	$ —

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

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

8. Disclosure About Fair Value of Financial Instruments – Continued

The following table sets forth our Level 3 asset:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Asset:				
Tax Increment Financing Bond				
Beginning balance	$ 15,228	$ 17,017	$ 15,699	$ 16,871
Unrealized gain (in AOCL)	600	325	129	471
Ending balance	$ 15,828	$ 17,342	$ 15,828	$ 17,342

We own a tax increment financing bond associated with a property developed by us. This bond amortizes to maturity in 2020. The estimated fair value at September 30, 2011 was $2.4 million below the outstanding principal due on the bond. If the yield-to-maturity used to fair value this bond was 100 basis points higher or lower, the fair value of the bond would have been $0.6 million lower or higher, respectively, as of September 30, 2011. Currently, we intend to hold this bond and have concluded that we will not be required to sell this bond before recovery of the bond principal. Payment of the principal and interest for the bond is guaranteed by us and, therefore, we have recorded no credit losses related to the bond in the three and nine months ended September 30, 2011 and 2010. There is no legal right of offset with the liability, which we report as a financing obligation, related to this tax increment financing bond.

The following table sets forth the carrying amounts and fair values of our financial instruments not disclosed elsewhere in this Quarterly Report on Form 10-Q:

	Carrying Amount	Fair Value
September 30, 2011		
Mortgages and notes receivable	$ 18,706	$ 19,094
Mortgages and notes payable	$ 1,893,981	$ 1,987,983
Financing obligations	$ 32,775	$ 21,252
December 31, 2010		
Mortgages and notes receivable	$ 19,044	$ 19,093
Mortgages and notes payable	$ 1,522,945	$ 1,581,518
Financing obligations	$ 33,114	$ 23,880

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

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

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

9. Share-Based Payments

During the nine months ended September 30, 2011, we granted 146,581 stock options with an exercise price equal to the closing market price of a share of our Common Stock on the date of grant. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model, which resulted in a weighted average grant date fair value per share of $6.47. During the nine months ended September 30, 2011, we also granted 76,966 shares of time-based restricted stock and 57,386 shares of total return-based restricted stock with weighted average grant date fair values per share of $33.70 and $41.02, respectively. We recorded stock-based compensation expense of $1.3 million and $1.6 million during the three months ended September 30, 2011 and 2010, respectively, and $4.8 million and $5.1 million during the nine months ended September 30, 2011 and 2010, respectively. At September 30, 2011, there was $6.9 million of total unrecognized stock-based compensation costs, which will be recognized over a weighted average remaining service period of 2.2 years.

10. Comprehensive Income and Accumulated Other Comprehensive Loss

The following table sets forth the components of comprehensive income:

	Three Months Ended September 30, 2011	Three Months Ended September 30, 2010	Nine Months Ended September 30, 2011	Nine Months Ended September 30, 2010
Net income	$ 8,244	$ 8,773	$ 35,121	$ 60,904
Other comprehensive income:				
Unrealized gain on tax increment financing bond	600	325	129	471
Amortization of settled cash-flow hedges	(30)	(25)	(87)	262
Sale of cash-flow hedge related to disposition of investment in unconsolidated affiliate	—	—	—	103
Total other comprehensive income	570	300	42	836
Total comprehensive income	$ 8,814	$ 9,073	$ 35,163	$ 61,740

The following table sets forth the components of accumulated other comprehensive loss (“AOCL”):

	September 30, 2011	December 31, 2010
Tax increment financing bond	$ 2,413	$ 2,543
Settled cash-flow hedges	1,193	1,105
Total accumulated other comprehensive loss	$ 3,606	$ 3,648

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HIGHWOODS PROPERTIES, INC.

Notes To Consolidated Financial Statements (Continued)

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

11. Discontinued Operations

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Rental and other revenues	$ 480	$ 535	$ 1,593	$ 3,092
Operating expenses:				
Rental property and other expenses	211	166	570	1,214