

HRPT PROPERTIES TRUST  
Form 10-Q  
November 08, 2006

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
WASHINGTON, DC 20549

**FORM 10-Q**

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

**For the quarterly period ended September 30, 2006**

**OR**

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

**Commission File Number 1-9317**

**HRPT PROPERTIES TRUST**

**Maryland**  
(State of Organization)

**04-6558834**  
(IRS Employer Identification No.)

**400 Centre Street, Newton, Massachusetts 02458**

**617-332-3990**

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 **x** No **o**

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer **x** Accelerated filer **o** Non-accelerated filer **o**

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes **o** No **x**

Number of registrant's common shares of beneficial interest, \$0.01 par value per share, outstanding as of November 6, 2006: 210,036,590

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HRPT PROPERTIES TRUST

FORM 10-Q

SEPTEMBER 30, 2006

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*References in this Form 10-Q to the Company, we, us, our, and HRPT Properties refers to HRPT Properties Trust and its consolidated subsidiaries, unless otherwise noted.*

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**PART I      Financial Information****Item 1. Financial Statements**

## HRPT PROPERTIES TRUST

## CONSOLIDATED BALANCE SHEET

(amounts in thousands, except share data)

|                                                                                                                                                                                                 | September 30,<br>2006<br>(unaudited) | December 31,<br>2005 |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------|----------------------|
| <b><u>ASSETS</u></b>                                                                                                                                                                            |                                      |                      |
| Real estate properties:                                                                                                                                                                         |                                      |                      |
| Land                                                                                                                                                                                            | \$ 1,112,035                         | \$ 1,080,563         |
| Buildings and improvements                                                                                                                                                                      | 4,472,412                            | 4,144,011            |
|                                                                                                                                                                                                 | 5,584,447                            | 5,224,574            |
| Accumulated depreciation                                                                                                                                                                        | (639,132)                            | (548,460)            |
|                                                                                                                                                                                                 | 4,945,315                            | 4,676,114            |
| Properties held for sale                                                                                                                                                                        | 2,725                                | 10,779               |
| Acquired real estate leases                                                                                                                                                                     | 164,155                              | 161,787              |
| Equity investments in former subsidiaries                                                                                                                                                       |                                      | 194,297              |
| Cash and cash equivalents                                                                                                                                                                       | 33,458                               | 19,445               |
| Restricted cash                                                                                                                                                                                 | 22,775                               | 18,348               |
| Rents receivable, net of allowance for doubtful accounts of \$3,696 and \$3,767, respectively                                                                                                   | 165,691                              | 145,385              |
| Other assets, net                                                                                                                                                                               | 120,659                              | 101,012              |
| Total assets                                                                                                                                                                                    | \$ 5,454,778                         | \$ 5,327,167         |
| <b><u>LIABILITIES AND SHAREHOLDERS' EQUITY</u></b>                                                                                                                                              |                                      |                      |
| Revolving credit facility                                                                                                                                                                       | \$ 310,000                           | \$ 256,000           |
| Senior unsecured debt, net                                                                                                                                                                      | 1,940,878                            | 1,889,991            |
| Mortgage notes payable, net                                                                                                                                                                     | 388,743                              | 374,165              |
| Accounts payable and accrued expenses                                                                                                                                                           | 75,796                               | 80,125               |
| Acquired real estate lease obligations                                                                                                                                                          | 42,472                               | 38,987               |
| Rent collected in advance                                                                                                                                                                       | 20,211                               | 17,858               |
| Security deposits                                                                                                                                                                               | 15,154                               | 13,679               |
| Due to affiliates                                                                                                                                                                               | 19,643                               | 10,876               |
| Total liabilities                                                                                                                                                                               | 2,812,897                            | 2,681,681            |
| Shareholders' equity:                                                                                                                                                                           |                                      |                      |
| Preferred shares of beneficial interest, \$0.01 par value:                                                                                                                                      |                                      |                      |
| 50,000,000 shares authorized;                                                                                                                                                                   |                                      |                      |
| Series A preferred shares; 9 7/8% cumulative redeemable at par on February 22, 2006; zero and 8,000,000 shares issued and outstanding, respectively, aggregate liquidation preference \$200,000 |                                      | 193,086              |
| Series B preferred shares; 8 3/4% cumulative redeemable at par on September 12, 2007; 12,000,000 shares issued and outstanding, aggregate liquidation preference \$300,000                      | 289,849                              | 289,849              |
| Series C preferred shares; 7 1/8% cumulative redeemable at par on February 15, 2011; 6,000,000 and zero shares issued and outstanding, respectively, aggregate liquidation preference \$150,000 | 145,015                              |                      |
| Common shares of beneficial interest, \$0.01 par value:                                                                                                                                         |                                      |                      |
| 250,000,000 shares authorized; 210,036,590 and 209,860,625 shares issued and outstanding, respectively                                                                                          | 2,100                                | 2,099                |
| Additional paid in capital                                                                                                                                                                      | 2,774,270                            | 2,779,159            |
| Cumulative net income                                                                                                                                                                           | 1,665,477                            | 1,452,774            |
| Cumulative common distributions                                                                                                                                                                 | (2,027,081)                          | (1,894,818)          |
| Cumulative preferred distributions                                                                                                                                                              | (207,749)                            | (176,663)            |
| Total shareholders' equity                                                                                                                                                                      | 2,641,881                            | 2,645,486            |
| Total liabilities and shareholders' equity                                                                                                                                                      | \$ 5,454,778                         | \$ 5,327,167         |

See accompanying notes

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## HRPT PROPERTIES TRUST

## CONSOLIDATED STATEMENT OF INCOME

(amounts in thousands, except per share data)

(unaudited)

|                                                                                                                                                           | Three Months Ended<br>September 30,<br>2006 |         | Nine Months Ended<br>September 30,<br>2006 |          |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------|---------|--------------------------------------------|----------|
|                                                                                                                                                           | 2005                                        |         | 2005                                       |          |
| Rental income                                                                                                                                             | \$                                          | 202,542 | \$                                         | 182,894  |
|                                                                                                                                                           |                                             |         | \$                                         | 590,058  |
|                                                                                                                                                           |                                             |         | \$                                         | 523,262  |
| Expenses:                                                                                                                                                 |                                             |         |                                            |          |
| Operating expenses                                                                                                                                        |                                             | 80,219  |                                            | 69,173   |
| Depreciation and amortization                                                                                                                             |                                             | 41,064  |                                            | 34,490   |
| General and administrative                                                                                                                                |                                             | 8,513   |                                            | 9,102    |
| Total expenses                                                                                                                                            |                                             | 129,796 |                                            | 112,765  |
|                                                                                                                                                           |                                             |         |                                            | 372,016  |
|                                                                                                                                                           |                                             |         |                                            | 319,861  |
| Operating income                                                                                                                                          |                                             | 72,746  |                                            | 70,129   |
|                                                                                                                                                           |                                             |         |                                            | 218,042  |
|                                                                                                                                                           |                                             |         |                                            | 203,401  |
| Interest income                                                                                                                                           |                                             | 573     |                                            | 408      |
| Interest expense (including amortization of note discounts and premiums and deferred financing fees of \$1,105, \$392, \$3,348 and \$1,725, respectively) | (43,169                                     | )       | (35,628                                    | )        |
| Loss on early extinguishment of debt                                                                                                                      |                                             | (168    | )                                          | (126,317 |
| Equity in earnings of equity investments                                                                                                                  |                                             | 3,494   |                                            | 3,136    |
| Gain on sale of equity investments                                                                                                                        |                                             |         |                                            | 116,287  |
| Gain on issuance of shares by equity investees                                                                                                            |                                             |         |                                            | 4,708    |
| Income from continuing operations                                                                                                                         | 30,150                                      |         | 38,235                                     |          |
| Income (loss) from discontinued operations                                                                                                                | 32                                          |         | 62                                         |          |
| Gain on sale of properties                                                                                                                                | 1,172                                       |         |                                            | (76      |
| Net income                                                                                                                                                | 31,354                                      |         | 38,297                                     |          |
| Preferred distributions                                                                                                                                   | (9,234                                      | )       | (11,500                                    | )        |
| Excess redemption price paid over carrying value of preferred shares                                                                                      |                                             |         |                                            | (6,914   |
| Net income available for common shareholders                                                                                                              | \$                                          | 22,120  | \$                                         | 26,797   |
|                                                                                                                                                           |                                             |         | \$                                         | 175,813  |
|                                                                                                                                                           |                                             |         | \$                                         | 86,778   |
| Weighted average common shares outstanding                                                                                                                |                                             | 209,992 |                                            | 201,459  |
|                                                                                                                                                           |                                             |         |                                            | 209,941  |
|                                                                                                                                                           |                                             |         |                                            | 193,778  |
| Basic and diluted earnings per common share:                                                                                                              |                                             |         |                                            |          |
| Income from continuing operations                                                                                                                         | \$                                          | 0.10    | \$                                         | 0.13     |
| Income (loss) from discontinued operations                                                                                                                | \$                                          |         | \$                                         |          |
| Net income available for commonshareholders                                                                                                               | \$                                          | 0.11    | \$                                         | 0.13     |
|                                                                                                                                                           |                                             |         | \$                                         | 0.84     |
|                                                                                                                                                           |                                             |         | \$                                         | 0.45     |

See accompanying notes

## HRPT PROPERTIES TRUST

## CONSOLIDATED STATEMENT OF CASH FLOWS

(amounts in thousands)

(unaudited)

|                                                                               | Nine Months Ended September 30, |            |
|-------------------------------------------------------------------------------|---------------------------------|------------|
|                                                                               | 2006                            | 2005       |
| Cash flows from operating activities:                                         |                                 |            |
| Net income                                                                    | \$ 212,703                      | \$ 121,278 |
| Adjustments to reconcile net income to cash provided by operating activities: |                                 |            |
| Depreciation                                                                  | 96,452                          | 82,806     |
| Amortization of note discounts and premiums and deferred financing fees       | 3,348                           | 1,725      |
| Amortization of acquired real estate leases                                   | 22,495                          | 16,625     |
| Other amortization                                                            | 8,191                           | 6,484      |
| Loss on early extinguishment of debt                                          | 1,659                           |            |
| Equity in earnings of equity investments                                      | (3,136)                         | (9,940)    |
| Gain on sale of equity investments                                            | (116,287)                       |            |
| Gain on issuance of shares by equity investees                                |                                 | (4,708)    |
| Distributions of earnings from equity investments                             | 3,136                           | 9,940      |
| Gain on sale of properties                                                    | (1,172)                         | (7,592)    |
| Change in assets and liabilities:                                             |                                 |            |
| (Increase) decrease in restricted cash                                        | (4,427)                         | 5,162      |
| Increase in rents receivable and other assets                                 | (44,349)                        | (54,518)   |
| Decrease in accounts payable and accrued expenses                             | (4,329)                         | (2,715)    |
| Increase in rent collected in advance                                         | 2,353                           | 4,852      |
| Increase in security deposits                                                 | 1,475                           | 1,759      |
| Increase in due to affiliates                                                 | 8,767                           | 9,396      |
| Cash provided by operating activities                                         | 186,879                         | 180,554    |
| Cash flows from investing activities:                                         |                                 |            |
| Real estate acquisitions and improvements                                     | (366,370)                       | (411,277)  |
| Distributions in excess of earnings from equity investments                   | 2,251                           | 7,014      |
| Proceeds from sale of properties                                              | 6,231                           | 20,078     |
| Proceeds from sale of equity investments                                      | 308,333                         |            |
| Cash used for investing activities                                            | (49,555)                        | (384,185)  |
| Cash flows from financing activities:                                         |                                 |            |
| Proceeds from issuance of preferred shares, net                               | 145,015                         |            |
| Redemption of preferred shares                                                | (200,000)                       |            |
| Proceeds from issuance of common shares, net                                  |                                 | 383,974    |
| Proceeds from borrowings                                                      | 1,044,000                       | 622,000    |
| Payments on borrowings                                                        | (945,950)                       | (642,248)  |
| Deferred financing fees                                                       | (3,027)                         | (4,881)    |
| Distributions to common shareholders                                          | (132,263)                       | (121,161)  |
| Distributions to preferred shareholders                                       | (31,086)                        | (34,500)   |
| Cash (used for) provided by financing activities                              | (123,311)                       | 203,184    |
| Increase (decrease) in cash and cash equivalents                              | 14,013                          | (447)      |
| Cash and cash equivalents at beginning of period                              | 19,445                          | 21,961     |
| Cash and cash equivalents at end of period                                    | \$ 33,458                       | \$ 21,514  |

See accompanying notes



HRPT PROPERTIES TRUST

CONSOLIDATED STATEMENT OF CASH FLOWS (CONTINUED)

(amounts in thousands)

(unaudited)

|                                      | Nine Months Ended September 30, |            |
|--------------------------------------|---------------------------------|------------|
|                                      | 2006                            | 2005       |
| Supplemental cash flow information:  |                                 |            |
| Interest paid                        | \$ 131,809                      | \$ 120,666 |
| Non-cash investing activities:       |                                 |            |
| Real estate acquisitions             | \$ (20,585 )                    | \$         |
| Non-cash financing activities:       |                                 |            |
| Issuance of common shares            | \$ 2,026                        | \$ 565     |
| Assumption of mortgage notes payable | 20,585                          |            |

See accompanying notes

HRPT PROPERTIES TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(amounts in thousands, except share data)

**Note 1. Basis of Presentation**

The accompanying consolidated financial statements of HRPT Properties Trust and its subsidiaries have been prepared without audit. Certain information and footnote disclosures required by accounting principles generally accepted in the United States for complete financial statements have been condensed or omitted. We believe the disclosures made are adequate to make the information presented not misleading. However, the accompanying financial statements should be read in conjunction with the financial statements and notes contained in our Annual Report on Form 10-K for the year ended December 31, 2005. In the opinion of management, all adjustments, which include only normal recurring adjustments considered necessary for a fair presentation, have been included. All intercompany transactions and balances between HRPT Properties Trust and its subsidiaries have been eliminated. Operating results for interim periods are not necessarily indicative of the results that may be expected for the full year. Reclassifications have been made to the prior years' financial statements to conform to the current year's presentation.

**Note 2. Real Estate Properties**

During the nine months ended September 30, 2006, we acquired 46 office properties and one industrial property for \$306,856, excluding closing costs, and funded \$75,946 of improvements to our owned properties using cash on hand, borrowings under our revolving credit facility and the assumption of \$20,585 of mortgage debt. We also sold four office properties for gross proceeds of \$9,200 (\$6,231 after closing costs and deposits required to defease related mortgages) and recognized a gain of \$1,172 during the nine months ended September 30, 2006.

As of September 30, 2006, we had outstanding agreements to purchase 15 properties containing approximately 1,652 square feet of space for \$120,475, plus closing costs. These properties were acquired in October 2006.

**Note 3. Indebtedness**

In March 2006 we issued \$400,000 of unsecured floating rate senior notes in a public offering, raising net proceeds of approximately \$398,700. The notes bear interest at LIBOR plus a premium (6.0% at September 30, 2006), require quarterly interest payments and mature in March 2011. Net proceeds from this offering were used to reduce amounts outstanding under our revolving credit facility and for general business purposes. In March 2006 we also repaid our \$350,000 term loan that was scheduled to mature in August 2009. We recognized a loss of \$1,659 from the write off of deferred financing fees in connection with this repayment.

We have an unsecured revolving credit facility with a borrowing capacity of \$750,000 that we use for acquisitions, working capital and general business purposes. In August 2006, we amended and extended the maturity of this credit facility from April 2009 to August 2010, with an option to extend the facility an additional year. Interest paid on drawings under this facility was reduced from LIBOR plus 65 basis points to LIBOR plus 55 basis points. Certain covenants were also amended to reflect current market conditions. The interest rate on this facility averaged 5.6% and 3.8% per annum, for the nine months ended September 30, 2006 and 2005, respectively. As of September 30, 2006, we had \$310,000 outstanding and \$440,000 available under our revolving credit facility. Our public debt indentures and credit facility agreement contain a number of financial and other covenants, including a credit facility covenant which limits the amount of aggregate distributions on common shares to 90% of operating cash flow available for shareholder distributions as defined in the credit facility agreement.

**Note 4. Shareholders' Equity**

In February 2006 we issued 6,000,000 series C cumulative redeemable preferred shares in a public offering, raising net proceeds of \$145,015. Each series C preferred share has a liquidation preference of \$25.00 and requires dividends of \$1.78125, 7 1/8% of the liquidation preference per annum, payable in equal quarterly payments. Our series C preferred shares are redeemable, at our option, for \$25.00 each plus accrued and unpaid dividends at any time on or after February 15, 2011. Net proceeds from this offering were used to reduce amounts outstanding under our revolving credit facility. In March 2006 we redeemed all \$200,000 of our 9.875% series A preferred shares by borrowing under our revolving credit facility. In connection with this redemption, the \$6,914 excess of the liquidation preference of the redeemed shares over their carrying amount was deducted from net income to determine net income available for common shareholders for the first quarter of 2006.



On April 10, 2006, we issued 113,665 common shares to our manager, Reit Management & Research LLC, or RMR, in payment of an incentive fee of \$1,298 for services rendered during 2005 based upon a per common share price of \$11.42, the closing price of our common shares on the New York Stock Exchange, or NYSE, on that day. On May 23, 2006, we issued 11,250 common shares to our trustees as part of their annual compensation based upon a per common share price of \$10.87, the closing price of our common shares on the NYSE on that day, and on September 20, 2006, we granted 51,050 common shares pursuant to our Incentive Share Award Plan to our officers and certain employees of RMR, based upon a per common share price of \$11.88, the closing price of our common shares on the NYSE on that day.

**Note 5. Equity Investments**

At September 30, 2006, and December 31, 2005, we had the following equity investments in Senior Housing Properties Trust, or Senior Housing, and Hospitality Properties Trust, or Hospitality Properties:

|                        | Equity Investments    |                      | Equity in Earnings<br>Three Months Ended |          | Nine Months Ended     |          |
|------------------------|-----------------------|----------------------|------------------------------------------|----------|-----------------------|----------|
|                        | September 30,<br>2006 | December 31,<br>2005 | September 30,<br>2006                    | 2005     | September 30,<br>2006 | 2005     |
| Senior Housing         | \$                    | \$ 94,952            | \$                                       | \$ 1,770 | \$ 1,512              | \$ 5,425 |
| Hospitality Properties |                       | 99,345               |                                          | 1,724    | 1,624                 | 4,515    |
|                        | \$                    | \$ 194,297           | \$                                       | \$ 3,494 | \$ 3,136              | \$ 9,940 |

In March 2006 we sold all 7,710,738 Senior Housing common shares we owned for \$17.60 per common share, raising gross proceeds of \$135,709 (net \$133,064) and realizing a gain of \$39,066, and we sold all 4,000,000 Hospitality Properties common shares we owned for \$44.75 per common share, raising gross proceeds of \$179,000 (net \$175,269) and realizing a gain of \$77,221.

**Note 6. Segment Information**

As of September 30, 2006, we owned 348 office properties and 139 industrial properties, excluding properties under contract for sale. We account for our office and industrial properties in geographic operating segments for financial reporting purposes based on our method of internal reporting. We define these individual geographic segments as those which currently, or during either of the last two quarters, represent or generate 5% or more of our total square feet, revenues or property net operating income. Property level information by geographic segment and property type as of and for the three and nine months ended September 30, 2006 and 2005, is as follows:

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|                                   | As of September 30, 2006 |                          |        | As of September 30, 2005 |                          |        |
|-----------------------------------|--------------------------|--------------------------|--------|--------------------------|--------------------------|--------|
|                                   | Office<br>Properties     | Industrial<br>Properties | Totals | Office<br>Properties     | Industrial<br>Properties | Totals |
| Property square feet:             |                          |                          |        |                          |                          |        |
| Metro Philadelphia, PA            | 5,453                    |                          | 5,453  | 5,454                    |                          | 5,454  |
| Oahu, HI                          |                          | 17,929                   | 17,929 |                          | 17,879                   | 17,879 |
| Metro Washington, DC              | 2,645                    |                          | 2,645  | 2,645                    |                          | 2,645  |
| Metro Boston, MA                  | 2,740                    |                          | 2,740  | 2,738                    |                          | 2,738  |
| Southern California               | 1,444                    |                          | 1,444  | 1,444                    |                          | 1,444  |
| Metro Austin, TX                  | 1,492                    | 1,316                    | 2,808  | 1,490                    | 1,316                    | 2,806  |
| Other Markets                     | 20,170                   | 4,881                    | 25,051 | 16,491                   | 4,573                    | 21,064 |
| Totals                            | 33,944                   | 24,126                   | 58,070 | 30,262                   | 23,768                   | 54,030 |
| Central business district, or CBD | 11,335                   | 158                      | 11,493 | 11,331                   | 158                      | 11,489 |
| Suburban                          | 22,609                   | 23,968                   | 46,577 | 18,931                   | 23,610                   | 42,541 |
| Total                             | 33,944                   | 24,126                   | 58,070 | 30,262                   | 23,768                   | 54,030 |

|                         | Three Months Ended<br>September 30, 2006 |                          |            | Three Months Ended<br>September 30, 2005 |                          |            |
|-------------------------|------------------------------------------|--------------------------|------------|------------------------------------------|--------------------------|------------|
|                         | Office<br>Properties                     | Industrial<br>Properties | Totals     | Office<br>Properties                     | Industrial<br>Properties | Totals     |
| Property rental income: |                                          |                          |            |                                          |                          |            |
| Metro Philadelphia, PA  | \$ 31,784                                | \$                       | \$ 31,784  | \$ 33,761                                | \$                       | \$ 33,761  |
| Oahu, HI                |                                          | 16,369                   | 16,369     |                                          | 14,462                   | 14,462     |
| Metro Washington, DC    | 19,972                                   |                          | 19,972     | 19,741                                   |                          | 19,741     |
| Metro Boston, MA        | 15,517                                   |                          | 15,517     | 15,093                                   |                          | 15,093     |
| Southern California     | 12,323                                   |                          | 12,323     | 12,457                                   |                          | 12,457     |
| Metro Austin, TX        | 7,298                                    | 3,454                    | 10,752     | 5,749                                    | 3,888                    | 9,637      |
| Other Markets           | 85,775                                   | 10,050                   | 95,825     | 68,179                                   | 9,564                    | 77,743     |
| Totals                  | \$ 172,669                               | \$ 29,873                | \$ 202,542 | \$ 154,980                               | \$ 27,914                | \$ 182,894 |
| CBD                     | \$ 72,382                                | \$ 291                   | \$ 72,673  | \$ 72,537                                | \$ 279                   | \$ 72,816  |
| Suburban                | 100,287                                  | 29,582                   | 129,869    | 82,443                                   | 27,635                   | 110,078    |
| Total                   | \$ 172,669                               | \$ 29,873                | \$ 202,542 | \$ 154,980                               | \$ 27,914                | \$ 182,894 |

|                                | Three Months Ended<br>September 30, 2006 |                          |            | Three Months Ended<br>September 30, 2005 |                          |            |
|--------------------------------|------------------------------------------|--------------------------|------------|------------------------------------------|--------------------------|------------|
|                                | Office<br>Properties                     | Industrial<br>Properties | Totals     | Office<br>Properties                     | Industrial<br>Properties | Totals     |
| Property net operating income: |                                          |                          |            |                                          |                          |            |
| Metro Philadelphia, PA         | \$ 17,025                                | \$                       | \$ 17,025  | \$ 18,641                                | \$                       | \$ 18,641  |
| Oahu, HI                       |                                          | 13,274                   | 13,274     |                                          | 11,568                   | 11,568     |
| Metro Washington, DC           | 12,333                                   |                          | 12,333     | 12,651                                   |                          | 12,651     |
| Metro Boston, MA               | 9,917                                    |                          | 9,917      | 10,074                                   |                          | 10,074     |
| Southern California            | 8,522                                    |                          | 8,522      | 8,630                                    |                          | 8,630      |
| Metro Austin, TX               | 3,334                                    | 1,863                    | 5,197      | 2,384                                    | 1,968                    | 4,352      |
| Other Markets                  | 49,258                                   | 6,797                    | 56,055     | 41,591                                   | 6,214                    | 47,805     |
| Totals                         | \$ 100,389                               | \$ 21,934                | \$ 122,323 | \$ 93,971                                | \$ 19,750                | \$ 113,721 |
| CBD                            | \$ 40,136                                | \$ 214                   | \$ 40,350  | \$ 41,209                                | \$ 215                   | \$ 41,424  |
| Suburban                       | 60,253                                   | 21,720                   | 81,973     | 52,762                                   | 19,535                   | 72,297     |
| Total                          | \$ 100,389                               | \$ 21,934                | \$ 122,323 | \$ 93,971                                | \$ 19,750                | \$ 113,721 |



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|                         | Nine Months Ended<br>September 30, 2006 |                          |            | Nine Months Ended<br>September 30, 2005 |                          |            |
|-------------------------|-----------------------------------------|--------------------------|------------|-----------------------------------------|--------------------------|------------|
|                         | Office<br>Properties                    | Industrial<br>Properties | Totals     | Office<br>Properties                    | Industrial<br>Properties | Totals     |
| Property rental income: |                                         |                          |            |                                         |                          |            |
| Metro Philadelphia, PA  | \$ 95,277                               | \$                       | \$ 95,277  | \$ 100,490                              | \$                       | \$ 100,490 |
| Oahu, HI                |                                         | 45,580                   | 45,580     |                                         | 36,724                   | 36,724     |
| Metro Washington, DC    | 59,182                                  |                          | 59,182     | 57,461                                  |                          | 57,461     |
| Metro Boston, MA        | 45,545                                  |                          | 45,545     | 43,157                                  |                          | 43,157     |
| Southern California     | 36,128                                  |                          | 36,128     | 35,525                                  |                          | 35,525     |
| Metro Austin, TX        | 21,157                                  | 10,548                   | 31,705     | 16,830                                  | 12,279                   | 29,109     |
| Other Markets           | 247,069                                 | 29,572                   | 276,641    | 192,237                                 | 28,559                   | 220,796    |
| Totals                  | \$ 504,358                              | \$ 85,700                | \$ 590,058 | \$ 445,700                              | \$ 77,562                | \$ 523,262 |
| CBD                     | \$ 214,960                              | \$ 850                   | \$ 215,810 | \$ 208,049                              | \$ 811                   | \$ 208,860 |
| Suburban                | 289,398                                 | 84,850                   | 374,248    | 237,651                                 | 76,751                   | 314,402    |
| Total                   | \$ 504,358                              | \$ 85,700                | \$ 590,058 | \$ 445,700                              | \$ 77,562                | \$ 523,262 |

|                                | Nine Months Ended<br>September 30, 2006 |                          |            | Nine Months Ended<br>September 30, 2005 |                          |            |
|--------------------------------|-----------------------------------------|--------------------------|------------|-----------------------------------------|--------------------------|------------|
|                                | Office<br>Properties                    | Industrial<br>Properties | Totals     | Office<br>Properties                    | Industrial<br>Properties | Totals     |
| Property net operating income: |                                         |                          |            |                                         |                          |            |
| Metro Philadelphia, PA         | \$ 51,096                               | \$                       | \$ 51,096  | \$ 55,509                               | \$                       | \$ 55,509  |
| Oahu, HI                       |                                         | 37,033                   | 37,033     |                                         | 29,431                   | 29,431     |
| Metro Washington, DC           | 37,068                                  |                          | 37,068     | 37,298                                  |                          | 37,298     |
| Metro Boston, MA               | 29,920                                  |                          | 29,920     | 29,268                                  |                          | 29,268     |
| Southern California            | 25,084                                  |                          | 25,084     | 24,093                                  |                          | 24,093     |
| Metro Austin, TX               | 10,028                                  | 5,779                    | 15,807     | 7,794                                   | 5,861                    | 13,655     |
| Other Markets                  | 146,284                                 | 19,785                   | 166,069    | 118,825                                 | 19,169                   | 137,994    |
| Totals                         | \$ 299,480                              | \$ 62,597                | \$ 362,077 | \$ 272,787                              | \$ 54,461                | \$ 327,248 |
| CBD                            | \$ 120,211                              | \$ 644                   | \$ 120,855 | \$ 119,304                              | \$ 646                   | \$ 119,950 |
| Suburban                       | 179,269                                 | 61,953                   | 241,222    | 153,483                                 | 53,815                   | 207,298    |
| Total                          | \$ 299,480                              | \$ 62,597                | \$ 362,077 | \$ 272,787                              | \$ 54,461                | \$ 327,248 |

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The table below reconciles our calculation of property net operating income, or NOI, to net income available for common shareholders, the most directly comparable financial measure under generally accepted accounting principles, or GAAP, reported in our consolidated financial statements for the three and nine months ended September 30, 2006 and 2005. We consider NOI to be appropriate supplemental information to net income available for common shareholders because it helps both investors and management to understand the operations of our properties. We use NOI internally as a performance measure and believe NOI provides useful information to investors regarding our results of operations because it reflects only those income and expense items that are incurred at the property level. Our management also uses NOI to evaluate individual, regional and company wide property level performance. NOI excludes certain components from net income available for common shareholders in order to provide results that are more closely related to our properties' results of operations. NOI does not represent cash generated by operating activities in accordance with GAAP and should not be considered an alternative to net income, net income available for common shareholders or cash flow from operating activities as a measure of financial performance.

|                                                                      | Three Months Ended<br>September 30, |            | Nine Months Ended<br>September 30, |            |
|----------------------------------------------------------------------|-------------------------------------|------------|------------------------------------|------------|
|                                                                      | 2006                                | 2005       | 2006                               | 2005       |
| Rental income                                                        | \$ 202,542                          | \$ 182,894 | \$ 590,058                         | \$ 523,262 |
| Operating expenses                                                   | (80,219 )                           | (69,173 )  | (227,981 )                         | (196,014 ) |
| Property net operating income (NOI)                                  | \$ 122,323                          | \$ 113,721 | \$ 362,077                         | \$ 327,248 |
| Property net operating income                                        | \$ 122,323                          | \$ 113,721 | \$ 362,077                         | \$ 327,248 |
| Depreciation and amortization                                        | (41,064 )                           | (34,490 )  | (119,109 )                         | (100,417 ) |
| General and administrative                                           | (8,513 )                            | (9,102 )   | (24,926 )                          | (23,430 )  |
| Operating income                                                     | 72,746                              | 70,129     | 218,042                            | 203,401    |
| Interest income                                                      | 573                                 | 408        | 2,118                              | 1,289      |
| Interest expense                                                     | (43,169 )                           | (35,628 )  | (126,317 )                         | (105,967 ) |
| Loss on early extinguishment of debt                                 |                                     | (168 )     | (1,659 )                           | (168 )     |
| Equity in earnings of equity investments                             |                                     | 3,494      | 3,136                              | 9,940      |
| Gain on sale of equity investments                                   |                                     |            | 116,287                            |            |
| Gain on issuance of shares by equity investees                       |                                     |            |                                    | 4,708      |
| Income from continuing operations                                    | 30,150                              | 38,235     | 211,607                            | 113,203    |
| Income (loss) from discontinued operations                           | 32                                  | 62         | (76 )                              | 483        |
| Gain on sale of properties                                           | 1,172                               |            | 1,172                              | 7,592      |
| Net income                                                           | 31,354                              | 38,297     | 212,703                            | 121,278    |
| Preferred distributions                                              | (9,234 )                            | (11,500 )  | (29,976 )                          | (34,500 )  |
| Excess redemption price paid over carrying value of preferred shares |                                     |            | (6,914 )                           |            |
| Net income available for common shareholders                         | \$ 22,120                           | \$ 26,797  | \$ 175,813                         | \$ 86,778  |

### **Note 7. Subsequent Events**

In October 2006, we declared a distribution of \$0.21 per common share, or approximately \$44,000, to be paid on or about November 22, 2006, to shareholders of record on October 23, 2006. We also announced a distribution on our series B preferred shares of \$0.5469 per share, or \$6,563, and a distribution on our series C preferred shares of \$0.4453 per share, or \$2,672, which will be paid on or about November 15, 2006, to our series B and C preferred shareholders of record as of November 1, 2006.

In October 2006, we purchased 15 properties with a total of approximately 1,652 square feet of space for \$120,475, plus closing costs, using cash on hand, borrowings under our revolving credit facility and the assumption of debt. As of November 6, 2006, we have executed purchase agreements for two additional properties with an aggregate of 167 square feet of space and an aggregate purchase price of \$29,200. In addition, we have an executed purchase agreement for the sale of one property with approximately 33 square feet of space at a sale price of \$4,500. This property is classified as held for sale on our consolidated balance sheet and its operating results are included in discontinued operations in our consolidated statement of income. We currently expect to close the sale of this property in the fourth quarter of 2006. These potential purchase and sale transactions are subject to completion of due diligence and customary closing contingencies, and because of these contingencies we can provide no assurances that we will purchase or sell these properties.

In October 2006, we issued an aggregate of 15,180,000 series D cumulative convertible preferred shares, including 1,980,000 shares issued to cover over-allotments, in a public offering for net proceeds of approximately \$368,300. Each series D preferred share has a liquidation preference of \$25.00 and requires dividends of \$1.625, 6 ½%, per annum, payable in equal quarterly payments. Our series D preferred shares are convertible, at the holder's option, into our common shares at an initial conversion rate of 1.9231 common shares per series D preferred share, which is equivalent to an initial conversion price of \$13.00 per common share. On or after November 20, 2011, if our common shares trade at or above the then applicable conversion price, we may, at our option, convert some or all of the series D preferred shares into common shares at the then applicable conversion rate. Net proceeds from this offering were used to reduce amounts outstanding on our revolving credit facility and for general business purposes, including acquisitions.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and tables should be read in conjunction with our consolidated financial statements and notes thereto included in this quarterly report and our 2005 Annual Report on Form 10-K for the year ended December 31, 2005.

### OVERVIEW

We primarily own office buildings located throughout the United States. We also own approximately 18 million square feet of leased industrial and commercial lands in Oahu, Hawaii.

#### *Property Operations*

As of September 30, 2006, 93.4% of our total square feet was leased, compared to 93.9% leased as of September 30, 2005. The decrease reflects property acquisitions and a decrease in occupancy of 0.4% at properties we owned continuously since July 1, 2005. Occupancy data is as follows (square feet in thousands):

|                    | All Properties (1)<br>As of September 30, |        | Comparable Properties (2)<br>As of September 30, |        |
|--------------------|-------------------------------------------|--------|--------------------------------------------------|--------|
|                    | 2006                                      | 2005   | 2006                                             | 2005   |
| Total properties   | 487                                       | 429    | 410                                              | 410    |
| Total square feet  | 58,070                                    | 54,030 | 52,750                                           | 52,750 |
| Percent leased (3) | 93.4                                      | %      | 93.9                                             | %      |

---

(1) Excludes properties sold or under contract for sale.

(2) Based on properties owned continuously since July 1, 2005, and excludes properties under contract for sale.

(3) Percent leased includes (i) space being fitted out for occupancy pursuant to signed leases and (ii) space which is leased, but is not occupied or is being offered for sublease by tenants.

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During the third quarter of 2006 we signed new leases for 642,000 square feet and lease renewals for 766,000 square feet, at weighted average rental rates that were 9% above rents previously charged for the same space. Average lease terms for leases signed during the quarter ended September 30, 2006, were 6.3 years. Commitments for tenant improvement and leasing costs for leases signed during the quarter ended September 30, 2006, totaled \$25.7 million, or \$18.24 per square foot (approximately \$2.89/sq. ft. per year of the lease term).

During the past twelve months, the leasing market conditions in some of our markets have been improving. The occupancies at some of our continuously owned properties have stabilized and quoted rental rates in most of the areas where our properties are located seem to have increased modestly. Although required landlord funded tenant build outs and leasing commissions payable to tenant brokers for new leases and lease renewals rose to \$18.24 per square foot during the current quarter, these costs have generally stabilized or declined modestly over the past twelve months. These build out costs and leasing commissions are generally amortized as a reduction of our income during the terms of the affected leases. We believe that modest increases in effective rents will improve the financial results at some of our currently owned properties during the remainder of 2006. There are too many variables for us to reasonably project what the financial impact of market conditions will be on our results for future periods beyond 2006.

Approximately 22% of our leased square feet are under leases scheduled to expire through December 31, 2008. Lease renewals and rental rates at which available space may be relet in the future will depend on prevailing market conditions at that time. Lease expirations by year, as of September 30, 2006, are as follows (in thousands):

| Year                                              | Sq. Ft.<br>Expiring (1) | % of Sq. Ft.<br>Expiring | Annualized<br>Rental Income<br>Expiring (2) | % of<br>Annualized<br>Rental<br>Income<br>Expiring | Cumulative<br>% of<br>Annualized<br>Rental<br>Income<br>Expiring |   |
|---------------------------------------------------|-------------------------|--------------------------|---------------------------------------------|----------------------------------------------------|------------------------------------------------------------------|---|
| 2006                                              | 1,476                   | 2.7                      | % \$ 30,589                                 | 3.8                                                | % 3.8                                                            | % |
| 2007                                              | 3,890                   | 7.2                      | % 69,245                                    | 8.5                                                | % 12.3                                                           | % |
| 2008                                              | 4,602                   | 8.5                      | % 80,247                                    | 9.9                                                | % 22.2                                                           | % |
| 2009                                              | 3,658                   | 6.7                      | % 65,468                                    | 8.1                                                | % 30.3                                                           | % |
| 2010                                              | 5,166                   | 9.5                      | % 91,899                                    | 11.3                                               | % 41.6                                                           | % |
| 2011                                              | 4,957                   | 9.1                      | % 87,948                                    | 10.8                                               | % 52.4                                                           | % |
| 2012                                              | 3,748                   | 6.9                      | % 74,273                                    | 9.2                                                | % 61.6                                                           | % |
| 2013                                              | 2,210                   | 4.1                      | % 41,673                                    | 5.1                                                | % 66.7                                                           | % |
| 2014                                              | 2,440                   | 4.5                      | % 43,222                                    | 5.3                                                | % 72.0                                                           | % |
| 2015                                              | 2,405                   | 4.4                      | % 52,087                                    | 6.4                                                | % 78.4                                                           | % |
| 2016 and thereafter                               | 19,700                  | 36.4                     | % 174,765                                   | 21.6                                               | % 100.0                                                          | % |
|                                                   | 54,252                  | 100.0                    | % \$ 811,416                                | 100.0                                              | %                                                                |   |
| Weighted average remaining lease term (in years): |                         |                          |                                             |                                                    |                                                                  |   |
|                                                   | 9.5                     |                          | 6.5                                         |                                                    |                                                                  |   |

(1) Square feet is pursuant to signed leases as of September 30, 2006, and includes (i) space being fitted out for occupancy and (ii) space which is leased, but is not occupied or is being offered for sublease by tenants. Excludes square feet from properties classified in discontinued operations.

(2) Rents are pursuant to signed leases as of September 30, 2006, plus expense reimbursements; includes some triple net lease rents and excludes lease value amortization and rents from properties classified in discontinued operations.

**Our principal source of funds for our operations is rents from tenants at our properties. Rents are generally received from our non-government tenants monthly in advance, and from our government tenants monthly in arrears. As of September 30, 2006, tenants responsible for 1% or more of our total rent were as follows (square feet in thousands):**

| <b>Tenant</b>                              | <b>Square Feet (1)</b> | <b>% of Total<br/>Square Feet (1)</b> | <b>% of<br/>Rent (2)</b> | <b>Expiration</b>     |
|--------------------------------------------|------------------------|---------------------------------------|--------------------------|-----------------------|
| 1. U. S. Government                        | 4,943                  | 9.1                                   | % 13.4                   | % 2006 to 2020        |
| 2. GlaxoSmithKline plc                     | 608                    | 1.1                                   | % 1.8                    | % 2013                |
| 3. PNC Financial Services Group            | 460                    | 0.8                                   | % 1.4                    | % 2011, 2021          |
| 4. Comcast Corporation                     | 400                    | 0.7                                   | % 1.2                    | % 2006, 2008          |
| 5. Solecron Corporation                    | 765                    | 1.4                                   | % 1.1                    | % 2014                |
| 6. Motorola, Inc.                          | 766                    | 1.4                                   | % 1.1                    | 2006, 2008,<br>% 2010 |
| 7. JDA Software Group, Inc.                | 283                    | 0.5                                   | % 1.1                    | % 2012                |
| 8. The Scripps Research Institute          | 164                    | 0.3                                   | % 1.1                    | % 2019                |
| 9. Tyco International Ltd                  | 660                    | 1.2                                   | % 1.1                    | % 2007, 2017          |
| 10. Ballard Spahr Andrews & Ingersoll, LLP | 231                    | 0.4                                   | % 1.0                    | % 2008, 2015          |
| 11. Westinghouse Electric Corporation      | 534                    | 1.0                                   | % 1.0                    | % 2010, 2011          |
| Total                                      | 9,814                  | 17.9                                  | % 25.3                   | %                     |

(1) Square feet is pursuant to signed leases as of September 30, 2006, and includes (i) space being fitted out for occupancy and (ii) space which is leased, but is not occupied or is being offered for sublease by tenants. Excludes square feet from properties classified in discontinued operations.

(2) Rents are pursuant to signed leases as of September 30, 2006, plus expense reimbursements; includes some triple net lease rents and excludes lease value amortization and rents from properties classified in discontinued operations.

#### ***Investing Activities***

During the nine months ended September 30, 2006, we acquired 46 office properties and one industrial property for \$306.9 million, excluding closing costs, and funded \$75.9 million of improvements to our owned properties using cash on hand, borrowings under our revolving credit facility and the assumption of \$20.6 million of mortgage debt. We also sold four office properties with a total of approximately 68,000 square feet of space for gross proceeds of \$9.2 million (\$6.2 million after closing costs and deposits required to defease related mortgages). In addition, we have an executed purchase agreement for the sale of one property with approximately 33,000 square feet of space at a sale price of \$4.5 million. We currently expect to close the sale of this property in the fourth quarter of 2006. This potential sale transaction is subject to closing contingencies, and because of these contingencies we can provide no assurances that we will sell this property. This property is classified as held for sale on our consolidated balance sheet and its operating results are included in discontinued operations in our consolidated statement of income.

***Financing Activities***

In February 2006 we issued six million series C cumulative redeemable preferred shares in a public offering, raising net proceeds of \$145.0 million. In March 2006 we issued \$400 million of unsecured floating rate senior notes in a public offering, raising net proceeds of approximately \$398.7 million. Net proceeds from these offerings were used to reduce amounts outstanding under our revolving credit facility and for general business purposes. In March 2006 we redeemed all \$200 million of our series A preferred shares and repaid our \$350 million term loan by borrowing under our revolving credit facility. In October 2006, we issued 15.2 million series D cumulative convertible preferred shares, including 2.0 million shares issued to cover over-allotments, in a public offering for net proceeds of approximately \$368.3 million. Each series D preferred share has a liquidation preference of \$25.00 and requires dividends of \$1.625, 6 ½%, per annum, payable in equal quarterly payments. Our series D preferred shares are convertible, at the holder's option, into our common shares at an initial conversion rate of 1.9231 common shares per series D preferred share, which is equivalent to an initial conversion price of \$13.00 per common share. On or after November 20, 2011, if our common shares trade at or above the then applicable conversion price, we may, at our option, convert some or all of the series D preferred shares into common shares at the then applicable conversion rate. Net proceeds from this offering were used to reduce amounts outstanding on our revolving credit facility and for general business purposes, including acquisitions.

**RESULTS OF OPERATIONS***Three Months Ended September 30, 2006, Compared to Three Months Ended September 30, 2005*

|                                                        | Three Months Ended September 30,<br>2006                      2005<br>(in thousands, except per share data) |            | Change      | % Change |   |
|--------------------------------------------------------|-------------------------------------------------------------------------------------------------------------|------------|-------------|----------|---|
| Rental income                                          | \$ 202,542                                                                                                  | \$ 182,894 | \$ 19,648   | 10.7     | % |
| Expenses:                                              |                                                                                                             |            |             |          |   |
| Operating expenses                                     | 80,219                                                                                                      | 69,173     | 11,046      | 16.0     | % |
| Depreciation and amortization                          | 41,064                                                                                                      | 34,490     | 6,574       | 19.1     | % |
| General and administrative                             | 8,513                                                                                                       | 9,102      | (589 )      | (6.5 )   | % |
| Total expenses                                         | 129,796                                                                                                     | 112,765    | 17,031      | 15.1     | % |
| Operating income                                       | 72,746                                                                                                      | 70,129     | 2,617       | 3.7      | % |
| Interest income                                        | 573                                                                                                         | 408        | 165         | 40.4     | % |
| Interest expense                                       | (43,169 )                                                                                                   | (35,628 )  | (7,541 )    | (21.2 )  | % |
| Loss on early extinguishment of debt                   |                                                                                                             | (168 )     | 168         | 100.0    | % |
| Equity in earnings of equity investments               |                                                                                                             | 3,494      | (3,494 )    | (100.0 ) | % |
| Income from continuing operations                      | 30,150                                                                                                      | 38,235     | (8,085 )    | (21.1 )  | % |
| Income (loss) from discontinued operations             | 32                                                                                                          | 62         | (30 )       | (48.4 )  | % |
| Gain on sale of properties                             | 1,172                                                                                                       |            | 1,172       | 100.0    | % |
| Net income                                             | 31,354                                                                                                      | 38,297     | (6,943 )    | (18.1 )  | % |
| Preferred distributions                                | (9,234 )                                                                                                    | (11,500 )  | 2,266       | 19.7     | % |
| Net income available for common shareholders           | \$ 22,120                                                                                                   | \$ 26,797  | \$ (4,677 ) | (17.5 )  | % |
| Weighted average common shares outstanding             | 209,992                                                                                                     | 201,459    | 8,533       | 4.2      | % |
| Income from continuing operations per share            | \$ 0.10                                                                                                     | \$ 0.13    | \$ (0.03 )  | (23.1 )  | % |
| Income (loss) from discontinued operations per share   | \$                                                                                                          | \$         | \$          |          | % |
| Net income available for common shareholders per share | \$ 0.11                                                                                                     | \$ 0.13    | \$ (0.02 )  | (15.4 )  | % |

*Rental income.* Rental income increased for the three months ended September 30, 2006, compared to the same period in 2005, primarily due to increases in rental income from our Oahu, HI, Austin, TX and Other Markets segments, offset by the decrease in rental income from our Philadelphia segment, all as described in Note 6 to our consolidated financial statements. Rental income for the Oahu, HI segment increased \$1.9 million, or 13%, primarily because of increases in weighted average rental rates for new leases and lease renewals signed during 2005 and 2006. Rental income for the Austin, TX segment increased \$1.1 million, or 12%, primarily due to an increase in occupancy in 2006. Rental income for the Other Markets segment increased \$18.1 million, or 23%, primarily because of the acquisition of 74 properties since June 2005, partially offset by approximately \$3 million of lease termination fees received during 2005. Rental income for the Metro Philadelphia, PA segment decreased \$2.0 million, or 6%, primarily due to a decline in occupancy during 2006. Rental income includes non cash straight line rent adjustments totaling \$7.8 million in 2006 and \$9.0 million in 2005 and amortization of acquired real estate leases and obligations totaling (\$2.4 million) in 2006 and (\$1.5 million) in 2005. Rental income also includes lease termination fees totaling \$50,000 in 2006 and \$3.1 million in 2005.

*Total expenses.* Total expenses increased for the three months ended September 30, 2006, compared to the same period in 2005, due to increases in operating expenses and depreciation and amortization expenses primarily related to the acquisition of properties in 2005 and 2006.

*Interest expense.* Interest expense increased for the three months ended September 30, 2006, compared to the three months ended September 30, 2005, reflecting an increase in average total debt outstanding which was used primarily to finance acquisitions in 2006 and 2005, and the increase in weighted average interest rates on our floating rate debt from 4.2% during the three months ended September 30, 2005, to 5.9% during the three months ended September 30, 2006.

*Equity in earnings of equity investments.* Equity in earnings of equity investments decreased in 2006 due to the sale of all of the common shares we owned in Senior Housing and Hospitality Properties in March 2006.

*Gain on sale of properties.* The gain on sale of properties in 2006 reflects the sale of four office properties located in Atlanta, GA for \$9.2 million.

*Income from continuing operations.* The decrease in income from continuing operations is due primarily to our sale of equity investments during the first quarter of 2006, and an increase during 2006 in interest expense due to the increase in average total debt outstanding and the increase in floating interest rates, offset by the acquisition of properties since June 2005.

*Net income and net income available for common shareholders.* The decrease in net income and net income available for common shareholders is due primarily to the sale of Senior Housing and Hospitality Properties common shares in 2006, and an increase during 2006 in interest expense due to an increase in average total debt outstanding, offset by property acquisitions since June 2005. Net income available for common shareholders is net income reduced by preferred distributions.

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## Nine Months Ended September 30, 2006, Compared to Nine Months Ended September 30, 2005

|                                                                      | Nine Months Ended September 30,<br>2006                      2005 |            | Change    | % Change |    |
|----------------------------------------------------------------------|-------------------------------------------------------------------|------------|-----------|----------|----|
|                                                                      | (in thousands, except per share data)                             |            |           |          |    |
| Rental income                                                        | \$ 590,058                                                        | \$ 523,262 | \$ 66,796 | 12.8     | %  |
| Expenses:                                                            |                                                                   |            |           |          |    |
| Operating expenses                                                   | 227,981                                                           | 196,014    | 31,967    | 16.3     | %  |
| Depreciation and amortization                                        | 119,109                                                           | 100,417    | 18,692    | 18.6     | %  |
| General and administrative                                           | 24,926                                                            | 23,430     | 1,496     | 6.4      | %  |
| Total expenses                                                       | 372,016                                                           | 319,861    | 52,155    | 16.3     | %  |
| Operating income                                                     | 218,042                                                           | 203,401    | 14,641    | 7.2      | %  |
| Interest income                                                      | 2,118                                                             | 1,289      | 829       | 64.3     | %  |
| Interest expense                                                     | (126,317 )                                                        | (105,967 ) | (20,350 ) | (19.2 )  | %) |
| Loss on early extinguishment of debt                                 | (1,659 )                                                          | (168 )     | (1,491 )  | (887.5 ) | %) |
| Equity in earnings of equity investments                             | 3,136                                                             | 9,940      | (6,804 )  | (68.5 )  | %) |
| Gain on sale of equity investments                                   | 116,287                                                           |            | 116,287   | 100.0    | %  |
| Gain on issuance of shares by equity investees                       |                                                                   | 4,708      | (4,708 )  | (100.0 ) | %) |
| Income from continuing operations                                    | 211,607                                                           | 113,203    | 98,404    | 86.9     | %  |
| (Loss) income from discontinued operations                           | (76 )                                                             | 483        | (559 )    | (115.7 ) | %) |
| Gain on sale of properties                                           | 1,172                                                             | 7,592      | (6,420 )  | (84.6 )  | %) |
| Net income                                                           | 212,703                                                           | 121,278    | 91,425    | 75.4     | %  |
| Preferred distributions                                              | (29,976 )                                                         | (34,500 )  | 4,524     | 13.1     | %  |
| Excess redemption price paid over carrying value of preferred shares | (6,914 )                                                          |            | (6,914 )  | (100.0 ) | %) |
| Net income available for common shareholders                         | \$ 175,813                                                        | \$ 86,778  | \$ 89,035 | 102.6    | %  |
| Weighted average common shares outstanding                           | 209,941                                                           | 193,778    | 16,163    | 8.3      | %  |
| Income from continuing operations per share                          | \$ 0.83                                                           | \$ 0.41    | \$ 0.42   | 102.4    | %  |
| (Loss) income from discontinued operations per share                 | \$                                                                | \$         | \$        |          | %  |
| Net income available for common shareholders per share               | \$ 0.84                                                           | \$ 0.45    | \$ 0.39   | 86.7     | %  |

*Rental income.* Rental income increased for the nine months ended September 30, 2006, compared to the same period in 2005, primarily due to increases in rental income from our Oahu, HI and Other Markets segments, offset by the decrease in rental income from the Metro Philadelphia, PA market, as described in Note 6 to our consolidated financial statements. Rental income for the Oahu, HI segment increased \$8.9 million, or 24%, primarily because of the acquisition of 44 properties in June 2005, and increases in weighted average rental rates for new leases and lease renewals signed during 2005 and 2006. Rental income for the Other Markets segment increased \$55.8 million, or 25%, primarily because of the acquisition of 76 properties since December 2004, partially offset by approximately \$3 million of lease termination fees received during 2005. Rental income for the Metro Philadelphia, PA segment decreased \$5.2 million, or 5%, primarily because of non-recurring rent recovery income received during 2005 and a decline in occupancy during 2006. Rental income includes non cash straight line rent adjustments totaling \$17.9 million in 2006 and \$21.3 million in 2005 and amortization of acquired real estate leases and obligations totaling (\$7.9 million) in 2006 and (\$5.0 million) in 2005. Rental income also includes lease termination fees totaling \$550,000 in 2006 and \$3.5 million in 2005.

*Total expenses.* Total expenses increased for the nine months ended September 30, 2006, compared to the same period in 2005, due to increases in operating expenses, depreciation and amortization and general and administrative expenses primarily related to the acquisition of properties in 2005 and 2006.

*Interest expense.* Interest expense increased for the nine months ended September 30, 2006, compared to the nine months ended September 30, 2005, reflecting an increase in average total debt outstanding which was used primarily to finance acquisitions in 2006 and 2005, and the increase in weighted average interest rates on our floating rate debt from 3.8% during the nine months ended September 30, 2005, to 5.7% during the nine months ended September 30, 2006.

*Loss on early extinguishment of debt.* The loss on early extinguishment of debt in 2006 relates to the write off of deferred financing fees associated with the repayment of our \$350 million term loan in March.

*Equity in earnings of equity investments.* Equity in earnings of equity investments decreased in 2006 due to our sale of all of the common shares we owned in Senior Housing and Hospitality Properties in March 2006.

*Gain on sale of equity investments.* The gain on sale of equity investments reflects the sale in March 2006 of all of the common shares we owned in Senior Housing and Hospitality Properties.

*Gain on issuance of shares by equity investees.* The gain on issuance of shares by equity investees reflects the issuance of common shares during 2005 by Hospitality Properties at prices above our per share carrying value.

*Gain on sale of properties.* The gain on sale of properties in 2006 reflects the sale of four office properties located in Atlanta, GA for \$9.2 million. The gain on sale of properties in the prior year reflects the sale of 237,000 square feet of industrial property located in the Metro Boston, MA area for \$20.5 million during the second quarter of 2005.

*Income from continuing operations.* The increase in income from continuing operations is due primarily to the gain on sale of the common shares we owned in Senior Housing and Hospitality Properties in 2006 and income from properties acquired since December 2004, offset by an increase during 2006 in interest expense due to the increase in average total debt outstanding and the increase in floating interest rates.

*Net income and net income available for common shareholders.* The increase in net income and net income available for common shareholders is due primarily to the gain on sale of Senior Housing and Hospitality Properties common shares in 2006 and property acquisitions since December 2004, offset by an increase in interest expense due to the increase in average total debt outstanding and the increase in floating interest rates. Net income available for common

Our principal source of funds for our operations is rents from tenants at our properties. Rents are generally received

shareholders is net income reduced by preferred distributions and the excess of the redemption price paid over the carrying value of our 9.875% series A preferred shares that we redeemed in March 2006.

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Our principal source of funds for our operations is rents from tenants at our properties. Rents are generally received

## **LIQUIDITY AND CAPITAL RESOURCES**

### ***Our Operating Liquidity and Resources***

Our principal sources of funds for current expenses and distributions to shareholders are rents from our properties. This flow of funds has historically been sufficient for us to pay our operating expenses, debt service and distributions. We believe that our operating cash flow will be sufficient to meet our operating expenses, debt service and distribution payments for the foreseeable future. Our future cash flows from operating activities will depend primarily upon the following factors:

- our ability to maintain or improve occupancies and effective rent rates at our continuously owned properties;
- our ability to restrain operating cost increases at our properties; and
- our ability to purchase new properties which produce positive cash flows from operations.

As discussed above, we believe that present leasing market conditions in some areas where our properties are located may result in modest increases in effective rents at some of our properties. Recent rises in fuel prices may cause our future operating costs to increase; however, the impact of these increases is expected to be partially offset by pass through operating cost increases to our tenants pursuant to lease terms. We generally do not engage in development activities (except on a build to suit basis), and we generally do not purchase turn around properties or properties which do not generate positive cash flows. Our future purchases of properties which generate positive cash flows can not be accurately projected because such purchases depend entirely upon available opportunities which come to our attention.

Cash flows provided by (used for) operating, investing and financing activities were \$186.9 million, (\$49.6) million and (\$123.3) million, respectively, for the nine months ended September 30, 2006, and \$180.6 million, (\$384.2) million and \$203.2 million, respectively, for the nine months ended September 30, 2005. Changes in all three categories between 2006 and 2005 are primarily related to property acquisitions and sales in 2006 and 2005, our sale of all of our Senior Housing and Hospitality Properties common shares in 2006, our repayments and issuances of debt obligations and redemption and issuance of preferred shares, and our issuance of common shares in 2005.

### ***Our Investment and Financing Liquidity and Resources***

In order to fund acquisitions and to accommodate cash needs that may result from timing differences between our receipt of rents and our desire or need to make distributions or pay operating or capital expenses, we maintain an unsecured revolving credit facility with a group of commercial banks. At September 30, 2006, there was \$310 million outstanding and \$440 million available on our revolving credit facility, and we had cash and cash equivalents of \$33.5 million. We expect to use cash balances, borrowings under our credit facility and net proceeds of offerings of equity or debt securities to fund future property acquisitions. In August 2006, we amended and extended the maturity of our revolving credit facility from April 2009 to August 2010, with an option to extend the facility an additional year, and we reduced the interest rate on borrowings from LIBOR plus 65 basis points to LIBOR plus 55 basis points. Certain covenants in the facility were also amended to reflect current market conditions.

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Our outstanding debt maturities and weighted average interest rates as of September 30, 2006, are as follows (dollars in thousands):

| Year                | Scheduled Principal Payments During Period |                                    |                                 | Total (1)    | Weighted<br>Average<br>Interest Rate |
|---------------------|--------------------------------------------|------------------------------------|---------------------------------|--------------|--------------------------------------|
|                     | Secured<br>Fixed Rate<br>Debt              | Unsecured<br>Floating<br>Rate Debt | Unsecured<br>Fixed<br>Rate Debt |              |                                      |
| 2006                | \$ 2,659                                   | \$                                 | \$                              | \$ 2,659     | 7.0 %                                |
| 2007                | 9,402                                      |                                    |                                 | 9,402        | 6.9 %                                |
| 2008                | 25,507                                     |                                    |                                 | 25,507       | 7.0 %                                |
| 2009                | 6,957                                      |                                    |                                 | 6,957        | 6.9 %                                |
| 2010                | 7,319                                      | 310,000                            | 50,000                          | 367,319      | 6.0 %                                |
| 2011                | 228,854                                    | 400,000                            |                                 | 628,854      | 6.1 %                                |
| 2012                | 29,990                                     |                                    | 200,000                         | 229,990      | 7.0 %                                |
| 2013                | 2,603                                      |                                    | 200,000                         | 202,603      | 6.5 %                                |
| 2014                | 14,505                                     |                                    | 250,000                         | 264,505      | 5.7 %                                |
| 2015                | 2,658                                      |                                    | 450,000                         | 452,658      | 6.0 %                                |
| 2016 and thereafter | 59,642                                     |                                    | 400,000                         | 459,642      | 6.4 %                                |
|                     | \$ 390,096                                 | \$ 710,000                         | \$ 1,550,000                    | \$ 2,650,096 | 6.2 %                                |

(1) Total debt outstanding as of September 30, 2006, net of unamortized premiums and discounts, is \$2,639,621.

When amounts are outstanding on our revolving credit facility and as the maturity dates of our revolving credit facility and term debts approach, we explore alternatives for the repayment of amounts due. Such alternatives usually include incurring additional term debt and issuing new equity securities. In 2006 we filed a shelf registration statement that allows for an indeterminate amount of securities to be issued by us. This shelf registration statement is effective for three years. An effective shelf registration statement allows us to issue public securities on an expedited basis, but it does not assure that there will be buyers for such securities. Although there can be no assurance that we will consummate any debt or equity offerings or other financings, we believe we will have access to various types of financing, including debt or equity offerings, with which to finance future acquisitions and to pay our debt and other obligations.

The completion and the costs of our future debt transactions will depend primarily upon market conditions and our credit ratings. We have no control over market conditions, but we expect the recent volatility in both short and long term debt costs to moderate for the next few months. Our credit ratings depend upon evaluations by credit rating agencies of our business practices and plans and, in particular, whether we appear to have the ability to maintain our earnings, to space our debt maturities and to balance our use of debt and equity capital so that our financial performance and leverage ratios afford us flexibility to withstand any reasonably anticipatable adverse changes. We intend to conduct our business activities in a manner which will continue to afford us reasonable access to capital for investment and financing activities.

During the first nine months of 2006 we purchased 46 office properties and one industrial property for \$306.9 million, excluding closing costs, and funded improvements to our owned properties totaling \$75.9 million. We funded all our 2006 acquisitions and improvements to our owned properties with cash on hand, by borrowing under our revolving credit facility and assuming \$20.6 million of mortgage debt. We sold four office properties with a total of approximately 68,000 square feet of space for gross proceeds of \$9.2 million (\$6.2 million after closing costs and deposits required to defease related mortgages). As of November 6, 2006, we have executed purchase agreements for two additional properties with an aggregate of 167,000 square feet of space and an aggregate purchase price of \$29.2 million. In addition, we have an executed purchase agreement for the sale of one property with approximately 33,000 square feet of space at a sale price of \$4.5 million. The acquisitions and sale of these properties are subject to various closing conditions customary in real estate transactions and no assurances can be given as to when or if we will purchase or sell these properties.

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As of September 30, 2006, we had outstanding agreements to purchase 15 properties containing approximately 1,652,000 square feet of space for \$120.5 million, plus closing costs. These properties were acquired in October 2006 using cash on hand, borrowings under our revolving credit facility and the assumption of debt.

During the three and nine months ended September 30, 2006 and 2005, cash expenditures made and capitalized for tenant improvements, leasing costs, building improvements and development and redevelopment activities were as follows (in thousands):

|                                                     | <b>Three Months Ended<br/>September 30,</b> |             | <b>Nine Months Ended<br/>September 30,</b> |             |
|-----------------------------------------------------|---------------------------------------------|-------------|--------------------------------------------|-------------|
|                                                     | <b>2006</b>                                 | <b>2005</b> | <b>2006</b>                                | <b>2005</b> |
| Tenant improvements                                 | \$ 13,032                                   | \$ 27,829   | \$ 42,841                                  | \$ 60,801   |
| Leasing costs                                       | 5,339                                       | 4,617       | 20,081                                     | 15,295      |
| Building improvements (1)                           | 5,615                                       | 7,044       | 17,484                                     | 13,849      |
| Development, redevelopment and other activities (2) | 8,114                                       | 4,674       | 15,621                                     | 10,606      |

(1) Building improvements generally include recurring expenditures that are necessary to maintain the value of our properties.

(2) Development, redevelopment and other activities generally include non-recurring expenditures that increase the value of our properties.

Commitments made for expenditures in connection with leasing space during the three months ended September 30, 2006, are as follows (in thousands, except as noted):

|                                                             | <b>Total</b> | <b>Renewals</b> | <b>New<br/>Leases</b> |
|-------------------------------------------------------------|--------------|-----------------|-----------------------|
| Square feet leased during the quarter                       | 1,408        | 766             | 642                   |
| Total commitments for tenant improvements and leasing costs | \$ 25,678    | \$ 5,205        | \$ 20,473             |
| Leasing costs per square foot (whole dollars)               | \$ 18.24     | \$ 6.80         | \$ 31.89              |
| Average lease term (years)                                  | 6.3          | 5.0             | 7.6                   |
| Leasing costs per square foot per year (whole dollars)      | \$ 2.89      | \$ 1.36         | \$ 4.20               |

In March 2006 we sold all 7.7 million of the common shares of beneficial interest we owned of Senior Housing, and all four million of the common shares of beneficial interest we owned of Hospitality Properties. Net sales proceeds of \$308.3 million were used to reduce amounts outstanding on our revolving credit facility. As a result of these sales, we recognized gains of \$116.3 million in 2006. We received cash distributions in 2006 before the sale of these shares totaling \$2.5 million from Senior Housing and \$2.9 million from Hospitality Properties.

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In February 2006 we issued six million series C cumulative redeemable preferred shares in a public offering for net proceeds of \$145.0 million. Each series C preferred share has a liquidation preference of \$25.00 and requires dividends of \$1.78125, 7 1/8% of the liquidation preference per annum, payable in equal quarterly payments. Our series C preferred shares are redeemable, at our option, for \$25.00 each plus accrued and unpaid dividends at any time on or after February 15, 2011. We applied the net proceeds from this offering to reduce amounts outstanding on our revolving credit facility. In March 2006 we issued \$400 million unsecured floating rate senior notes in a public offering raising net proceeds of approximately \$398.7 million. The notes bear interest at LIBOR plus a premium (6.0% at September 30, 2006), require quarterly interest payments and mature in March 2011. Net proceeds from this offering were used to reduce amounts outstanding under our revolving credit facility and for general business purposes. In March 2006 we redeemed all \$200 million of our 9.875% series A preferred shares and repaid our \$350 million term loan that was scheduled to mature in August 2009 by borrowing under our revolving credit facility.

In October 2006, we issued an aggregate of 15.2 million series D cumulative convertible preferred shares, including 2.0 million shares issued to cover over-allotments, in a public offering for net proceeds of approximately \$368.3 million. Each series D preferred share has a liquidation preference of \$25.00 and requires dividends of \$1.625, 6 1/2%, per annum, payable in equal quarterly payments. Our series D preferred shares are convertible, at the holder's option, into our common shares at an initial conversion rate of 1.9231 common shares per series D preferred share, which is equivalent to an initial conversion price of \$13.00 per common share. On or after November 20, 2011, if our common shares trade at or above the then applicable conversion price, we may, at our option, convert some or all of the series D preferred shares into common shares at the then applicable conversion rate. Net proceeds from this offering were used to reduce amounts outstanding on our revolving credit facility and for general business purposes, including acquisitions.

As of September 30, 2006, we have no commercial paper, derivatives, swaps, hedges, guarantees, joint ventures or off balance sheet arrangements. None of our debt documentation requires us to provide collateral security in the event of a ratings downgrade.

### ***Debt Covenants***

Our principal debt obligations at September 30, 2006, were our unsecured revolving credit facility and our \$2.0 billion of publicly issued unsecured term debt. Our publicly issued debt is governed by an indenture. Our public debt indenture and related supplements and our revolving credit facility agreement contain a number of financial ratio covenants which generally restrict our ability to incur debts, including debts secured by mortgages on our properties in excess of calculated amounts, require us to maintain a minimum net worth, restrict our ability to make distributions under certain circumstances and require us to maintain other ratios. At September 30, 2006, we were in compliance with all of our covenants under our indenture and related supplements and our revolving credit facility agreement.

In addition to our unsecured debt obligations, we have \$390.1 million of mortgage notes outstanding at September 30, 2006.

None of our indenture and related supplements, our revolving credit facility or our mortgage notes contain provisions for acceleration which could be triggered by our debt ratings. However, our senior debt rating is used to determine the interest rate and the fees payable under our revolving credit facility.

Our public debt indenture and related supplements contain cross default provisions to any other debts of \$20 million or more. Similarly, a default on our public debt indenture would be a default under our revolving credit facility.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

We are exposed to risks associated with market changes in interest rates. Our strategy to manage exposure to changes in interest rates is unchanged since December 31, 2005. Other than as described below, we do not foresee any significant changes in our exposure to fluctuations in interest rates or in how we manage this exposure in the near future.

Our unsecured revolving credit facility and \$400 million of our senior notes bear interest at floating rates and mature in August 2010 and March 2011, respectively. As of September 30, 2006, we had \$310 million outstanding and \$440 million available for drawing under our revolving credit facility. Repayments under our revolving credit facility may be made at any time without penalty. Repayments under our \$400 million floating rate senior notes may be made any time on or after September 16, 2006. We borrow in U.S. dollars and borrowings under our revolving credit facility and \$400 million of our senior notes require interest at LIBOR plus premiums. Accordingly, we are vulnerable to changes in U.S. dollar based short term rates, specifically LIBOR. Our exposure to fluctuations in floating interest rates will increase or decrease in the future with increases or decreases in the outstanding amount of our floating rate debt.

**Item 4. Controls and Procedures**

As of the end of the period covered by this report, our management carried out an evaluation, under the supervision and with the participation of our managing trustees, President and Chief Operating Officer and Treasurer and Chief Financial Officer of the effectiveness of our disclosure controls and procedures pursuant to Exchange Act Rules 13a-15 and 15d-15. Based upon that evaluation, our managing trustees, President and Chief Operating Officer and Treasurer and Chief Financial Officer concluded that our disclosure controls and procedures are effective.

There have been no changes in our internal control over financial reporting during the quarter ended September 30, 2006, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**FORWARD LOOKING STATEMENTS**

THIS QUARTERLY REPORT CONTAINS STATEMENTS WHICH CONSTITUTE FORWARD LOOKING STATEMENTS WITHIN THE MEANING OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995 AND OTHER FEDERAL SECURITIES LAWS. ALSO, WHENEVER WE USE WORDS SUCH AS BELIEVE , EXPECT , ANTICIPATE , INTEND , PLAN , ESTIMATE OR SIMILAR EXPRESSIONS, WE ARE MAKING FORWARD LOOKING STATEMENTS. THESE FORWARD LOOKING STATEMENTS ARE BASED UPON OUR PRESENT INTENT, BELIEFS OR EXPECTATIONS, BUT FORWARD LOOKING STATEMENTS ARE NOT GUARANTEED TO OCCUR AND MAY NOT OCCUR. ACTUAL RESULTS MAY DIFFER MATERIALLY FROM THOSE CONTAINED IN OR IMPLIED BY OUR FORWARD LOOKING STATEMENTS AS A RESULT OF VARIOUS FACTORS.

IMPORTANT FACTORS THAT COULD CAUSE ACTUAL RESULTS TO DIFFER MATERIALLY FROM THOSE IN OUR FORWARD LOOKING STATEMENTS ARE:

- CHANGES IN THE ECONOMY AND THE CAPITAL MARKETS,
- COMPETITION WITHIN THE REAL ESTATE INDUSTRY OR THOSE INDUSTRIES IN WHICH OUR TENANTS OPERATE, AND
- CHANGES IN FEDERAL, STATE AND LOCAL LEGISLATION.

FOR EXAMPLE:

- SOME OF OUR TENANTS MAY NOT RENEW EXPIRING LEASES, AND WE MAY BE UNABLE TO LOCATE NEW TENANTS TO MAINTAIN THE HISTORICAL OCCUPANCY RATES OF OUR PROPERTIES,
- RENTS THAT WE CAN CHARGE AT OUR PROPERTIES MAY DECLINE,
- OUR TENANTS MAY EXPERIENCE LOSSES AND BECOME UNABLE TO PAY OUR RENTS,
- CONTINGENCIES IN OUR COMMITTED ACQUISITIONS AND SALES MAY CAUSE THESE TRANSACTIONS NOT TO OCCUR OR TO BE DELAYED,
- WE MAY BE UNABLE TO IDENTIFY PROPERTIES WHICH WE WANT TO BUY OR TO NEGOTIATE ACCEPTABLE PURCHASE PRICES, AND

OTHER RISKS MAY ADVERSELY IMPACT US, AS DESCRIBED MORE FULLY IN OUR ANNUAL REPORT ON FORM 10-K FOR THE YEAR ENDED DECEMBER 31, 2005, UNDER ITEM 1A. RISK FACTORS AND LATER IN THIS FORM 10-Q UNDER ITEM 1A. RISK FACTORS .

YOU SHOULD NOT PLACE UNDUE RELIANCE UPON FORWARD LOOKING STATEMENTS.

EXCEPT AS REQUIRED BY LAW, WE UNDERTAKE NO OBLIGATION TO UPDATE OR REVISE ANY FORWARD LOOKING STATEMENTS AS A RESULT OF NEW INFORMATION, FUTURE EVENTS OR OTHERWISE.

**STATEMENT CONCERNING LIMITED LIABILITY**

**THE AMENDED AND RESTATED DECLARATION OF TRUST ESTABLISHING HRPT PROPERTIES TRUST, DATED JULY 1, 1994, A COPY OF WHICH, TOGETHER WITH ALL AMENDMENTS AND SUPPLEMENTS THERETO, AS DULY FILED IN THE OFFICE OF THE STATE DEPARTMENT OF ASSESSMENTS AND TAXATION OF MARYLAND, PROVIDES THAT THE NAME HRPT PROPERTIES TRUST REFERS TO THE TRUSTEES UNDER THE DECLARATION OF TRUST, AS SO AMENDED AND SUPPLEMENTED, COLLECTIVELY AS TRUSTEES, BUT NOT INDIVIDUALLY OR PERSONALLY, AND THAT NO TRUSTEE, OFFICER, SHAREHOLDER, EMPLOYEE OR AGENT OF HRPT PROPERTIES TRUST SHALL BE HELD TO ANY PERSONAL LIABILITY, JOINTLY OR SEVERALLY, FOR ANY OBLIGATION OF, OR CLAIM AGAINST, HRPT PROPERTIES TRUST. ALL PERSONS DEALING WITH HRPT PROPERTIES TRUST IN ANY WAY SHALL LOOK ONLY TO THE ASSETS OF HRPT PROPERTIES TRUST FOR THE PAYMENT OF ANY SUM OR THE PERFORMANCE OF ANY OBLIGATION.**

**Part II. Other Information**

**Item 1A. Risk Factors**

For a discussion of risk factors affecting us, see **Risk Factors** in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2005. As discussed elsewhere in this Quarterly Report, in October, 2006, we issued 15.2 million series D cumulative convertible preferred shares, or Series D Preferred Shares, in a public offering. In that connection, certain additional risks should be considered, including the following:

**Conversion rights of Series D Preferred Shares may be detrimental to holders of our common shares.**

Our Series D Preferred Shares are convertible into our common shares in various circumstances. The initial conversion rate (equivalent to an initial conversion price of \$13.00 per common share) is subject to adjustment upon the occurrence of various events, including if we make quarterly cash distributions on common shares in excess of \$0.21 per share (subject to adjustment). If a holder elects to convert Series D Preferred Shares in connection with a fundamental change that occurs on or prior to November 15, 2011, the conversion rate may be increased by a premium based on the market price of our common shares at the time. Fundamental changes include certain transactions constituting a change of control, our liquidation or dissolution and certain related events, or the circumstance in which our common shares are no longer traded on any national securities exchange or on an established over the counter market in the United States.

Holders have a special right to convert Series D Preferred Shares in connection with a fundamental change into a number of our common shares per \$25.00 liquidation preference equal to such liquidation preference, plus accrued and unpaid distributions, divided by 98% of the market price of our common shares at the time. We have the right in those circumstance to repurchase Series D Preferred Shares for cash in lieu of conversion at a repurchase price equal to 100% of the liquidation preference plus accrued and unpaid distributions. However, we may not have sufficient financial resources at the time of the conversion to pay the repurchase price and our then existing indebtedness could restrict or prohibit the repurchase.

The conversion of some or all of the Series D Preferred Shares will dilute the ownership interests of existing shareholders. Any sales in the public market of the common shares issuable upon such conversion could adversely affect prevailing market prices of our common shares. In addition, the existence of the Series D Preferred Shares may encourage short selling by market participants because the conversion of the Series D Preferred Shares could depress the price of our common shares. The conversion rights may make more difficult or discourage a party from taking over our company and removing incumbent management and may discourage or impede transactions that might otherwise be in the interests of our common shareholders.

## Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

On September 20, 2006, we granted 51,050 common shares pursuant to our Incentive Share Award Plan to our officers and certain employees of our manager, Reit Management & Research LLC, valued at \$11.88 per common share, the closing price of our common shares on the NYSE on September 20, 2006. The grants were made pursuant to the exemption from registration contained in Section 4(2) of the Securities Act of 1933, as amended.

## Item 5. Other Information

The following supplementary federal income tax considerations relating to the acquisition, ownership and disposition of our shares supplement and update the more detailed description of these matters in the section of our Annual Report on Form 10-K for the year ended December 31, 2005, or 2005 Annual Report, captioned "Federal Income Tax Considerations", which we incorporate in this Form 10-Q by reference. Sullivan & Worcester LLP, Boston, Massachusetts, has rendered a legal opinion that the discussion in the section of our 2005 Annual Report captioned

"Federal Income Tax Considerations", as supplemented by the discussion in this section, is accurate in all material respects and fairly summarizes the federal income tax issues discussed in those sections, and the opinions of counsel referred to in those sections represent Sullivan & Worcester LLP's opinions on those subjects. Specifically, subject to qualifications and assumptions contained in its opinion, in our 2005 Annual Report and in this section, Sullivan & Worcester LLP has given opinions to the effect that we have been organized and have qualified as a REIT under the Internal Revenue Code of 1986, as amended, or IRC, for each taxable year commencing with our taxable year ending December 31, 1987, and that our current investments and plan of operation will enable us to continue to meet the requirements for qualification and taxation as a REIT under the IRC. These opinions are conditioned upon the assumption that our leases and other contracts, our charter and bylaws, and all other legal documents to which we are or have been a party, have been and will be complied with by all parties to these documents, upon the accuracy and completeness of the factual matters described in our 2005 Annual Report and in this Form 10-Q, and upon representations that we have made. The opinions of Sullivan & Worcester LLP are based on the law as it exists today, but the law may change in the future, possibly with retroactive effect. Also, an opinion of counsel is not binding on the Internal Revenue Service, or IRS, or the courts, and the IRS or a court could take a position different from that expressed by counsel.

The IRC imposes upon us various REIT qualification tests discussed more fully in our 2005 Annual Report. While we believe that we have operated and will operate in a manner to satisfy these various REIT qualification tests, counsel has not reviewed and will not review our compliance with these tests on a continuing basis. Our actual qualification as a REIT will depend upon our ability to meet, and our meeting, through actual annual operating results and distributions, the various REIT qualification tests imposed under the IRC.

As long as we qualify as a REIT for federal income tax purposes, a distribution to our shareholders (including any cash received in exchange for our Series D Preferred Shares that is treated as a distribution and any constructive distribution, each as described below) that we do not designate as a capital gain dividend will be treated as an ordinary income dividend to the extent of our current or accumulated earnings and profits. Our current or accumulated earnings and profits will generally be allocated first to distributions with respect to the preferred shares we have outstanding, and thereafter to distributions with respect to our common shares. Distributions made out of our current or accumulated earnings and profits that we properly designate as capital gain dividends will be taxed as long-term capital gains, as discussed in our 2005 Annual Report, to the extent they do not exceed our actual net capital gain for the taxable year.

As discussed in our 2005 Annual Report, for noncorporate U.S. shareholders and certain noncorporate non-U.S. shareholders, long-term capital gains are generally taxed at maximum rates of 15% or 25% through 2010, depending upon the type of property disposed of and the previously claimed depreciation with respect to this property. If for any taxable year we designate capital gain dividends for any shareholders, then the portion of the capital gain dividends we designate will be allocated to the holders of a particular class of shares on a percentage basis equal to the ratio of the amount of the total dividends paid or made available for the year to the holders of that class of shares to the total dividends paid or made available for the year to holders of all classes of our shares. We will similarly designate the portion of any capital gain dividend that is to be taxed to eligible noncorporate shareholders at the maximum rates of 15% or 25% so that the designations will be proportionate among all classes of our shares.

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The conversion formula of our Series D Preferred Shares may be adjusted under a number of circumstances; adjustments may include changes in the type or amount of consideration a shareholder receives upon conversion. Section 305 of the IRC treats some of these adjustments as constructive taxable distributions. In general, a shareholder that holds our Series D Preferred Shares would be deemed to receive a constructive distribution if the conversion price is adjusted for a taxable distribution to the holders of common shares. Constructive distributions are taxed as distributions described above. Such a shareholder's adjusted tax basis in Series D Preferred Shares would be increased by constructive distributions that are taxable as dividends or gain, and would be unaffected by constructive distributions that were nontaxable returns of capital. Conversely, a failure to appropriately adjust the conversion price of the Series D Preferred Shares could result in a constructive distribution to shareholders that hold our common shares, which would be taxable to them in a similar manner as actual distributions. A shareholder may also receive a constructive distribution if a conversion of its Series D Preferred Shares is accompanied by a change in the conversion formula.

If a shareholder actually or constructively owns none or a small percentage of our common shares, and such shareholder surrenders its Series D Preferred Shares to us in redemption for cash only, then the repurchase of the Series D Preferred Shares is likely to qualify for sale or exchange treatment because the repurchase would not be essentially equivalent to a dividend as defined by the IRC. More specifically, a cash repurchase of Series D Preferred Shares will be treated under Section 302 of the IRC as a distribution, and hence taxable as a dividend to the extent of our allocable current or accumulated earnings and profits, as discussed above, unless the repurchase satisfies one of the tests set forth in Section 302(b) of the IRC and is therefore treated as a sale or exchange of the repurchased shares. The repurchase will be treated as a sale or exchange if it (1) is substantially disproportionate with respect to the surrendering shareholder's ownership in us, (2) results in a complete termination of the surrendering shareholder's common and preferred share interest in us, or (3) is not essentially equivalent to a dividend with respect to the surrendering shareholder, all within the meaning of Section 302(b) of the IRC. In determining whether any of these tests have been met, a shareholder must generally take into account our common and preferred shares considered to be owned by such shareholder by reason of constructive ownership rules set forth in the IRC, as well as our common and preferred shares actually owned by such shareholder. Because the determination as to whether a shareholder will satisfy any of the tests of Section 302(b) of the IRC depends upon the facts and circumstances at the time that the Series D Preferred Shares are repurchased, you are encouraged to consult your own tax advisor to determine your particular tax treatment.

In contrast to the discussion above, if a shareholder receives a number of our common shares as a result of a conversion or repurchase of Series D Preferred Shares, then the transaction will be treated as a recapitalization. As such, the shareholder would recognize income or gain only to the extent of the lesser of (1) the excess, if any, of the value of the cash and common shares received over such shareholder's adjusted tax basis in its Series D Preferred Shares surrendered or (2) the cash received. Any cash a shareholder receives, up to the amount of income or gain recognized, would generally be characterized as a dividend to the extent that a surrender of Series D Preferred Shares to us for cash only would be taxable as a dividend, taking into account the surrendering shareholder's continuing actual or constructive ownership interest in our shares, if any, as discussed above, and the balance of the recognized amount, if any, will be gain. If, in addition to common shares, upon conversion or repurchase a shareholder receives rights or warrants to acquire our common shares or other of our securities, then the receipt of the rights or warrants may be taxable, and we encourage you to consult your tax advisor as to the consequences of the receipt of rights or warrants upon conversion. A shareholder's basis in its common shares received would be equal to the basis for the Series D Preferred Shares surrendered less any cash received plus any income or gain recognized. A shareholder's holding period in the common shares received would be the same as the holding period for the Series D Preferred Shares surrendered. Non-U.S. shareholders may not be eligible for the foregoing partial nonrecognition rules and may instead be subject to special rules discussed below.

A shareholder generally will not recognize any income, gain or loss upon conversion of Series D Preferred Shares into common shares except with respect to cash, if any, received in lieu of a fractional common share. If, in addition to common shares, upon conversion a shareholder receives rights or warrants to acquire our common shares or other of our securities, then the receipt of the rights or warrants may be taxable, and we encourage you to consult your tax advisor as to the consequences of the receipt of rights or warrants upon conversion. A shareholder's basis in its common shares received would be equal to the basis for the Series D Preferred Shares surrendered less any basis allocable to any fractional share. A shareholder's holding period in the common shares received would be the same as the holding period for the Series D Preferred Shares surrendered. Any cash received in lieu of a fractional common share upon conversion will be treated as a

payment in exchange for the fractional common share. Accordingly, your receipt of cash in lieu of a fractional share generally will result in capital gain or loss, measured by the difference between the cash received for the fractional share and the adjusted tax basis attributable to the fractional share. Non-U.S. shareholders may not be eligible for the foregoing rules and may instead be subject to special rules discussed below.

As discussed more fully in our 2005 Annual Report, nonrecognition treatment may not apply at all, and a non-U.S. shareholder may be subject to federal income tax, increased United States tax filing requirements, and possibly a branch profits tax, in respect of all the gain realized on the sale, repurchase or conversion of our Series D Preferred Shares, if those shares constitute United States real property interests under Section 897 of the IRC and related Treasury regulations. The Series D Preferred Shares will not constitute such United States real property interests if we are a domestically controlled REIT. A domestically controlled REIT is a REIT in which at all times during the preceding five-year period less than 50% in value of its shares is held directly or indirectly by foreign persons. We believe that we are and will be a domestically controlled REIT and thus a non-U.S. shareholder's gain on sale, repurchase or conversion of our Series D Preferred Shares will not be subject to United States federal income taxation. However, because our shares are publicly traded, we can provide no assurance that we will be a domestically controlled REIT. If we are not a domestically controlled REIT, but the Series D Preferred Shares are regularly traded, as defined by applicable Treasury regulations, on an established securities market like the NYSE, then a non-U.S. shareholder's gain on sale, repurchase or conversion of our Series D Preferred Shares will not be subject to United States federal income taxation as a sale of a United States real property interest, if the non-U.S. shareholder has at all times during the preceding five years owned 5% or less by value of that class of shares. In this regard, because the Series D Preferred Shares of others may be repurchased and are convertible, a non-U.S. shareholder's percentage interest in the Series D Preferred Shares may increase even if it acquires no additional Series D Preferred Shares.

Effective generally from and after 2006, a special wash sale rule applies to a non-U.S. shareholder who owns any class of our shares if (1) the shareholder owns more than 5% of that class of shares at any time during the one-year period ending on the date of the distribution described below, or (2) that class of our shares is not, within the meaning of applicable Treasury Regulations, regularly traded on a domestic established securities market such as the NYSE. Although there can be no assurance in this regard, we believe that our common shares and each class of our preferred shares has been and will remain regularly traded on a domestic established securities market within the meaning of applicable Treasury regulations, all as described in our 2005 Annual Report. We thus anticipate this new wash sale rule to apply, if at all, only to a non-U.S. shareholder that owns more than 5% of either our common shares or any class of our preferred shares. Such a non-U.S. shareholder will be treated as having made a wash sale of our shares if it (1) disposes of an interest in our shares during the 30 days preceding the ex-dividend date of a distribution by us that, but for such disposition, would have been treated by the non-U.S. shareholder in whole or in part as gain from the sale or exchange of a United States real property interest, and then (2) acquires or enters into a contract to acquire a substantially identical interest in our shares, either actually or constructively through a related party, during the 61-day period beginning 30 days prior to the ex-dividend date. In the event of such a wash sale, the non-U.S. shareholder will have gain from the sale or exchange of a United States real property interest in an amount equal to the portion of the distribution that, but for the wash sale, would have been a gain from the sale or exchange of a United States real property interest. As described in our 2005 Annual Report, a non-U.S. shareholder's gain from the sale or exchange of a United States real property interest can trigger increased United States taxes, such as the branch profits tax applicable to non-U.S. corporations, and increased United States tax filing requirements.

As described in our 2005 Annual Report, shareholders may be subject to backup or other federal income tax withholding. If a shareholder is subject to backup or other federal income tax withholding, then a withholding agent may be required to withhold the appropriate amount with respect to a constructive distribution even though there is no related receipt of cash from which to satisfy the withholding obligation. To satisfy this withholding obligation, the withholding agent may reduce to cash for remittance to the IRS a sufficient portion of such shareholder's shares or other property. A shareholder may be responsible for brokerage commissions and other costs relating to the generation of sufficient cash to remit to the IRS.

**Item 6. Exhibits**

- 3.1 Articles Supplementary relating to the 6 ½% Series D Cumulative Convertible Preferred Shares. *(incorporated by reference to the Company's Current Report on Form 8-K dated October 10, 2006)*
- 4.1 Form of temporary 6½% Series D Cumulative Convertible Preferred Share Certificate. *(incorporated by reference to the Company's Current Report on Form 8-K dated October 5, 2006)*
- 8.1 Opinion of Sullivan & Worcester LLP as to certain tax matters. *(filed herewith)*
- 10.1 First Amendment to Amended and Restated Credit Agreement, dated as of August 22, 2006, among HRPT Properties Trust, Wachovia Bank, National Association, as Administrative Agent, and the additional agents, arrangers and financial institutions signatory thereto. *(incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K dated August 22, 2006)*
- 12.1 Computation of Ratio of Earnings to Fixed Charges. *(filed herewith)*
- 12.2 Computation of Ratio of Earnings to Combined Fixed Charges and Preferred Distributions. *(filed herewith)*
- 31.1 Rule 13a-14(a) Certification. *(filed herewith)*
- 31.2 Rule 13a-14(a) Certification. *(filed herewith)*
- 31.3 Rule 13a-14(a) Certification. *(filed herewith)*
- 31.4 Rule 13a-14(a) Certification. *(filed herewith)*
- 32.1 Section 1350 Certification. *(furnished herewith)*
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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.

HRPT PROPERTIES TRUST

By: /s/ John A. Mannix  
John A. Mannix  
President and Chief Operating Officer  
Dated: November 8, 2006

By: /s/ John C. Popeo  
John C. Popeo  
Treasurer and Chief Financial Officer  
(principal financial and accounting officer)  
Dated: November 8, 2006