



# Duke

REALTY CORPORATION

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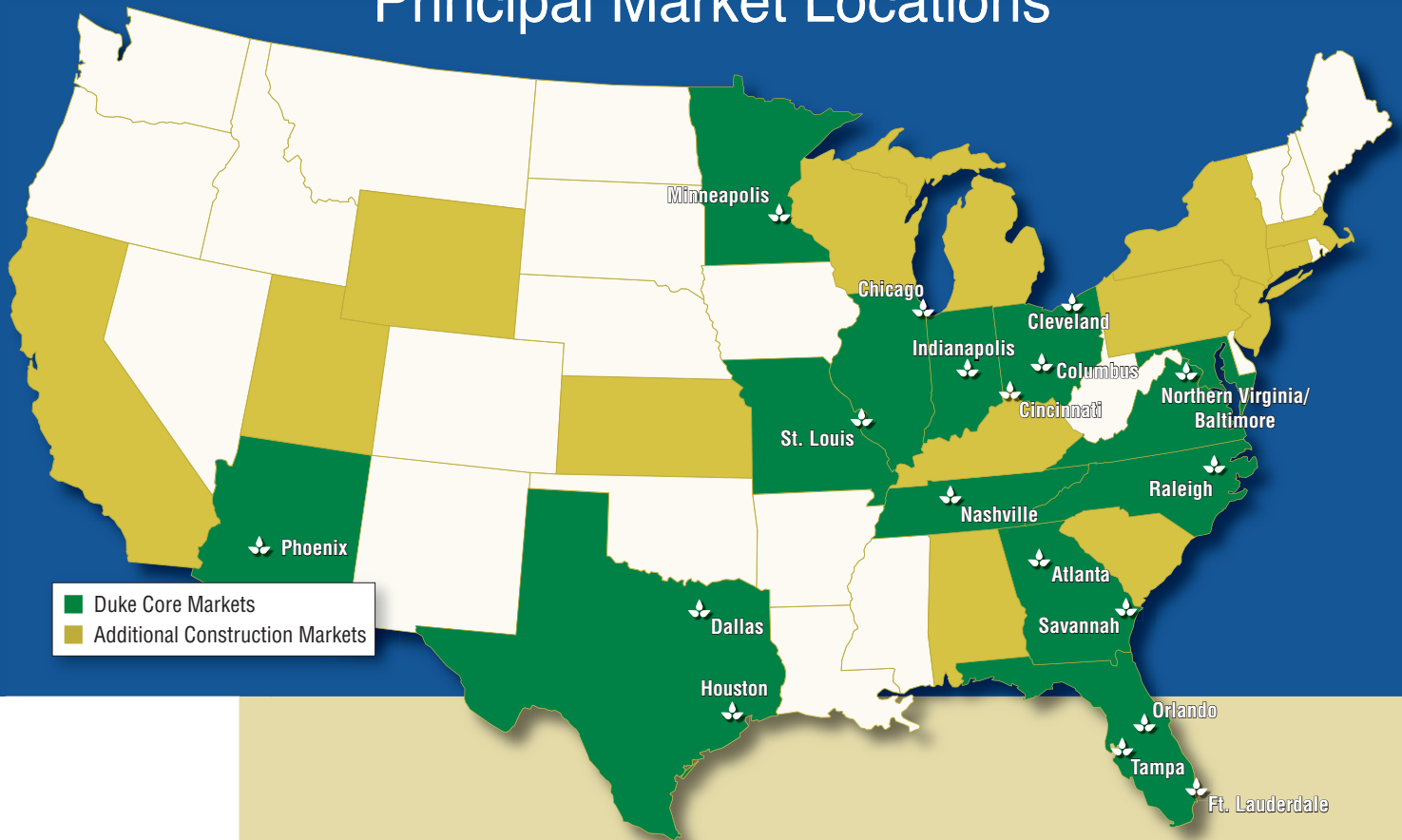
2005 ANNUAL REPORT



TWO HIGHLAND OAKS



## Principal Market Locations



## Corporate Profile

**DUKE REALTY CORPORATION** specializes in the ownership, construction, development, leasing and management of office, industrial, medical office and retail real estate. It is the largest publicly-traded, vertically integrated multi-product type real estate company in the United States. Duke's properties encompass more than 105 million rentable square feet that are leased by approximately 3,500 tenants, and 4,800 acres of undeveloped land that can support an additional 69 million square feet of development. Duke provides a full range of services in-house, backs them with more than 30 years experience, and delivers valuable real estate solutions to satisfied customers across the nation.

Duke common stock is listed on the New York Stock Exchange under the symbol: DRE. Approximately 60 percent of its outstanding common stock is owned by institutions, and the balance by approximately 120,000 individual investors.

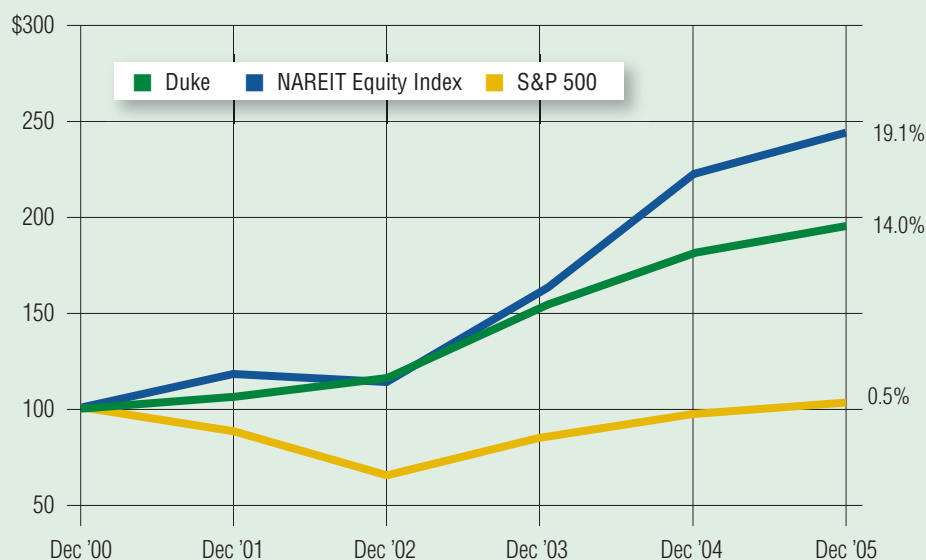


# Financial Highlights

(in thousands, except per share amounts)

	2005	2004	2003
<b>Operations</b>			
Total revenues from continuing operations	\$ 788,124	\$ 711,958	\$ 643,859
Net income available for common shareholders	309,183	151,279	161,911
Funds from operations — diluted	373,903	387,258	382,237
<b>Per share:</b>			
Diluted net income	\$ 2.17	\$ 1.06	\$ 1.19
Diluted FFO	2.40	2.47	2.45
Dividends paid	1.87	1.85	1.83
FFO Payout Ratio	78.1%	75.1%	74.9%
<b>At year-end</b>			
Total assets	\$ 5,647,560	\$ 5,896,643	\$ 5,561,249
Total shareholders' equity	2,452,798	2,825,869	2,666,749
<b>Senior Unsecured Debt Ratings</b>			
Standards & Poor's	BBB+	BBB+	BBB+
Moody's	Baa1	Baa1	Baa1
Fitch	BBB+	BBB+	BBB+

## Total Return to Shareholders\*



\* Total annualized return

## Fast Facts

Since Duke's public offering in 1993 at \$11.88 per share, its cumulative cash dividends have totaled \$17.49, or 47 percent more than the offering price.

A \$100 common stock investment in Duke Realty at its 1993 public offering price has increased in value to more than \$630, including the reinvestment of all dividends paid.

Duke's current annual dividend is \$1.88 per share, an increase of 109 percent since its 1993 public offering. The dividend has been increased for 12 consecutive years.

### About the cover

Highland Oaks in Tampa, FL. Highland Oaks is a six-building, 540,000 square foot office complex in suburban Tampa. Computer Associates is a major tenant in the park.





Dennis D. Oklak  
Chairman and Chief Executive Officer

## Report to Shareholders

We are extremely pleased with our performance in 2005. We accomplished the goals we set for ourselves at the beginning of the year: completing the large industrial portfolio sale; doubling our development pipeline; beginning our geographic expansion; and strengthening our balance sheet. We are confident that our achievements in 2005 will provide us with earnings growth momentum in 2006 and beyond.

As a result, even though our stock price reached a recent high of \$36.85 per share, we believe it is only now beginning to reflect the earnings potential of our much younger and more diversified real estate portfolio.

### Industrial Portfolio Sale

Last year we sold 212 of our older and more capital-intensive light industrial properties and received proceeds of approximately \$1 billion.

The average age of these properties was more than 14.5 years with capital expenditures exceeding \$1.46

per square foot. Today our remaining industrial portfolio averages less than 10 years old with capital expenditures at \$0.59 per square foot. By disposing of our more management-intensive projects, our development, leasing and property management teams are able to focus on newer, more higher-yielding projects.

### Acquisitions and New Developments

We utilized the proceeds from property dispositions to pursue acquisition and development opportunities that will provide long-term value creation for the Company. Our most notable acquisition in 2005 was the \$257 million purchase of a 1.4 million square foot suburban office portfolio near O'Hare International Airport. Even more significant to our long-term growth, our development starts last year exceeded the dollar value of all the development starts of the previous three years combined — \$704 million in 2005 compared

with \$599 million during the previous three years. We believe that our development expertise, combined with increasing demand in many of our markets, provides us with a great opportunity to develop buildings that will create significant value for our shareholders as these projects are placed in service over the next two years.

### Leasing

Leasing was especially strong in 2005. We had the highest quarterly leasing activity in the history of the Company in the fourth quarter, signing nearly 9.7 million square feet. This was by far the most leasing activity we've had since the first quarter of 2000, net absorbing nearly 4.5 million square feet in the existing portfolio.

During 2005, our in-service portfolio occupancy increased to 92.5 percent, the highest since the end of the first quarter of 2001. Our 63 million square foot in-service bulk industrial portfolio was 94.1 percent leased at year-end 2005, a 63 basis point improvement during the year. We also made great progress on the suburban office side, increasing the occupancy on our nearly 30 million square foot in-service portfolio to 89.1 percent, a 208 basis point increase for the year.

### Financial Performance

Net income available for common shareholders for 2005 totaled \$309 million, or \$2.17 per share on a diluted basis, compared with \$151 million, or \$1.06 per share for 2004. Diluted funds from operations (FFO) totaled \$2.40 per share for 2005 compared to \$2.47 per share in 2004. As a result of the industrial portfolio sale, FFO per share was diluted by \$0.07 in the fourth quarter 2005. We will begin to reap the



benefits as we redeploy the proceeds into new developments and acquisitions.

### Debt Reduction

The sale of our older industrial properties provided us with approximately \$955 million in additional cash last year. This allowed us to pay a special dividend of \$1.05 per share to our common shareholders on December 15, 2005 (an outlay of approximately \$157 million). The remaining proceeds were used to pay off a \$400 million term loan and to reduce the amount outstanding on our unsecured line of credit. We also repurchased nearly \$300 million of our common stock, representing more than 9 million shares. We are authorized to repurchase up to \$750 million of stock; however, we intend to utilize this program only as we believe the share price warrants.

### The Year Ahead

Looking to 2006, we will continue to transition the Company for future growth. We will reduce our property dispositions, as we are very pleased with the composition and quality of our existing portfolio. Continuing to expand our development pipeline, we have set a development goal in excess of \$800 million for 2006. We anticipate that a significant portion of this new development will be projects generated by our National Development Group, including medical office and retail projects. A majority of the remaining portion will come from our existing markets, with a modest amount of development expected to occur in our new markets.

Duke will pursue additional new market opportunities. It is our intent to acquire prime land positions in both Houston and Phoenix and

commence bulk warehouse development by the end of this year. In early 2006, we acquired 5.1 million square feet of bulk industrial properties at the Port of Savannah, Georgia, and 184 acres at the Port of Baltimore, Maryland. We will look for opportunities near other major ports and capitalize on the rapidly growing intermodal industry. We also obtained a 2.9 million square foot office and industrial portfolio in Northern Virginia through our acquisition of the Mark Winkler Company commercial division. Lastly, we will maintain a strong balance sheet, while moderately increasing our leverage.

### Outlook

We are confident that the strategic moves we made in 2005 will provide us with earnings growth momentum in 2006 and beyond. Our development pipeline is robust and we are excited about our new market opportunities. Duke is focused on growth in FFO per share and return on shareholders' equity, and we plan to achieve that growth through focusing on new development in our existing markets, expanding operations into new markets and increasing our fee income as we build our fund and joint venture business.

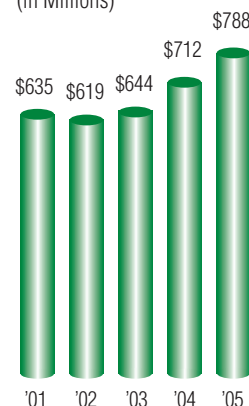
We acknowledge the support of our Board of Directors, Shareholders and Associates, and the very significant role that they play in making us the successful Company that we are today. Thank you for your continued confidence in Duke Realty Corporation.



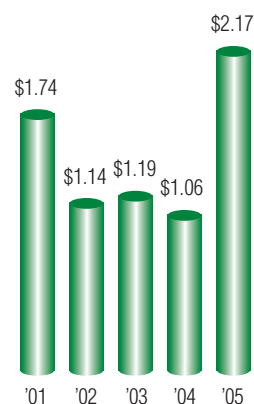
Dennis D. Oklak  
Chairman & CEO

Indianapolis, IN  
March 3, 2006

TOTAL REVENUE FROM  
CONTINUING OPERATIONS  
(in Millions)



DILUTED NET INCOME  
PER COMMON SHARE



DILUTED FUNDS FROM OPERATIONS  
(FFO) PER COMMON SHARE









◀ Duke Bridges Office Park in Frisco, TX. Duke entered the suburban Dallas office market in March with this 158,000 square foot speculative office building and by November, the building was substantially leased to T-Mobile. During 2006, Duke will develop its second office building in this park which will be fully leased to the same tenant.

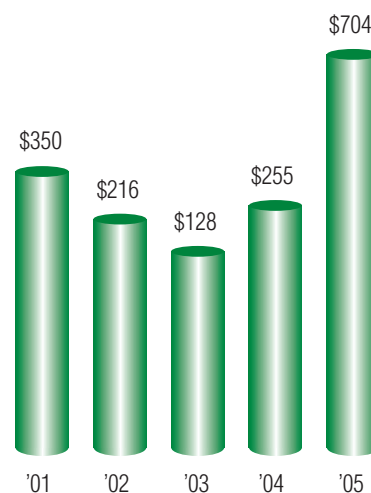
We accelerated our momentum in 2005. We more than doubled the size of our development pipeline, completed the sale of more than 14 million square feet of older properties, continued our geographic expansion, and further strengthened our balance sheet.

#### Development Starts Grow Rapidly

We greatly exceeded our goal to double our development starts over those of 2004. Last year starts were a record \$704 million, which was 18 percent greater than all development started in 2002, 2003, and 2004, combined. In 2006, new starts are expected to exceed those of 2005, fueling a growth engine that is building momentum and additional earnings power for Duke.

We are developing projects at record levels. In many instances, we have the projects substantially leased prior to completion. For example, by year-end 2005, 2003 starts were 100 percent leased; 2004 starts were 91 percent leased; and 2005 starts were already 42 percent pre-leased.

Development Starts — 2001-2005  
\$ in Millions







▲ Centre Pointe IV in Cincinnati, OH. Following our successful acquisition of the Centre Pointe I, II and III office buildings, Duke began this speculative office project. This building opened in November 2005 and is currently 91 percent leased.



▲ St. Vincent Medical Office Building in Carmel, IN. Buildings of this type are presently in high demand. At year-end 2005, Duke had six similar buildings under construction across the country totaling approximately \$91 million.



Overall, the past year's development starts were comprised of 50 percent office, 35 percent industrial and 15 percent medical office and retail. Major developments last year included:

On the industrial side, we completed a 140,000 square foot, build-to-suit industrial project near the Dallas airport and fully leased it to Chase for 12 years. In Atlanta, we began a 300,000 square foot, build-to-suit warehouse for Hartsfield Warehouse Company, Inc. We finished a 273,000 square foot property in Cincinnati, 46 percent of which was leased to Scholastic Books and was fully leased by year-end.

With regard to office development, we constructed Centre Pointe IV, a 135,000 square foot office building in Cincinnati, which was completed late last year and is 91 percent leased. We began two office buildings totaling 360,000 square feet in Raleigh, North Carolina for Lenovo USA, with plans for a third building within the next two years. And in Frisco, Texas, a fast-growing suburb north of Dallas, T-Mobile has leased 66 percent of a 158,000 square foot speculative project that is nearing completion, and will also take 100 percent of a second, 126,000 square foot building to be completed mid-year 2006.

### Success of Specialty Healthcare Projects

In December 2004, Duke began a joint venture with Bremner Healthcare Real Estate, a developer experienced



in medical office buildings primarily for hospitals, doctors and medical support groups, as well as a variety of other healthcare projects.

Healthcare facilities offer certain advantages. Generally, the customer's credit standing is excellent; occupancy reaches 100 percent quickly; and leases are long-term. Presently, demand is quite high, and the number of commercial builders skilled in this type of construction is substantially less than those in general office construction.

▲ Saks, Chicago, IL. Duke provides a wide variety of bulk distribution facilities for users in many industries, including major retailers. In 2005, Duke completed a nearly 100,000 square foot expansion for Saks in Chicago.

► Duke Construction offers tenant finish capabilities that foster rapid completion and lower construction costs.







Riverway East office building in Rosemont, IL. Part of a five-building, \$257 million acquisition which gave Duke a major presence in the O'Hare submarket of Chicago.



► Duke began \$244 million of bulk industrial buildings in 2005, averaging nearly 350,000 square feet per bulk development start.

▼ Duke's retail projects gained great momentum last year. Pembroke Pines in South Florida, and West Carmel Marketplace in Indianapolis are examples of planned new retail developments.



We have begun nearly \$100 million of healthcare developments since the program's inception in 2004. This included seven projects in four states across the eastern half of the country. Our goal for 2006 is \$160 million in new healthcare development starts.

### Development of Retail Properties

Duke's retail development strategy continues to be to build power, lifestyle, neighborhood and mixed-use properties in growing markets throughout the nation. Once we

achieve full occupancy, the assets are sold and the profits are recycled into new developments.

We are partnering with a Cincinnati-based developer to build lifestyle centers, which are the successors to enclosed shopping malls. They are smaller, more neighborhood-friendly, do not require a huge anchor retailer, and are far less costly to build.

Presently, planned retail developments total approximately \$206 million, including potential projects in Indiana, Pennsylvania and South Florida.







▲ **Anson, IN.** Ground work is well underway at the 1,700-acre mixed-use project to be developed over the next 15 years. Located on the northwest side of Indianapolis along Interstate 65, the project will include office, industrial, retail, medical and residential development with an ultimate value of more than \$750 million.

▼ **BlueCross BlueShield of Western New York, Buffalo, NY.** Duke began this \$98 million office facility for a subsidiary of HealthNow New York. Once completed, it will total 432,000 square feet. This illustrates Duke's national development capabilities outside of its traditional market areas.

## Land Acquisition

A primary factor in our development strategy is owning land inventory in key submarkets in all of our existing markets. In 2005, we employed more than \$130 million of land at cost through development and profitable land sales. Today we own or control approximately 4,800 acres of land at a direct cost of \$430 million which we believe has a value of approximately \$100 million in excess of our cost.

## The Industrial Portfolio Sale

In the third quarter of 2005, we sold 14.1 million square feet of primarily older and smaller industrial properties for approximately \$1 billion. Located in eight of our markets with primary concentrations in Atlanta, Minneapolis and Nashville, these properties were capital and management intensive. The average building size was 67,000 square feet, with the average tenant size of approximately 14,000 square feet.

### Profile of the 2005 Industrial Portfolio Sale

	Sold Flex Portfolio	Remaining In-Service Portfolio September 30, 2005		
		Industrial	Office	Total
Total Square Feet*	14,100	67,500	29,300	96,800
Number of Buildings	212	403	255	658
Avg. Building Age**	14.6	9.7	11.5	10.3
Avg. Building Size	67,000	167,000	115,000	147,000
Avg. Size of Lease*	14,000	48,600	12,000	25,600
Number of Tenants	868	1,278	2,164	3,442
Occupancy rate	84.7%	92.0%	88.5%	91.0%

\* (in thousands of square feet) \*\* (in years)



► **Freeport North, Coppell, TX.** An existing Duke tenant, Uline Inc. expanded at Freeport North by 143,000 square feet at Freeport XIV, scheduled for completion in the first quarter of 2006.













▲ Celebration Office Center, Celebration, FL. Located in Central Florida, this two-building 162,000 square foot office complex was fully leased at year-end.

The difference between what was retained and what was sold is significant. The retained industrial portfolio is comprised of buildings that average more than twice as large and five years newer. Leased space per tenant is nearly three times greater and occupancy is 7 percentage points higher. Today our industrial portfolio is now concentrated largely in major distribution markets across the Midwest and Southeast including Atlanta, Chicago, Dallas and Indianapolis.

The sale proceeds provide us with ample flexibility to both expand our development pipeline and to increase the return to our shareholders. As a result of the sale, we issued a special dividend of \$1.05 per share to our shareholders on December 15.

### Third-Party Construction Activity

We continue to meet our customers' needs by being flexible and offering third-party, fee-based construction services in addition to our development capabilities. Contracts awarded for such third-party work during 2005 were more than \$250 million. Fees that will be earned on these contracts totaled \$24.0 million or 10.4 percent of the job costs.

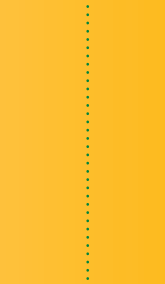
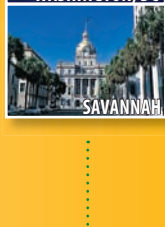
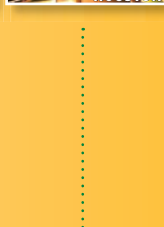
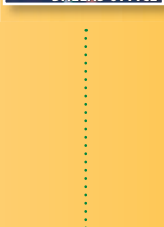
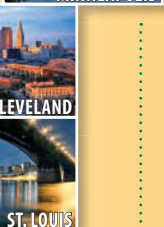
Major projects in process during 2005 included a 345,000 square foot corporate headquarters building for Simon Property Group in downtown Indianapolis; a 120,000 square foot corporate headquarters for Delmar Gardens in St. Louis; and a 400,000 square foot distribution center for Build-A-Bear Workshop, Inc. in Columbus, Ohio.



# Duke Timeline



Duke Realty Investments goes public



1972 1977 1985 1989 1993 1995 1997 1999 2004 2005 2006

## Geographic Expansion Accelerates

Duke has always considered geographic expansion to be an integral part of its growth strategy. In the 1990s, the Company grew from four markets to 14 with expansion throughout the Midwest and into the Southeast. Now we are poised for additional growth as we focus on large, fast-growing markets with bright economic futures.

During 2005 we carefully studied markets across the United States to determine where Duke had the greatest opportunities. After this study, we committed to open offices in Houston, Texas and Phoenix, Arizona. Both of these markets will allow us significant bulk distribution development opportunities. In early 2006, we continued our geographic expansion with focus on major ports.

We acquired a 5.1 million square foot bulk distribution portfolio adjacent to the Port of Savannah, Georgia. We also acquired a 184-acre former General Motors plant at the Port of Baltimore which can accommodate nearly three million square feet of future distribution development.

We also acquired the commercial operations of The Mark Winkler Company in the Washington, D.C. area. This acquisition gives us nearly three million square feet of office and industrial properties, 166 acres of land which can support the future development of 3.7 million square feet, and an operating team of real estate professionals who will join Duke and continue to build our presence in the Mid-Atlantic.





Shaughnessy Paper Company building, Maryland Heights, MO. Duke built this 130,000 square foot warehouse and distribution center last year specifically for the tenant at Lakeside Crossing in suburban St. Louis.





▲ St. Vincent Primary Care Network, Carmel, IN. This was the first project Duke completed after forming a joint venture with Bremner Healthcare Real Estate.

## Balance Sheet Management

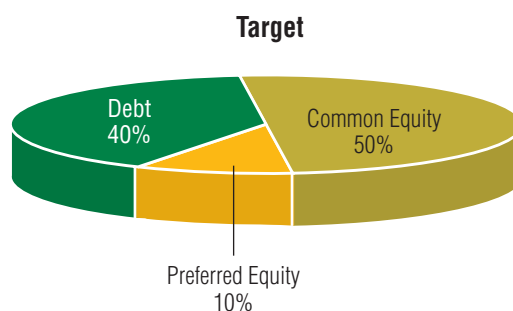
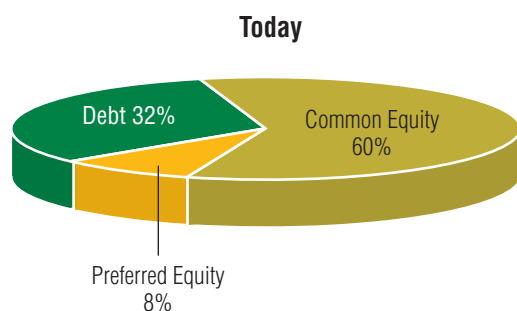
Our debt to total market capitalization was 32 percent at the end of 2005, our fixed charge covered ratio was 2.7 times, and our capitalization was 60 percent common equity, 8 percent preferred, and 32 percent debt. We expect to increase our leverage moderately while maintaining our current investment grade rating. Our target debt-to-market capitalization is between 35 percent and 40 percent with a fixed charge coverage ratio of 2.2 to 2.4 times. This would result in a capital structure of approximately 50 percent common equity, 10 percent preferred, and 40 percent debt.

In addition, since July 2005, more than \$300 million of proceeds from our property disposition was used to repurchase more than 9 million common shares at an average price of \$33.02 per share.

## Outlook

The future is bright for Duke Realty Corporation. We have positioned our portfolio through property dispositions, new development and acquisitions. We are well poised to grow our earnings through new development and geographic expansion. We are excited about our opportunities.

## Market Capitalization





## Selected Consolidated Financial Data

The following sets forth selected financial and operating information on a historical basis for each of the years in the five-year period ended December 31, 2005. The following information should be read in conjunction with “Management’s

Discussion and Analysis of Financial Condition and Results of Operations” and “Financial Statements and Supplementary Data” included in this Annual Report (in thousands, except per share amounts):

	2005	2004	2003	2002	2001
<b>Results of Operations:</b>					
Revenues:					
Rental Operations from Continuing Operations	\$ 706,183	\$ 641,155	\$ 584,403	\$ 550,232	\$ 554,305
Service Operations from Continuing Operations	81,941	70,803	59,456	68,580	80,459
<b>Total Revenues from Continuing Operations</b>	<b>\$ 788,124</b>	<b>\$ 711,958</b>	<b>\$ 643,859</b>	<b>\$ 618,812</b>	<b>\$ 634,764</b>
<b>Income from Continuing Operations</b>	<b>\$ 139,753</b>	<b>\$ 144,832</b>	<b>\$ 151,974</b>	<b>\$ 166,030</b>	<b>\$ 232,009</b>
<b>Net Income Available for common shareholders</b>	<b>\$ 309,183</b>	<b>\$ 151,279</b>	<b>\$ 161,911</b>	<b>\$ 153,969</b>	<b>\$ 227,743</b>

### Per Share Data :

Basic income per common share:

Continuing operations	\$ .66	\$ .76	\$ .84	\$ .84	\$ 1.37
Discontinued operations	1.53	.31	.35	.31	.39

Diluted income per common share:

Continuing operations	.65	.75	.84	.84	1.36
Discontinued operations	1.52	.31	.35	.30	.38

Dividends paid per common share

	1.87	1.85	1.83	1.81	1.76
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Dividends paid per common share – special

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Weighted average common shares outstanding

	141,508	141,379	135,595	133,981	129,660
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Weighted average common and dilutive potential common shares

	155,877	157,062	151,141	150,839	151,710
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### Balance Sheet Data (at December 31):

Total Assets	\$ 5,647,560	\$ 5,896,643	\$ 5,561,249	\$ 5,348,823	\$ 5,330,033
Total Debt	2,600,651	2,518,704	2,335,536	2,106,285	1,814,856
Total Preferred Equity	657,250	657,250	540,508	440,889	608,664
Total Shareholders’ Equity	2,452,798	2,825,869	2,666,749	2,617,336	2,785,323
Total Common Shares Outstanding	134,697	142,894	136,594	135,007	131,416

### Other Data:

Funds From Operations <sup>(1)</sup>	\$ 341,189	\$ 352,469	\$ 335,989	\$ 321,886	\$ 340,315
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<sup>(1)</sup> Funds From Operations (“FFO”) is used by industry analysts and investors as a supplemental operating performance measure of an equity real estate investment trust (“REIT”). FFO is calculated in accordance with the definition that was adopted by the Board of Governors of the National Association of Real Estate Investment Trusts (“NAREIT”). FFO, as defined by NAREIT, represents net income (loss) determined in accordance with accounting principles generally accepted in the United States of America (“GAAP”), excluding extraordinary items as defined under GAAP and gains or losses from sales of previously depreciated operating real estate assets, plus certain non-cash items such as real estate asset depreciation and amortization, and after similar adjustments for unconsolidated partnerships and joint ventures.

Historical cost accounting for real estate assets in accordance with GAAP implicitly assumes that the value of real estate assets diminishes predictably over time. Since real estate values instead have historically risen or fallen with market conditions, many industry investors and analysts have considered the presentation of operating results for real estate companies that use historical cost accounting to be insufficient by themselves. Thus, NAREIT created FFO as a supplemental measure of REIT operating performance that excludes historical cost depreciation, among other items, from GAAP net income. Management believes that the use of FFO, combined with the required primary GAAP presentations, has improved the understanding of operating results of REITs among the investing public and has made comparisons of REIT operating results more meaningful. Management considers FFO to be a useful measure for reviewing comparative operating and financial performance (although FFO should be reviewed in conjunction with net income which remains the primary measure of performance) because, by excluding gains or losses related to sales of previously depreciated operating real estate assets and excluding real estate asset depreciation and amortization, FFO assists in comparing the operating performance of a company’s real estate between periods or as compared to different companies.

See reconciliation of FFO to GAAP net income under Year in Review section of Management’s Discussion and Analysis of Financial Condition and Results of Operations.





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

## Cautionary Statement Regarding Forward-Looking Statements

Certain statements contained or incorporated by reference into this Annual Report, including those related to our future operations, constitute "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). These forward-looking statements involve known and unknown risks, uncertainties and other important factors that could cause our actual results, performance or achievements, or industry results, to differ materially from any predictions of future results, performance or achievements that we express or imply in this report. Some of the most significant risks, uncertainties and other important factors that may affect future results include, among others:

- If we were to cease to qualify as a real estate investment trust, we and our shareholders would lose significant tax benefits;
- Real estate investment trust distribution requirements limit the amount of cash we will have available for other business purposes, including amounts that we need to fund our future growth;
- U.S. federal income tax developments could affect the desirability of investing in us for individual taxpayers;
- U.S. federal income tax treatment of REITs and investments in REITs may change, which may result in the loss of our tax benefits of operating as a REIT;
- Our net earnings available for investment or distribution to shareholders could decrease as a result of factors outside of our control;
- Many real estate costs are fixed, even if income from properties decreases;
- Our real estate development activities are subject to risks particular to development;
- We are exposed to risks associated with entering new markets;
- We may be unsuccessful in operating completed real estate projects;
- We are exposed to the risks of defaults by tenants;
- We may be unable to renew leases or relet space;
- Our insurance coverage on our properties may be inadequate;
- Acquired properties may expose us to unknown liability;
- We could be exposed to significant environmental liabilities as a result of conditions of which we currently are not aware;
- Certain of our officers and directors hold units in our operating partnership and may not have the same interests as our shareholders with regard to certain tax matters;
- We do not have exclusive control over our joint venture investments;
- Our use of debt financing could have a material adverse effect on our financial condition;
- We are subject to various financial covenants under existing credit agreements;
- We are subject to certain provisions that could discourage change-of-control transactions, which may reduce the likelihood of our shareholders receiving a control premium for their shares; and
- We are dependent on key personnel.

This list of risks and uncertainties, however, is not intended to be exhaustive. We have on file with the Securities and Exchange Commission ("SEC") a Current Report on Form 10-K dated March 6, 2006, with additional risk factor information.

The words "believe," "estimate," "expect," "anticipate," "intend," "plan," "seek" and similar expressions or statements regarding future periods are intended to identify forward-looking statements. Although we believe that the plans, expectations and results expressed in or suggested by the forward-looking statements are reasonable, all forward-looking statements are inherently uncertain as they involve substantial risks and uncertainties beyond our control. New factors emerge from time to time, and it is not possible for us to predict the nature or assess the potential impact of each new factor on our business. Given these uncertainties, we caution you not to place undue reliance on these forward-looking statements. We undertake no obligation to update or revise any of our forward-looking statements for events or circumstances that arise after the statement is made.

## Business Overview

We are a self-administered and self-managed real estate investment trust that began operations through a related entity in 1972. As of December 31, 2005, we:

- Owned or jointly controlled 690 industrial, office and retail properties (including properties under development), consisting of over 105.4 million square feet primarily located in 13 operating platforms; and
- Owned or jointly controlled approximately 4,800 acres of land with an estimated future development potential of approximately 69 million square feet of industrial, office and retail properties.





We provide the following services for our properties and for certain properties owned by third parties and joint ventures:

- Property leasing;
- Property management;
- Construction;
- Development; and
- Other tenant-related services.

### Management Philosophy and Priorities

Our key business and financial strategies for the future include the following:

- Our business objective is to increase Funds From Operations (“FFO”) by (i) maintaining and increasing property occupancy and rental rates through the management of our portfolio of existing properties; (ii) developing and acquiring new properties for rental operations in our existing markets; (iii) expanding geographically by acquiring and developing properties in new markets; (iv) using our construction expertise to act as a general contractor in our existing markets and other domestic markets on a fee basis; (v) developing properties in our existing markets and other markets which we will sell through our merchant building development program and (vi) providing a full line of real estate services to our tenants and to third parties.

See the Year in Review section below for further explanation and definition of FFO.

- Our financing strategy is to actively manage the components of our capital structure including common and preferred equity and debt to maintain a conservatively leveraged balance sheet and investment grade ratings from our credit rating agencies. This strategy provides us with the financial flexibility to fund both development and acquisition opportunities. We seek to maintain a well-balanced, conservative and flexible capital structure by: (i) extending and sequencing the maturity dates of debt; (ii) borrowing primarily at fixed rates by targeting a variable rate component of total debt less than 20%; (iii) pursuing current and future long-term debt financings and refinancing on an unsecured basis; (iv) maintaining conservative debt service and fixed charge coverage ratios; and (v) issuing attractively priced perpetual preferred stock for 5-10% of our total capital structure.

### Year in Review

During 2005, we emerged from economic and market challenges that had affected the entire real estate industry to complete a successful year that included improving our portfolio of held for investment buildings through our capital

recycling program, increasing our development pipeline to over double that of 2004, and initiating geographic expansion that we anticipate will provide future earnings growth. As a result of these accomplishments, we achieved steady operating results while maintaining a strong balance sheet.

Net income available for common shareholders for the year ended December 31, 2005, was \$309.2 million, or \$2.17 per share (diluted), compared to net income of \$151.3 million, or \$1.06 per share (diluted) for the year ended 2004. The increase is primarily attributable to the sale of a portfolio of 212 real estate properties, consisting of 14.1 million square feet of primarily light distribution and service center properties (the “Industrial Portfolio Sale”). The net book gain on this sale was approximately \$201.5 million. See additional discussion of the transaction below. Through increased leasing activity, we achieved a growth in rental revenues in 2005 over 2004 as our in-service portfolio year-end occupancy increased from 90.9% at the end of 2004 to 92.5% at the end of 2005. We also experienced an increase in our development and construction of new properties for both owned investments and third party construction projects in 2005 as compared to 2004.

As an important performance metric for us as a real estate company, FFO available to common shareholders totaled \$341.2 million for the year ended December 31, 2005, compared to \$352.5 million for the same period in 2004. We anticipated a short-term decrease in FFO as a result of the Industrial Portfolio Sale noted above.

FFO is used by industry analysts and investors as a supplemental operating performance measure of an equity real estate investment trust (“REIT”). FFO is calculated in accordance with the definition that was adopted by the Board of Governors of the National Association of Real Estate Investment Trusts (“NAREIT”). FFO, as defined by NAREIT, represents net income (loss) determined in accordance with accounting principles generally accepted in the United States of America (“GAAP”), excluding extraordinary items as defined under GAAP and gains or losses from sales of previously depreciated operating real estate assets, plus certain non-cash items such as real estate asset depreciation and amortization, and after similar adjustments for unconsolidated partnerships and joint ventures.

Historical cost accounting for real estate assets in accordance with GAAP implicitly assumes that the value of real estate assets diminishes predictably over time. Since real estate values instead have historically risen or fallen with market conditions, many industry investors and analysts have considered presentation of operating results for real estate companies that use historical cost accounting to be insufficient by themselves. Thus, NAREIT created FFO as a supplemental measure of REIT operating performance that excludes historical cost depreciation, among other items, from GAAP net income. Management believes that the use of FFO, combined with the required primary GAAP presentations, improves the understanding of operating results of REITs among the investing public and makes comparisons





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of REIT operating results more meaningful. Management considers FFO to be a useful measure for reviewing comparative operating and financial performance (although FFO should be reviewed in conjunction with net income which remains the primary measure of performance) because by excluding gains or losses related to sales of previously depreciated operating

real estate assets and excluding real estate asset depreciation and amortization, FFO assists in comparing the operating performance of a company's real estate between periods or as compared to different companies.

The following table summarizes the calculation of FFO for the years ended December 31 (in thousands):

	2005	2004	2003
Net income available for common shareholders	<b>\$309,183</b>	\$ 151,279	\$ 161,911
Adjustments:			
Depreciation and amortization	<b>254,170</b>	228,582	196,234
Company share of joint venture depreciation and amortization	<b>19,510</b>	18,901	18,839
Earnings from depreciable property sales – wholly owned	<b>(227,513)</b>	(26,510)	(22,141)
Earnings from depreciable property sales – share of joint venture	<b>(11,096)</b>	–	–
Minority interest share of adjustments	<b>(3,065)</b>	(19,783)	(18,854)
Funds From Operations	<b><u>\$341,189</u></b>	<u>\$ 352,469</u>	<u>\$ 335,989</u>

Throughout 2005, we continued to maintain a conservative balance sheet and investment grade debt ratings from Moody's (Baa1), Standard & Poors (BBB+) and Fitch (BBB+). Our debt to total market capitalization ratio (total market capitalization is defined as the total market value of all outstanding common and preferred shares and units of limited partner interest in our operating partnership plus outstanding indebtedness) of 31.8% at December 31, 2005 compared to 29.5% at December 31, 2004 continues to provide us financial flexibility to fund new investments.

Highlights of our debt financing activity in 2005 are as follows:

- In January 2005, we retired a \$65.0 million variable-rate term loan.
- In March 2005, we retired \$100.0 million of 6.875% senior unsecured debt that matured.
- In May 2005, we obtained a \$400.0 million variable rate term loan. The proceeds from this term loan were used to finance a property portfolio acquisition. The loan was paid off in September 2005 with proceeds from the Industrial Portfolio Sale.
- In September 2005, we retired \$100.0 million of 7.375% corporate unsecured debt that matured.

On the equity side of our balance sheet, we repurchased approximately 9 million common shares totaling nearly \$300 million during the third and fourth quarters of 2005. With the added liquidity from the Industrial Portfolio Sale, we pursued a prudent repurchase program to supplement our other value creation activities.

In addition to steady operating performance and prudent balance sheet management during 2005, we continued to effectively execute our capital recycling program and began several key initiatives and projects to leverage our development and construction capabilities as follows:

- We disposed of over \$1.1 billion of older, non-strategic, held for investment properties and used the proceeds to help fund over \$300 million of acquisitions and pay down our operating line of credit. Most significantly, we completed the Industrial Portfolio Sale in September 2005 receiving net proceeds of \$955 million. This portfolio consisted of over 14 million square feet comprised of 212 properties across eight Duke markets as well as 50 acres of undeveloped land. Portions of the proceeds were used to pay down \$423 million of outstanding debt on our \$500 million unsecured line of credit and \$400 million term loan. This transaction was a continuation of our long-term strategy of recycling assets into higher yielding new developments. Within the industrial side of our business, it also positions our ownership focus toward newly developed bulk warehouse properties.
- We completed over \$300 million of acquisitions in 2005, including a \$257 million suburban office portfolio in our Chicago market. The portfolio consisted of five office buildings totaling 1.4 million square feet.
- We increased our investment in undeveloped land to provide greater opportunities to use our development and construction expertise in the improving economic cycle. Throughout 2005, we completed land acquisitions totaling over \$135 million. The new land positions include industrial, office and retail positions in Florida where we intend to develop a retail lifestyle center with a joint venture partner and continue office and industrial development in Broward County.
- Our National Development and Construction Group, which was formed in 2004 to pursue development and construction opportunities with companies that have a national presence including those outside our core





markets, completed a successful year that included the awarding of a 431,000 square foot office building development in Buffalo, New York. The project is pre-leased to a single tenant with construction expected to be completed in mid-2007.

- The National Development and Construction Group also experienced significant growth of its healthcare business. In 2004, we created a strategic agreement with Bremner Healthcare, a developer of medical office and healthcare related facilities, to jointly develop and sell medical facilities throughout the United States. Bremner develops, leases and manages the facilities while we provide construction financing and general contractor services. We share 50/50 in the profits upon sale of the projects. In 2005, we completed our first project in this venture, a medical office building in Indianapolis, Indiana that was sold in September 2005. As of December 31, 2005, we have six additional healthcare development projects underway, totaling nearly 470,000 square feet.
- We announced our intentions to enter the Phoenix, Arizona and Houston, Texas markets. We believe these markets provide significant growth opportunities in the future and have similar demographics and components that our existing markets provide.
- Finally, we will continue to develop long-term investment assets to be held in our portfolio, develop assets to be sold upon completion and perform third party construction projects. With nearly \$800 million in our development pipeline at December 31, 2005, we are encouraged about the long-term growth opportunities in our business.

### Significant 2006 Activity

We have continued to build on our momentum from 2005 by announcing the following significant transactions in early 2006:

- In January 2006, we announced the acquisition of approximately 5.1 million square feet of bulk industrial properties located at the Port of Savannah for a total purchase price of approximately \$194.1 million. The portfolio consists of 18 buildings and is located near one of the fastest growing ports in the country. The properties are 100% leased with a weighted average lease term of 7.5 years. This transaction makes us the largest industrial property owner in the Savannah area and complements our industrial holdings across the Southeast. In addition, we have the option to acquire future completed development projects on 400 acres of land in the same market.
- In January 2006, we issued \$184 million of 6.95% Series M Cumulative Redeemable Preferred Stock, which replaced our \$75 million 8.45% Series I Cumulative Redeemable Preferred Stock that we redeemed in February 2006.
- In January 2006, we renewed our unsecured revolving credit facility. The new facility provides borrowing capacity up to \$1 billion and, subject to certain conditions, may be increased to \$1.3 billion. Under the new facility, which replaces the previous unsecured line of credit agreement, we reduced the interest rate by 7.5 basis points to LIBOR plus 52.5 basis points, increased the borrowing capacity by \$500 million and extended the maturity date to January 25, 2010.
- In February 2006, we issued \$125.0 million of 5.5% senior notes, due 2016.
- In February 2006, we acquired 27 suburban office and light industrial buildings, encompassing more than 2.3 million square feet from the Mark Winkler Company for \$619.0 million. The 27 buildings are part of a 32 building portfolio located in three primary submarkets in Northern Virginia. We will close on the remaining five buildings in the portfolio throughout the first and second quarters of 2006. In addition to the 27 buildings we also closed on approximately 166 acres of undeveloped land located in major business parks that can support the future development of approximately 3.7 million square feet of office and industrial buildings. In connection with the acquisition, we obtained a \$700 million secured term loan priced at LIBOR plus 52.5 basis points with a scheduled maturity date of September 2006. Subject to Lender's approval, the maturity date may be extended to March 2007.

### Key Performance Indicators

Our operating results depend primarily upon rental income from our office, industrial and retail properties ("Rental Operations"). The following highlights the areas of Rental Operations that we consider critical for future revenue growth. All square footage totals and occupancy percentages reflect both wholly-owned properties and properties in joint ventures.

**Occupancy Analysis:** As discussed above, our ability to maintain occupancy rates is a principal driver of our results of operations. The following table sets forth occupancy information regarding our in-service portfolio of rental properties as of December 31, 2005 and 2004 (in thousands, except percentage data):





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Type	Total Square Feet		Percent of Total Square Feet		Percent Occupied	
	2005	2004	2005	2004	2005	2004
<b>Industrial</b>						
Service Centers	5,457	12,924	5.6%	11.8%	92.7%	85.2%
Bulk	63,062	67,940	63.9%	62.0%	94.1%	93.4%
<b>Office</b>	29,508	28,175	29.9%	25.7%	89.1%	87.1%
<b>Retail</b>	611	596	0.6%	0.5%	96.0%	100.0%
<b>Total</b>	<b>98,638</b>	<b>109,635</b>	<b>100.0%</b>	<b>100.0%</b>	<b>92.5%</b>	<b>90.9%</b>

The overall improvement in occupancy was driven by a number of factors, but the most significant factor was the volume of leasing activity for the year. We experienced significant activity in the fourth quarter of 2005 when we signed nearly 9.7 million square feet of new leases and renewals, which was the highest quarterly leasing activity in our history. Our industrial and office product types both showed improvement in occupancy and activity in our markets was strong in 2005.

**Lease Expiration and Renewals:** Our ability to maintain and grow occupancy rates primarily depends upon our continuing ability to re-lease expiring space. The following table reflects our in-service lease expiration schedule by property type as of December 31, 2005. The table indicates square footage and annualized net effective rents (based on December 2005 rental revenue) under expiring leases (in thousands, except percentage data):

Year of Expiration	Total Portfolio			Industrial		Office		Retail	
	Square Feet	Ann. Rent Revenue	% of Revenue	Square Feet	Ann. Rent Revenue	Square Feet	Ann. Rent Revenue	Square Feet	Ann. Rent Revenue
2006	7,938	\$ 52,743	8%	5,764	\$ 24,571	2,173	\$ 28,154	1	\$ 18
2007	10,938	67,978	11%	8,287	33,087	2,642	34,768	9	123
2008	13,263	84,550	14%	9,675	39,927	3,569	44,288	19	335
2009	11,190	73,741	12%	7,685	30,128	3,501	43,535	4	78
2010	11,444	90,491	15%	7,449	34,400	3,988	55,986	7	105
2011	8,470	58,304	9%	5,960	24,349	2,486	33,532	24	423
2012	6,316	37,519	6%	4,639	16,145	1,670	21,041	7	333
2013	4,867	47,676	8%	2,332	10,371	2,501	36,726	34	579
2014	4,102	21,397	3%	3,324	11,118	778	10,279	—	—
2015	5,492	35,866	6%	4,228	17,313	1,264	18,553	—	—
2016 and Thereafter	7,249	48,361	8%	5,035	19,433	1,734	25,707	480	3,221
	<u>91,269</u>	<u>\$ 618,626</u>	<u>100%</u>	<u>64,378</u>	<u>\$ 260,842</u>	<u>26,306</u>	<u>\$ 352,569</u>	<u>585</u>	<u>\$ 5,215</u>
<b>Total Portfolio</b>									
Square Feet	<u>98,638</u>			<u>68,519</u>		<u>29,508</u>		<u>611</u>	
Percent Occupied	<u>92.5%</u>			<u>94.0%</u>		<u>89.1%</u>		<u>96.0%</u>	

We renewed 74.3% and 73.9% of our leases up for renewal totaling approximately 10.0 million and 9.9 million square feet in 2005 and 2004, respectively. Our lease renewal percentages over the past three years have remained relatively consistent at a 70-75% success rate. We do not expect this renewal percentage in 2006 to differ from that experienced in 2005.

The average term of renewals increased to 4.3 years in 2005 from 3.8 years in 2004. The increase in the average term is due to competitive market conditions with tenants seeking longer leases at attractive rates.

**Future Development:** Another source of growth in earnings is the development of additional properties. These properties should provide future earnings through Service Operations income upon sale or from Rental Operations growth as they

are placed in service. We had 9.0 million square feet of property under development with total estimated costs of \$658.7 million at December 31, 2005, compared to 4.2 million square feet and total costs of \$194.9 million at December 31, 2004. We have increased our development pipeline significantly through 2005 as we focus on the development side of our business in 2006. We have assessed our markets and determined that between growing demand and the pricing of acquisitions, we can utilize our development expertise and achieve better returns on our own developments. The significant leasing activity experienced in the fourth quarter of 2005 as noted above has provided momentum heading into 2006.

The following table summarizes our properties under development as of December 31, 2005 (in thousands, except percentage data):





Anticipated In-Service Date	Square Feet	Percent Leased	Project Costs	Anticipated Stabilized Return
<b>Held for Rental:</b>				
1st Quarter 2006	844	16%	\$ 43,379	9.7%
2nd Quarter 2006	3,852	32%	168,286	9.6%
3rd Quarter 2006	727	26%	48,682	9.8%
Thereafter	<u>1,385</u>	62%	<u>111,588</u>	9.4%
	<u>6,808</u>	35%	<u>371,935</u>	9.6%
<b>Merchant Buildings:</b>				
1st Quarter 2006	818	23%	37,651	9.3%
2nd Quarter 2006	401	76%	57,351	9.0%
3rd Quarter 2006	146	72%	20,689	10.2%
Thereafter	<u>831</u>	95%	<u>171,040</u>	8.6%
	<u>2,196</u>	63%	<u>286,731</u>	9.0%
<b>Total</b>	<u><b>9,004</b></u>	<b>42%</b>	<u><b>\$ 658,666</b></u>	<b>9.3%</b>

**Acquisition and Disposition Activity:** In 2005, we continued our capital recycling program by disposing over \$1.1 billion of older, non-strategic properties. Most significantly, we completed the Industrial Portfolio Sale for nearly \$980 million. The Industrial Portfolio Sale consisted of over 14 million square feet of primarily light distribution and service center properties comprised of 212 properties across eight of our markets. The Industrial Portfolio Sale was a continuation of our strategy of recycling assets into higher yielding new developments. Within the industrial side of our business, it also positions our ownership focus toward newly developed bulk warehouse properties. See further discussion of the Industrial Portfolio Sale in the Year in Review section. As we focus on development

in 2006, we will continue to dispose of older assets, but do not anticipate the activity to be comparable to the dispositions activity of 2005.

On the acquisitions side, we completed over \$300 million of acquisitions in 2005, including a \$257 million suburban office portfolio in our Chicago market. The portfolio consists of five office buildings totaling 1.4 million square feet.

### Results of Operations

A summary of our operating results and property statistics for each of the years in the three-year period ended December 31, 2005, follows (in thousands, except number of properties and per share data):

	2005	2004	2003
Rental Operations revenues from Continuing Operations	\$ 706,183	\$ 641,155	\$ 584,403
Service Operations revenues from Continuing Operations	81,941	70,803	59,456
Earnings from Continuing Rental Operations	118,547	144,713	148,478
Earnings from Continuing Service Operations	41,019	24,421	21,821
Operating income	131,731	142,856	148,319
Net income available for common shareholders	309,183	151,279	161,911
Weighted average common shares outstanding	141,508	141,379	135,595
Weighted average common and dilutive potential common shares	155,877	157,062	151,141
Basic income per common share:			
Continuing operations	\$ .66	\$ .76	\$ .84
Discontinued operations	\$ 1.53	\$ .31	\$ .35
Diluted income per common share:			
Continuing operation	\$ .65	\$ .75	\$ .84
Discontinued operations	\$ 1.52	\$ .31	\$ .35
Number of in-service properties at end of year	664	874	883
In-service square footage at end of year	98,638	109,635	106,169
Under development square footage at end of year	6,808	3,244	2,103





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## Comparison of Year Ended December 31, 2005 to Year Ended December 31, 2004

### Rental Income from Continuing Operations

Overall, rental income from continuing operations increased from \$619.6 million in 2004 to \$676.6 million in 2005. The following table reconciles rental income from continuing operations by reportable segment to total reported rental income from continuing operations for the years ended December 31, 2005 and 2004 (in thousands):

	2005	2004
Office	<b>\$491,895</b>	\$ 448,682
Industrial	<b>174,963</b>	160,709
Non-segment	<b>9,776</b>	10,178
Total	<b><u>\$676,634</u></b>	<u>\$ 619,569</u>

Both of our reportable segments that comprise Rental Operations (office and industrial) are within the real estate industry; however, the same economic and industry conditions do not affect each segment in the same manner. The primary causes of the increase in rental income from continuing operations, with specific references to a particular segment when applicable, are summarized below:

- In 2005, we have acquired nine new properties and placed 17 development projects in-service. These acquisitions and developments are the primary factor in the \$57.1 million overall increase in rental revenue for the year ended 2005, compared to 2004.

The nine property acquisitions provided revenues of \$21.0 million. These acquisitions totaled \$307.5 million on 2.2 million square feet and were 86.5% leased at December 31, 2005. Revenues from acquisitions that occurred in 2004 grew to \$31.8 million in 2005 compared to \$13.4 million in 2004.

Developments placed in service in 2005 provided revenues of \$5.8 million. Revenues from developments placed in service in 2004 increased \$9.9 million to \$17.4 million in 2005.

- Our in-service occupancy increased from 90.9% at December 31, 2004, to 92.5% at December 31, 2005.
- Rental income includes lease termination fees. Lease termination fees relate to specific tenants who pay a fee to terminate their lease obligations before the end of the contractual lease term. Lease termination fees in 2005 continued to steadily decrease as a result of improving market conditions. Lease termination fees decreased from \$14.7 million in 2004 to \$7.3 million in 2005.

### Equity in Earnings of Unconsolidated Companies

Equity in earnings represents our ownership share of net income from investments in unconsolidated companies. These joint ventures generally own and operate rental properties and hold land for development. These earnings increased from \$21.6 million in 2004 to \$29.5 million in 2005. During the second quarter of 2005, one of our ventures sold three buildings with our share of the net gain recorded through equity in earnings totaling \$11.1 million.

### Rental Expenses and Real Estate Taxes

The following table reconciles rental expenses and real estate taxes by reportable segment to our total reported amounts in the statement of operations for the years ended December 31, 2005 and 2004, respectively (in thousands):

	2005	2004
Rental Expenses:		
Office	<b>\$ 133,383</b>	\$ 113,688
Industrial	<b>23,073</b>	20,147
Non-segment	<b>1,557</b>	1,214
Total	<b><u>\$ 158,013</u></b>	<u>\$ 135,049</u>
Real Estate Taxes:		
Office	<b>\$ 56,820</b>	\$ 47,620
Industrial	<b>20,827</b>	17,726
Non-segment	<b>5,104</b>	4,681
Total	<b><u>\$ 82,751</u></b>	<u>\$ 70,027</u>

Rental and real estate tax expenses for 2005, as compared to 2004, have increased as a result of our 2004 and 2005 acquisitions as well as our increase in occupancy. This increase in rental and real estate taxes continues to be in line with our expectations.

### Interest Expense

Interest expense increased from \$109.9 million in 2004 to \$120.4 million in 2005, as a result of increased debt levels and higher interest rates. Since August 2004, we had the following debt issuances and redemptions:

- In August 2004, we issued \$250 million of 5.40% unsecured notes due in 2014.
- In December 2004, we issued \$250 million of unsecured floating rate debt at 26 basis points over LIBOR.
- In March 2005, we paid off \$100 million of senior unsecured notes.
- In May 2005, we obtained a \$400 million term loan at 30 basis points over LIBOR. This loan was used to temporarily finance the acquisition of five office properties located in our Chicago market.





- In September 2005, we repaid the \$400 million term loan, as well as \$100 million of corporate unsecured debt, with proceeds from the Industrial Portfolio Sale.
- We assumed approximately \$40.7 million of secured debt in conjunction with property acquisitions in August 2004 and June 2005.

Interest expense on our unsecured line of credit totaled \$6.2 million in 2005 compared to \$6.1 million in 2004. We had \$383 million outstanding on the facility at December 31, 2005.

### Depreciation and Amortization Expense

Depreciation and amortization expense increased from \$181.4 million in 2004 to \$226.5 million in 2005 as a result of increased capital spending associated with increased leasing, the additional basis resulting from acquisition and development activity and the application of Statement of Financial Accounting Standard (“SFAS”) No. 141, *Business Combinations* (“SFAS 141”) as described below. The points below highlight the significant increase in depreciation and amortization.

- Depreciation expense on tenant improvements increased by approximately \$16.4 million.
- Depreciation expense on buildings increased by \$16.6 million.
- Lease commission amortization expense increased by \$1.6 million.

The amortization expense associated with acquired lease intangible assets increased by approximately \$10.5 million. The acquisitions were accounted for in accordance with SFAS 141, which requires the allocation of a portion of a property’s purchase price to intangible assets for leases acquired and in-place at the closing date of the acquisition. These intangible assets are amortized over the remaining life of the leases (generally 3-5 years) as compared to the building basis portion of the acquisition, which is depreciated over 40 years.

### Service Operations

Service Operations primarily consist of our merchant building sales and the leasing, management, construction and development services for joint venture properties and properties owned by third parties. These operations are heavily influenced by the current state of the economy as leasing and management fees are dependent upon occupancy while construction and development services rely on the expansion of business operations. Service Operations earnings increased from \$24.4 million in 2004 to \$41.0 million in 2005. The increase reflects higher construction volumes partially offset by increased staffing costs for our expanded National Development and Construction group in 2005. Other factors impacting service operations are discussed below.

- Our merchant building development and sales program, whereby a building is developed by us and then sold, is a significant component of construction and development income. During 2005, we generated after tax gains of \$19.0 million from the sale of 10 properties compared to \$16.5 million from the sale of six properties in 2004. Profit margins on these types of building sales fluctuate by sale depending on the type of property being sold, the strength of the underlying tenant and nature of the sale, such as a pre-contracted purchase price for a primary tenant versus a sale on the open market.
- In 2005, we experienced an increase in our third party construction business as evidenced by the increase in general contractor revenues in 2005 over 2004. We achieved a slight increase in our profit margins during 2005, which reflects improved pricing in certain markets and our ability to select more profitable projects as resources are re-positioned to our increasing held-for-investment development pipeline.
- In the first quarter of 2005, we recognized \$2.7 million of a deferred gain associated with the sale of our landscaping operations in 2001. The gain was deferred as a result of future performance provisions contained in the original sales agreement. As a result of contract renegotiations effective in the first quarter of 2005, all future performance provisions were removed and the deferred gain was recognized.

### General and Administrative Expense

General and administrative expense increased from \$26.3 million in 2004 to \$27.8 million in 2005. General and administrative expenses are comprised of two components. The first is direct expenses that are not attributable to specific assets such as legal fees, external audit fees, marketing costs, investor relations expenses and other corporate overhead. The second component is the unallocated overhead costs associated with the operation of our owned properties and Service Operations, including construction, leasing and maintenance operations. Overhead costs not allocated to these operations are charged to general and administrative expenses. The increase in general and administrative expenses is primarily the result of an increase in payroll expenses associated with long-term compensation plans and an increase in the number of employees to support our growth in our National Development and Construction practice.





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

## Other Income and Expenses

Earnings from the sale of land and ownership interests in unconsolidated companies, net of impairment adjustments, are comprised of the following amounts in 2005 and 2004, respectively (in thousands):

	2005	2004
Gain on land sales	<b>\$14,459</b>	\$10,543
Gain on sale of ownership interests in unconsolidated companies	–	83
Impairment adjustment	(258)	(424)
Total	<b>\$14,201</b>	\$10,202

Gain on land sales is derived from sales of undeveloped land that we own. We pursue opportunities to dispose of land in those markets with a high concentration of undeveloped land and in those markets where the land no longer meets our strategic development plans.

We recorded \$258,000 and \$424,000 of impairment charges associated with contracts to sell land parcels for the years ended December 31, 2005 and 2004, respectively. All parcels related to the \$258,000 of impairment recorded in 2005 were sold during 2005. One of the parcels on which we recorded an impairment charge in 2004 was sold in the first quarter of 2005, while all remaining parcels of the \$424,000 impairment charge were sold in 2004.

## Discontinued Operations

The results of operations for properties sold during the year or designated as held-for-sale at the end of the period are required to be classified as discontinued operations. The property specific components of net earnings that are classified as discontinued operations include rental revenues, rental expenses, real estate taxes, interest expense, depreciation expense and minority interest, as well as the net gain or loss on the disposition of properties.

We have classified operations of 320 buildings as discontinued operations as of December 31, 2005. These 320 buildings consist of 292 industrial, 23 office and five retail properties. As a result, we classified net income from operations, net of minority interest, of \$11.6 million, \$20.0 million and \$35.5 million as net income from discontinued operations for the years ended December 31, 2005, 2004 and 2003, respectively. Of these properties, 234 were sold during 2005, 41 properties were sold during 2004, 42 properties were sold during 2003 and three operating properties are classified as held-for-sale at December 31, 2005. The gains on disposal of these properties, net of impairment adjustment and minority interest, of \$204.3 million, \$23.9 million and \$11.8 million for the years ended December 31, 2005, 2004 and 2003, respectively, are also reported in discontinued operations.

## Comparison of Year Ended December 31, 2004 to Year Ended December 31, 2003

### Rental Income from Continuing Operations

Rental income from continuing operations increased from \$560.7 million in 2003 to \$619.6 million in 2004. The following table reconciles rental income from continuing operations by reportable segment to total reported rental income from continuing operations for the years ended December 31, 2004 and 2003 (in thousands):

	2004	2003
Office	<b>\$448,682</b>	\$409,071
Industrial	<b>160,709</b>	142,087
Non-Segment	<b>10,178</b>	9,557
Total	<b>\$619,569</b>	\$560,715

Both of our reportable segments that comprise Rental Operations (office and industrial) are within the real estate industry; however, the same economic and industry conditions do not affect each segment in the same manner. The primary causes of the increase in rental income from continuing operations, with specific references to a particular segment when applicable, are summarized below:

- Our in-service occupancy increased from 89.3% at December 31, 2003, to 90.9% at December 31, 2004.
- During the year ended 2004, we acquired 19 new properties and placed 18 development projects in-service. These acquisitions and developments are the primary factors in the overall \$58.9 million increase in rental revenue for the year ended 2004, compared to the same period in 2003.

The 19 property acquisitions totaled \$264.0 million on 2.6 million square feet and were 80.3% leased at December 31, 2004. The two largest acquisitions were office buildings in Atlanta and Cincinnati. The 2004 acquisitions provided revenues of \$14.2 million. Revenues from acquisitions that occurred during 2003 were \$35.2 million in 2004 compared to \$11.9 million in 2003.

Developments placed in service in 2004 provided revenues of \$9.9 million, while revenues associated with developments placed in service in 2003 totaled \$14.7 million in 2004 compared to \$6.6 million in 2003.

- The rental income shown above includes lease termination fees. Lease termination fees relate to specific tenants who pay a fee to terminate their lease obligations before the end of the contractual lease term. Lease termination fees totaled \$16.2 million in 2003, compared to \$14.7 million in 2004. The decrease in termination fees corresponds with fewer corporate downsizings due to improving market conditions.





### Equity in Earnings of Unconsolidated Companies

Equity in earnings represents our ownership share of net income from investments in unconsolidated companies. These joint ventures generally own and operate rental properties and hold land for development. These earnings decreased from \$23.7 million in 2003 to \$21.6 million in 2004 despite overall occupancy remaining relatively flat around 94%. The decrease in earnings is the result of the following:

- A tenant filed for bankruptcy in one joint venture property resulting in occupancy for the property at the end of 2004 being 69.7% versus 87.4% in 2003.
- We sold our interest in one joint venture in December 2003 and, as a result, no earnings were recorded in 2004.

### Rental Expenses and Real Estate Taxes

The following table reconciles rental expenses and real estate taxes by reportable segment to our total reported amounts in the statement of operations for the years ended December 31, 2004 and 2003 (in thousands):

	2004	2003
Rental Expenses:		
Office	\$ 113,688	\$ 100,509
Industrial	20,147	18,632
Non-Segment	1,214	2,295
Total	<u>\$ 135,049</u>	<u>\$ 121,436</u>
Real Estate Taxes:		
Office	\$ 47,620	\$ 41,921
Industrial	17,726	16,457
Non-Segment	4,681	4,447
Total	<u>\$ 70,027</u>	<u>\$ 62,825</u>

The increased rental and real estate tax expenses for 2004, as compared to 2003, were primarily the result of our increase in average in-service square feet and occupancy. These increases resulted from our acquisition activities and developments placed in service as noted above.

### Interest Expense

Interest expense increased from \$100.7 million in 2003 to \$109.9 million in 2004. We issued new debt to fund debt maturities, new developments and acquisitions and to take advantage of the favorable interest rate environment. The following is a summary of debt activities for 2004:

- In January, we obtained a \$65 million floating rate term loan and immediately fixed the rate at 2.18% with two interest rate swaps. We paid off this loan in the first quarter of 2005. Also in January, we issued \$125 million of unsecured debt with a four-year maturity at 3.35%. In August we issued \$250 million of unsecured debt with a ten-year maturity at an

effective rate of 6.33%. In December we issued \$250 million of unsecured floating rate debt at 26 basis points over LIBOR. The debt matures in two years, but is callable at our option after six months.

- In August, we paid off \$15 million of a \$40 million secured floating rate term loan. We also assumed \$29.9 million of secured debt in conjunction with a property acquisition in Atlanta.
- The average balance and average borrowing rate of our \$500 million revolving credit facility were slightly higher in 2004 than in 2003. At the end of 2004, we were not utilizing our credit facility.

### Depreciation and Amortization Expense

Depreciation and amortization expense increased from \$151.0 million in 2003 to \$181.4 million in 2004 as a result of increased capital spending associated with increased leasing, the additional basis resulting from acquisition and development activity and the application of SFAS 141. The points below highlight the significant increase in depreciation and amortization.

- Depreciation expense on tenant improvements increased by \$14.1 million.
- Depreciation expense on buildings increased by \$6.0 million.
- Lease commission amortization expense increased by \$2.2 million.
- The amortization expense associated with acquired lease intangible assets increased by approximately \$10.0 million.

### Service Operations

Service Operations earnings increased from \$21.8 million in 2003 to \$24.4 million in 2004. The increase reflects higher construction volumes partially offset by increased staffing costs for our new National Development and Construction group and construction jobs in certain markets. Other factors impacting service operations are discussed below.

- We experienced a 1.6% decrease in our overall gross profit margin percentage in our general contractor business in 2004 as compared to 2003, due to continued competitive pricing pressure in many of our markets. We expect margins to increase in 2005 as economic conditions improve. However, despite this decrease, we were able to increase our net general contractor revenues from \$26.8 million in 2003 to \$27.6 million in 2004 because of an increase in volume. This volume increase was attributable to continued low financing costs available to businesses, thereby making it more attractive for them to own instead of lease facilities. We have a substantial backlog of \$183.2 million for third party construction as of December 31, 2004, which was carried into 2005.





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- Our merchant building development and sales program, whereby a building is developed by us and then sold, is a significant component of construction and development income. During 2004, we generated after tax gains of \$16.5 million from the sale of six properties compared to \$9.6 million from the sale of four properties in 2003. Profit margins on these types of building sales fluctuate by sale depending on the type of property being sold, the strength of the underlying tenant and nature of the sale, such as a pre-contracted purchase price for a primary tenant versus a sale on the open market.

## General and Administrative Expense

General and administrative expense increased from \$22.0 million in 2003 to \$26.3 million in 2004. The increase was a result of increased staffing and employee compensation costs to support development of our National Development and Construction group. We also experienced an increase in marketing to support certain new projects.

## Other Income and Expenses

Earnings from sales of land and ownership interests in unconsolidated companies, net of impairment adjustments, is comprised of the following amounts in 2004 and 2003 (in thousands):

	2004	2003
Gain on land sales	<b>\$10,543</b>	\$ 7,695
Gain on sale of ownership interests in unconsolidated companies	<b>83</b>	8,617
Impairment adjustment	<b>(424)</b>	(560)
Total	<b><u>\$10,202</u></b>	<b><u>\$15,752</u></b>

In the first quarter of 2003, we sold our 50% interest in a joint venture that owned and operated depreciable investment property. The joint venture developed and operated real estate assets; thus, the gain was not included in operating income.

Gain on land sales are derived from sales of undeveloped land owned by us. We pursue opportunities to dispose of land in markets with a high concentration of undeveloped land and in those markets where the land no longer meets our strategic development plans. The increase was partially attributable to a land sale to a current corporate tenant for potential future expansion.

We recorded \$424,000 and \$560,000 of impairment charges associated with contracts to sell land parcels for the years ended December 31, 2004 and 2003, respectively. As of December 31, 2004, only one parcel on which we recorded impairment charges was still owned by us. We sold this parcel in the first quarter of 2005.

## Critical Accounting Policies

The preparation of our consolidated financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP") requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Our estimates, judgments and assumptions are continually evaluated based upon available information and experience. Note 2 to the Consolidated Financial Statements includes further discussion of our significant accounting policies.

Our management has assessed the accounting policies used in the preparation of our financial statements and discussed them with our Audit Committee and independent auditors. The following accounting policies are considered critical based upon materiality to the financial statements, degree of judgment involved in estimating reported amounts and sensitivity to changes in industry and economic conditions:

**Accounting for Joint Ventures:** We analyze our investments in joint ventures under Financial Accounting Standards Board ("FASB") Interpretation No. 46(R), *Consolidation of Variable Interest Entities*, to determine if the joint venture is considered a variable interest entity and would require consolidation. To the extent that our joint ventures do not qualify as variable interest entities, we further assess under the guidelines of Emerging Issues Task Force ("EITF") Issue No. 04-5, *Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights* ("EITF 04-5"), Statement of Position 78-9, *Accounting for Investments in Real Estate Ventures*; Accounting Research Bulletin No. 51, *Consolidated Financial Statements* and FASB No. 94, *Consolidation of All Majority-Owned Subsidiaries*, to determine if the venture should be consolidated. We have equity interests ranging from 10%-75% in joint ventures that own and operate rental properties and hold land for development. We consolidate those joint ventures that we control through majority ownership interests or substantial participating rights. Control is further demonstrated by the ability of the general partner to manage day-to-day operations, refinance debt and sell the assets of the joint venture without the consent of the limited partner and inability of the limited partner to replace the general partner. We use the equity method of accounting for those joint ventures where we do not have control over operating and financial policies. Under the equity method of accounting, our investment in each joint venture is included on our balance sheet; however, the assets and liabilities of the joint ventures for which we use the equity method are not included on our balance sheet.





**Cost Capitalization:** Direct and certain indirect costs, including interest, clearly associated with and incremental to the development, construction, leasing or expansion of real estate investments are capitalized as a cost of the property. The following discusses the significant categories of costs we incur:

Within our Rental Operations, direct and indirect costs are capitalized under the guidelines of SFAS No. 67, *Accounting for Costs and Initial Rental Operations of Real Estate Projects* ("SFAS 67"), and interest costs are capitalized under the guidelines of SFAS No. 34, *Capitalization of Interest Cost* ("SFAS 34"). We capitalize these project costs associated with the initial construction of a property up to the time the property is substantially complete and ready for its intended use. We believe the completion of the building shell is the proper basis for determining substantial completion and that this basis is the most widely accepted standard in the real estate industry. The interest rate used to capitalize interest is based upon our average borrowing rate on existing debt.

In addition, we capitalize costs, including interest costs, on vacant space during extended lease-up periods after construction of the building shell has been completed if costs are being incurred to ready the vacant space for its intended use. If costs and activities incurred to ready the vacant space cease, then cost capitalization is also discontinued until such activities are resumed. Once necessary work has been completed on a vacant space, project costs are no longer capitalized. We cease capitalization of all project costs on extended lease-up periods after the shorter of a one-year period after the completion of the building shell or when the property attains a 90% occupancy. We follow guidelines in SFAS 34 and SFAS 67 in determining the capitalization of project costs during the lease-up period of a property and believe that this treatment is consistent with real estate industry standards for project cost capitalization.

All direct construction and development costs associated with the development of a new property are capitalized. In addition, all leasing commissions paid to third parties for new leases or lease renewals are capitalized. A portion of our indirect costs considered directly related and incremental to construction/development and leasing efforts are capitalized. In assessing the amount of indirect costs to be capitalized, we first allocate payroll costs, on a department-by-department basis, among activities for which capitalization is warranted (i.e., construction, development and leasing) and those for which capitalization is not warranted (i.e., property management, maintenance, acquisitions and dispositions and general corporate functions). To the extent the employees of a department split their time between capitalizable and non-capitalizable activities, the allocations are made based on estimates of the actual amount of time spent in each activity. Once the payroll costs are allocated, the non-payroll costs of each department are allocated among the capitalizable and non-capitalizable activities in the same proportion as payroll costs.

To ensure that an appropriate amount of costs are capitalized, the amount of capitalized costs that are allocated to a specific project are limited to amounts using standards we developed. These standards consist of a percentage of the total development costs of a project and a percentage of the total gross lease amount payable under a specific lease. These standards are derived after considering the amounts that would be allocated if the personnel in the departments were working at full capacity. The use of these standards ensures that overhead costs attributable to downtime or to unsuccessful projects or leasing activities are not capitalized by us.

**Impairment of Real Estate Investments:** We evaluate our real estate investments upon occurrence of significant changes in the operations, but not less than annually, to assess whether any impairment indications are present that affect the recovery of the recorded value. If any real estate investment is considered to be impaired, a loss is provided to reduce the carrying value of the asset to its estimated fair value. We utilize the guidelines established under SFAS No. 144, *Accounting for the Impairment or Disposal of Long Lived Assets* ("SFAS 144"), to determine if impairment conditions exist. Under SFAS 144, we review the expected undiscounted cash flows of each property in our held for rental portfolio to determine if there are any indications of impairment of a property. The review of anticipated cash flows involves subjective assumptions of estimated occupancy and rental rates and ultimate residual value. In addition to reviewing anticipated cash flows, we assess other factors such as changes in business climate and legal factors that may affect the ultimate value of the property. These assumptions are subjective and the anticipated cash flows may not ultimately be achieved.

Real estate assets to be disposed of are reported at the lower of their carrying value amount or the fair value less estimated cost to sell.

**Acquisition of Real Estate Property:** In accordance with SFAS 141, we allocate the purchase price of acquired properties to net tangible and identified intangible assets based on their respective fair values.

The allocation to tangible assets (buildings, tenant improvements and land) is based upon management's determination of the value of the property as if it were vacant using discounted cash flow models similar to those used by independent appraisers. Factors considered by management include an estimate of carrying costs during the expected lease-up periods considering current market conditions, and costs to execute similar leases. The remaining purchase price is allocated among three categories of intangible assets consisting of the above or below market component of in-place leases, the value of in-place leases and the value of customer relationships.





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- The value allocable to the above or below market component of an acquired in-place lease is determined based upon the present value (using an interest rate which reflects the risks associated with the lease) of the difference between (i) the contractual amounts to be paid pursuant to the lease over its remaining term and (ii) management's estimate of the amounts that would be paid using current fair market rates over the remaining term of the lease. The amounts allocated to above market leases are included in deferred leasing and other costs in the balance sheet and below market leases are included in other liabilities in the balance sheet; both are amortized to rental income over the remaining terms of the respective leases.
- The total amount of intangible assets is further allocated to in-place lease values and to customer relationship values, based upon management's assessment of their respective values. These intangible assets are included in deferred leasing and other costs in the balance sheet and are depreciated over the remaining term of the existing lease, or the anticipated life of the customer relationship, as applicable.

**Valuation of Receivables:** We are subject to tenant defaults and bankruptcies that could affect the collection of outstanding receivables. In order to mitigate these risks, we perform in-house credit review and analysis on major existing tenants and all significant leases before they are executed. We have established the following procedures and policies to evaluate the collectibility of outstanding receivables and record allowances:

- We maintain a tenant "watch list" containing a list of significant tenants for which the payment of receivables and future rent may be at risk. Various factors such as late rent payments, lease or debt instrument defaults, and indications of a deteriorating financial position are considered when determining whether to include a tenant on the watch list.
- As a matter of policy, we reserve the entire receivable balance, including straight-line rent, of any tenant with an amount outstanding over 90 days.
- Straight-line rent receivables for any tenant on the watch list or any other tenant identified as a potential long-term risk, regardless of the status of rent receivables, are reviewed and reserved as necessary.

**Revenue Recognition on Construction Contracts:** We recognize income on construction contracts where we serve as a general contractor on the percentage of completion method. Using this method, profits are recorded on the basis of our estimates of the overall profit and percentage of completion of individual contracts. A portion of the estimated profits is accrued based upon our estimates of the percentage of completion of the

construction contract. Cumulative revenues recognized may be less or greater than cumulative costs and profits billed at any point in time during a contract's term. This revenue recognition method involves inherent risks relating to profit and cost estimates with those risks reduced through approval and monitoring processes.

With regard to critical accounting policies, management has discussed the following with the Audit Committee:

- Criteria for identifying and selecting;
- Methodology in applying; and
- Impact on the financial statements.

The Audit Committee has reviewed the critical accounting policies we identified.

## Liquidity and Capital Resources

### Sources of Liquidity

We expect to meet our liquidity requirements over the next twelve months, including payments of dividends and distributions as well as recurring capital expenditures relating to maintaining our current real estate assets, primarily through the following:

- working capital; and
- net cash provided by operating activities.

Although we typically do not use other sources of funds to pay for recurring capital expenditures on our current real estate investments, we may rely on the temporary use of borrowings or property disposition proceeds to fund such expenditures during periods of high leasing volume. We expect to meet long-term liquidity requirements, such as scheduled mortgage debt maturities, refinancing of long-term debt, preferred share redemptions, the retirement of unsecured notes and amounts outstanding under the unsecured credit facility, property acquisitions, financing of development activities and other non-recurring capital improvements, primarily from the following sources:

- issuance of additional notes;
- issuance of additional preferred shares;
- undistributed cash provided by operating activities, if any; and
- proceeds received from real estate dispositions.

### Rental Operations

We believe our principal source of liquidity, cash flows from Rental Operations, provides a stable source of cash to fund operational expenses. We believe this cash-based revenue stream is substantially aligned with revenue recognition (except for periodic straight-line rental income accruals and amortization of above or below market rents) as cash receipts from the leasing of rental properties are generally received in advance of or in a short time following the actual revenue recognition.





We are subject to risks of decreased occupancy through market conditions as well as tenant defaults and bankruptcies, and potential reduction in rental rates upon renewal or re-letting of properties, which would result in reduced cash flow from operations. However, we believe that these risks are mitigated by our strong market presence in most of our locations and the fact

that we perform in-house credit review and analysis on major tenants and all significant leases before they are executed.

#### *Credit Facility*

We had one unsecured line of credit available at December 31, 2005, summarized as follows (in thousands):

Description	Borrowing Capacity	Maturity Date	Interest Rate	Outstanding at December 31, 2005
Unsecured Line of Credit	\$500,000	January 2007	LIBOR + .60%	\$ 383,000

We use this line of credit to fund development activities, acquire additional rental properties and provide working capital.

The line of credit provides us with an option to obtain borrowings from financial institutions that participate in the line, at rates lower than the stated interest rate, subject to certain restrictions.

The line of credit contains various financial covenants that require us to meet defined levels of performance, including variable interest indebtedness, consolidated net worth, and debt-to-market capitalization. As of December 31, 2005, we were in compliance with all financial covenants under our line of credit.

In January 2006, we renewed our unsecured revolving credit facility. The new facility provides borrowing capacity up to \$1 billion and, subject to certain conditions, may be increased to \$1.3 billion. Under the new facility, which replaces the previous unsecured line of credit agreement, we reduced the interest rate by 7.5 basis points to LIBOR plus 52.5 basis points, increased the borrowing capacity by \$500 million and extended the maturity date to January 25, 2010.

#### *Debt and Equity Securities*

At December 31, 2005, we had on file with the SEC an effective shelf registration statement that permits us to sell up to an additional \$795.0 million of unsecured debt securities and an additional \$350.7 million of common and preferred stock. From time to time, we expect to issue additional securities under these registration statements to fund development and acquisition of additional rental properties and to fund the repayment of the credit facility and other long-term debt upon maturity.

The indenture governing our unsecured notes also requires us to comply with financial ratios and other covenants regarding our operations. At December 31, 2005, we were in compliance with all such covenants.

#### *Sale of Real Estate Assets*

We utilize sales of real estate assets as an additional source of liquidity. We pursue opportunities to sell real estate assets at favorable prices to capture value created by us as well as to improve the overall quality of our portfolio by recycling sale proceeds into new properties with greater value creation opportunities.

#### *Uses of Liquidity*

Our principal uses of liquidity include the following:

- Property investments;
- Recurring leasing/capital costs;
- Dividends and distributions to shareholders and unit-holders;
- Long-term debt maturities; and
- Other contractual obligations.

#### *Property Investments*

We evaluate development and acquisition opportunities based upon market outlook, supply and long-term growth potential.

#### *Recurring Expenditures*

One of our principal uses of our liquidity is to fund the development, acquisition and recurring leasing/capital expenditures of our real estate investments. The following is a summary of our recurring capital expenditures for the year ended December 31 (in thousands):

	2005	2004	2003
Tenant improvements	\$ 60,633	\$ 58,847	\$ 35,972
Leasing costs	33,175	27,777	20,932
Building improvements	15,232	21,029	19,544
Totals	<u>\$109,040</u>	<u>\$107,653</u>	<u>\$ 76,448</u>

Recurring capital expenditures remained relatively stable for 2005 as compared to 2004. Our lease renewal percentage remained steady in 2005 at 74.3% compared to 73.9% in 2004.

#### *Dividends and Distributions*

In order to qualify as a REIT for federal income tax purposes, we must currently distribute at least 90% of our taxable income to shareholders. We paid dividends per share of \$1.87, \$1.85 and \$1.83 for the years ended December 31, 2005, 2004 and 2003, respectively. We also paid a one-time special dividend of \$1.05 per share in 2005 as a result of the significant gain realized from the Industrial Portfolio Sale. We expect to continue to distribute taxable earnings to meet the requirements to maintain our REIT status. However, distributions are declared at the discretion of





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our board of directors and are subject to actual cash available for distribution, our financial condition, capital requirements and such other factors, as our board of directors deems relevant.

## *Debt Maturities*

Debt outstanding at December 31, 2005, totaled \$2.6 billion with a weighted average interest rate of 5.73% maturing at various

dates through 2028. We had \$2.4 billion of unsecured debt and \$167.3 million of secured debt outstanding at December 31, 2005. Scheduled principal amortization of such debt totaled \$46.7 million for the year ended December 31, 2005.

The following is a summary of the scheduled future amortization and maturities of our indebtedness at December 31, 2005 (in thousands except percentage data):

Year	Future Repayments			Weighted Average Interest Rate of Future Repayments
	Scheduled Amortization	Maturities	Total	
2006	\$ 7,094	\$ 390,249	\$ 397,343	5.49%
2007	6,620	597,615	604,235	5.08%
2008	5,639	268,968	274,607	4.90%
2009	4,926	275,000	279,926	7.38%
2010	4,316	175,000	179,316	5.39%
2011	4,497	175,000	179,497	6.95%
2012	3,172	200,000	203,172	5.87%
2013	2,879	150,000	152,879	4.65%
2014	2,799	272,112	274,911	6.27%
2015	926	—	926	6.80%
Thereafter	3,839	50,000	53,839	7.10%
	<u>\$ 46,707</u>	<u>\$ 2,553,944</u>	<u>\$ 2,600,651</u>	5.73%

## *Historical Cash Flows*

Cash and cash equivalents were \$26.7 million and \$5.6 million at December 31, 2005 and 2004, respectively. The following

highlights significant changes in net cash associated with our operating, investing and financing activities (in millions):

	Years Ended December 31,		
	2005	2004	2003
Net Cash Provided by Operating Activities	\$ 404.3	\$ 375.5	\$ 368.6
Net Cash Provided by (Used for) Investing Activities	328.1	(427.2)	(320.7)
Net Cash Provided by (Used for) Financing Activities	(711.2)	44.7	(52.7)

## *Operating Activities*

Cash flows from operating activities represents the cash necessary to meet normal operational requirements of our rental operations and merchant building activities. The receipt of rental income from rental operations continues to provide the primary source of our revenues and operating cash flows. In addition, we develop buildings with the intent to sell them, which provides another significant source of operating cash flow activity.

- During the year ended December 31, 2005, we incurred merchant building development costs of \$83.4 million, compared to \$43.1 million and \$55.6 million for the years ended December 31, 2004 and 2003. The difference is reflective of the increased activity in our held-for-sale pipeline. The pipeline of held-for-sale projects under construction as of December 31, 2005, has anticipated costs of \$286.7 million. In addition, we also acquired a building for \$6.0 million during the first quarter of 2005 on which

we made improvements of approximately \$7.5 million and sold in June 2005 for \$20.0 million.

- We sold ten merchant buildings in 2005 compared to six in 2004 and four in 2003, receiving net proceeds of \$113.0 million, \$72.7 million and \$50.1 million, respectively. After-tax gains of \$19.0 million, \$16.5 million and \$9.6 million, respectively, were recognized on these merchant building sales.

## *Investing Activities*

Investing activities are one of the primary uses of our funds. Development and acquisition activities typically generate additional rental revenues and provide cash flows for operational requirements. Highlights of significant cash uses are as follows:

- Sales of land and depreciated property provided \$1.1 billion in net proceeds in 2005, compared to \$178.3 million in 2004 and \$167.6 million in 2003. The Industrial Portfolio Sale provided \$955 million of





proceeds during the third quarter of 2005. We continue to dispose of non-strategic and older properties as part of our capital recycling program to fund acquisitions and new developments while improving the overall quality of our investment portfolio.

- Development costs increased to \$210.0 million for the year ended December 31, 2005, from \$145.6 and \$129.2 million for the years ended December 31, 2004 and 2003, respectively. Management anticipated this increase, as a commitment to development activity is part of our strategic plan for 2006.
- During 2005, we acquired \$285.3 million of real estate, compared to \$204.4 million in 2004 and \$201.8 million in 2003. The largest of the 2005 acquisitions was a five-building office complex in our Chicago market for \$257.0 million.
- In 2005, we acquired \$135.8 million of undeveloped land, compared to \$116.7 million in 2004 and \$32.9 million in 2003. These acquisitions provide us greater opportunities to use our development and construction expertise in the improving economic cycle.

#### *Financing Activities*

The following significant items highlight fluctuations in net cash provided by financing activities:

- In January 2005, we retired a \$65.0 million variable-rate term loan.
- In March 2005, we retired \$100.0 million of 6.875% senior unsecured debt that matured.
- In September 2005, we retired \$100.0 million of 7.375% corporate unsecured debt that matured.
- Throughout the third and fourth quarters of 2005, we repurchased and retired approximately 9.0 million of our common shares.
- In December 2005, we paid special dividends of \$143.8 million to common shareholders and special distributions of \$14.1 million to minority interest common unitholders, representing a one-time dividend of \$1.05 per share or per unit that was declared in order to maintain our compliance with the minimum distribution requirements for a REIT. The one-time special dividend was declared as a result of the significant gain realized as a result of the Industrial Portfolio Sale.

#### **Credit Ratings**

We are currently assigned investment grade corporate credit ratings on our senior unsecured notes from Fitch Ratings, Moody's Investor Service and Standard and Poor's Ratings Group. Currently, Fitch and Standard and Poor's have assigned

a rating of BBB+ and Moody's Investors has assigned a rating of Baa1 to our senior notes.

We also received investment grade credit ratings from the same rating agencies on our preferred stock. Fitch and Standard and Poor's have assigned a Preferred Stock rating of BBB and Moody's Investors has assigned a Preferred Stock rating of Baa2 to our preferred stock.

These senior notes and preferred stock ratings could change based upon, among other things, our results of operations and financial condition.

#### **Financial Instruments**

We are exposed to capital market risk, such as changes in interest rates. In order to manage the volatility relating to interest rate risk, we may enter into interest rate hedging arrangements from time to time. We do not utilize derivative financial instruments for trading or speculative purposes. We account for derivative instruments under Statement of Financial Accounting Standard No. 133, *Accounting for Derivative Instruments and Hedging Activities* ("SFAS 133"), as amended by SFAS No. 138, *Accounting for Certain Derivative Instruments and Certain Hedging Activities* ("SFAS 138").

In March 2005, we entered into \$300.0 million of cash flow hedges through forward-starting interest rate swaps to hedge interest rates on \$300.0 million of estimated debt offerings in 2006. The swaps qualify for hedge accounting under SFAS 133, as amended by SFAS 138, with any changes in fair value recorded in Accumulated Other Comprehensive Income ("OCI"). The market value of these interest rate swaps is dependent upon existing market interest rates, which change over time. At December 31, 2005, the estimated fair value of the swaps was a liability of approximately \$6.6 million. The effective rates of the swaps were higher than interest rates at December 31, 2005.

In August 2005, we entered into \$300.0 million of cash flow hedges through forward-starting interest rate swaps to hedge interest rates on \$300.0 million of estimated debt offerings in 2007. The swaps qualify for hedge accounting under SFAS 133, as amended by SFAS 138, with any changes in fair value recorded in OCI. At December 31, 2005, the fair value of these swaps was an asset of \$5.3 million. The effective rates of the swaps were lower than interest rates at December 31, 2005.

In June 2004, we simultaneously entered into three forward-starting interest rate swaps aggregating \$144.3 million, which effectively fixed the rate on financing expected in 2004 at 5.346%, plus our credit spread over the swap rate. The swaps qualified for hedge accounting under SFAS 133; therefore, changes in the fair value were recorded in OCI. In August 2004, we settled these three swaps when we issued \$250.0 million of unsecured notes with an effective interest rate of 6.33%, due in 2014. We paid \$6.85 million to unwind the swaps, which is amortized from OCI into interest expense over the life of the new 6.33% notes.





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

In December 2002, we simultaneously entered into two \$50 million forward-starting interest rate swaps as a hedge to effectively fix the rate on unsecured debt financings expected in 2003. Then again in February 2003, we simultaneously entered into two additional \$25 million forward-starting interest rate swaps as a hedge to effectively fix the rate on unsecured debt financings expected in 2003. All four swaps qualified for hedge accounting under SFAS 133; therefore, changes in fair value were recorded in OCI. In July 2003, we terminated the swaps for a net gain of \$643,000, which is included in other revenue in the Statements of Operations. The swaps were terminated because our capital needs were met through the issuance of the Series J Preferred Stock in lieu of the previously contemplated issuance of debt.

In May 2003, the Financial Accounting Standards Board ("FASB") issued SFAS No. 150, *Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity* ("SFAS 150"). SFAS 150 establishes standards for classifying and measuring as liabilities certain financial instruments that embody obligations of the issuer and have characteristics of both liabilities and equity. SFAS 150 was effective for all financial instruments created or modified after May 31, 2003, and otherwise was effective July 1, 2003. We consolidated the operations of one joint venture in our consolidated financial statements at December 31, 2005. This joint venture is partially owned by unaffiliated parties that have noncontrolling interests. SFAS 150 requires the disclosure of the estimated settlement value of these noncontrolling interests. As of December 31, 2005, the estimated settlement value of the noncontrolling interest in this consolidated joint venture was approximately \$1.1 million, as compared to the \$24,000 receivable reported in our financial statements for this joint venture.

## Off Balance Sheet Arrangements

### Investments in Unconsolidated Companies

We analyze our investments in joint ventures under FASB Interpretation No. 46(R), *Consolidation of Variable Interest Entities* ("FIN 46(R)"), to determine if the joint venture is a

variable interest entity and would require consolidation. To the extent that our joint ventures do not qualify as variable interest entities, we further assess under the guidelines of Emerging Issues Task Force ("EITF") No. 04-5, *Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights* ("EITF 04-5"); Statement of Position 78-9, *Accounting for Investments in Real Estate Ventures*; Accounting Research Bulletin No. 51, *Consolidated Financial Statements* and FASB No. 94, *Consolidation of All Majority-Owned Subsidiaries*, to determine if the venture should be consolidated.

In 2004, we announced a 50/50 joint venture agreement with a medical office developer to develop healthcare facilities. Under the terms of the agreement, we provide the project financing and construction services while our partner provides the business development, leasing and property management of the co-developed properties. We evaluated this partnership under FIN 46(R) and determined that this joint venture qualifies as a variable interest entity subject to consolidation. We are the primary beneficiary as determined under FIN 46(R) and fully consolidate the joint venture. At December 31, 2005, there were six properties under development with the joint venture. These properties total nearly 470,000 square feet and have an aggregate construction in-process balance of approximately \$14.9 million that is consolidated into our balance sheet.

We have equity interests ranging from 10% – 64% in unconsolidated companies that own and operate rental properties and hold land for development. The equity method of accounting is used for these investments in which we have the ability to exercise significant influence, but not control, over operating and financial policies. As a result, the assets and liabilities of these joint ventures are not included on our balance sheet.

Our investment in unconsolidated companies represents 5% of our total assets as of December 31, 2005. These investments provide several benefits to us, including increased market share, tenant and property diversification and an additional source of capital to fund real estate projects.

The following table presents summarized financial





information for unconsolidated companies for the years ended December 31, 2005 and 2004 (in thousands, except percentage data):

	Other Industrial Dugan Realty, LLC		Dugan Texas, LLC		Dugan Office, LLC		and Office Joint Ventures		Total	
	2005	2004	2005	2004	2005	2004	2005	2004	2005	2004
Land, buildings and tenant improvements, net	\$ 677,377	\$ 715,931	\$ 211,818	\$ 210,524	\$ 88,303	\$ 88,088	\$ 143,756	\$ 143,525	\$ 1,121,254	\$ 1,158,068
Land held for development	11,628	18,174	9,222	11,312	4,293	4,293	22,793	16,394	47,936	50,173
Other assets	35,959	29,738	17,347	13,223	4,116	3,256	15,662	15,973	73,084	62,190
	\$ 724,964	\$ 763,843	\$ 238,387	\$ 235,059	\$ 96,712	\$ 95,637	\$ 182,211	\$ 175,892	\$ 1,242,274	\$ 1,270,431
Property indebtedness	\$ 360,290	\$ 412,179	\$ 17,999	\$ 18,000	\$ 67,362	\$ 68,393	\$ 69,541	\$ 72,369	\$ 515,192	\$ 570,941
Other liabilities	23,903	18,921	10,436	8,791	2,793	3,318	21,093	20,347	58,225	51,377
	384,193	431,100	28,435	26,791	70,155	71,711	90,634	92,716	573,417	622,318
Owners' equity	340,771	332,743	209,952	208,268	26,557	23,926	91,577	83,176	668,857	648,113
	\$ 724,964	\$ 763,843	\$ 238,387	\$ 235,059	\$ 96,712	\$ 95,637	\$ 182,211	\$ 175,892	\$ 1,242,274	\$ 1,270,431
Rental income	\$ 94,045	\$ 98,020	\$ 30,481	\$ 29,860	\$ 11,423	\$ 14,776	\$ 27,498	\$ 25,147	\$ 163,447	\$ 167,803
Net income (loss)	\$ 41,678	\$ 23,398	\$ 12,351	\$ 13,039	\$ (1,517)	\$ 252	\$ 5,049	\$ 3,449	\$ 57,561	\$ 40,138
Total square feet	21,436	22,763	6,255	6,018	652	652	4,573	4,465	32,916	33,898
Percent leased	95.9%	95.0%	90.7%	95.3%	70.2%	69.7%	94.0%	94.2%	94.2%	94.4%
Company ownership percentage	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%	10.0%- 64.0%	10.0%- 64.0%		

#### Off Balance Sheet Arrangements

We do not have any relationships with unconsolidated entities or financial partnerships, such as "special purpose entities," which are generally established for the purpose of facilitating off-balance sheet arrangements or other specific purposes.

#### Contractual Obligations

At December 31, 2005, we are subject to certain contractual payment obligations as described in the table and notes below (in thousands):

Contractual Obligations	Payments due by Period						
	Total	2006	2007	2008	2009	2010	Thereafter
Long-term debt <sup>(1)</sup>	\$ 2,610,618	\$ 296,635	\$ 326,205	\$ 361,330	\$ 355,506	\$ 234,114	\$ 1,036,828
Line of credit <sup>(2)</sup>	404,166	18,499	385,667	—	—	—	—
Share of mortgage debt of unconsolidated joint ventures <sup>(3)</sup>	291,172	30,187	60,112	33,551	55,826	106,915	4,581
Ground leases	8,973	346	364	360	343	336	7,224
Operating leases	1,460	622	317	297	191	33	—
Development and construction backlog costs <sup>(4)</sup>	360,216	333,049	27,167	—	—	—	—
Future land acquisitions <sup>(5)</sup>	69,269	59,526	6,983	2,760	—	—	—
Service contracts <sup>(6)</sup>	33,803	9,028	8,854	8,224	7,697	—	—
Other <sup>(7)</sup>	194,110	194,110	—	—	—	—	—
Total Contractual Obligations	\$ 3,973,787	\$ 942,002	\$ 815,669	\$ 406,522	\$ 419,563	\$ 341,398	\$ 1,048,633

- (1) Our long-term debt consists of both secured and unsecured debt and includes both principal and interest. Interest expense for variable rate debt was calculated using the interest rate at December 31, 2005.
- (2) Our unsecured line of credit was originally scheduled to mature in 2007. In January 2006, the maturity date was extended to January 2010.
- (3) Our share of unconsolidated mortgage debt includes both principal and interest. Interest expense for variable rate debt was calculated using the interest rate at December 31, 2005.
- (4) Represents estimated remaining costs on the completion of held-for-rental, held-for-sale and third party construction projects.
- (5) These land acquisitions are subject to the completion of due diligence requirements, resolution of certain contingencies and completion of certain contingencies and completion of customary closing conditions. If we were to terminate these contracts, we would forfeit our total escrow amount of \$320,000 and would have no further contractual obligations.
- (6) Service contracts defined as those which cover periods greater than one year and are not cancelable without cause by either party.
- (7) Represents the contracted purchase price of a portfolio of buildings that we expect to acquire in 2006.





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

## Related Party Transactions

We provide property management, leasing, construction and other tenant related services to unconsolidated companies in which we have equity interests. For the years ended December 31, 2005, 2004 and 2003, respectively, we received from these unconsolidated companies management fees of \$4.8 million, \$4.9 million and \$4.9 million, leasing fees of \$4.3 million, \$2.6 million and \$2.3 million and construction and development fees of \$2.0 million, \$1.5 million and \$1.4 million. We recorded these fees at market rates and eliminated our ownership percentages of these fees in the consolidated financial statements.

## Commitments and Contingencies

In October 2000, we sold or contributed industrial properties and undeveloped land with a fair value of \$487 million to a joint venture (Dugan Realty LLC) in which we have a 50% interest and recognized a net gain of \$35.2 million. This transaction expanded an existing joint venture with an institutional real estate investor. As a result of the total transactions, we received \$363.9 million of proceeds. The joint venture partially financed this transaction with \$350 million of secured mortgage debt, the repayment of which we directly or indirectly guaranteed. The guarantee associated with \$260 million of such debt expired in December 2003 without us being required to satisfy the guarantee. The remaining \$90 million of such debt is still guaranteed by us. In connection with this transaction, the joint venture partners were given an option to put up to a \$50 million interest in the joint venture to us in exchange for our common stock or cash (at our option), subject to certain timing and other restrictions. As a result of this put option, we deferred \$10.2 million of gain on sale of depreciated property and recorded a \$50 million liability.

We have guaranteed the repayment of \$12.3 million of economic development bonds issued by various municipalities in connection with certain commercial developments. We will be required to make payments under our guarantees to the extent that incremental taxes from specified developments are not sufficient to pay the bond debt service. Management does not believe that it is probable that we will be required to make any significant payments in satisfaction of these guarantees.

We also have guaranteed the repayment of a \$2 million mortgage loan encumbering the real estate of one of our unconsolidated joint ventures. At December 31, 2005, the outstanding balance on this loan was approximately \$1.2 million. Management believes that the value of the real estate exceeds the loan balance and that we will not be required to satisfy this guarantee.

We evaluated all applicable guarantees under FASB Interpretation 45 ("FIN 45") in order to determine whether there is a need to recognize a liability for the obligations under the guarantees. Based upon our review, no liability was recorded at December 31, 2005.

We have entered into agreements, subject to the completion of due diligence requirements, resolution of certain contingencies and completion of customary closing conditions, for the future acquisition of land totaling \$65.0 million. We also have entered into an agreement to acquire an 18 building portfolio for approximately \$194.1 million, which is expected to close in 2006.

We renewed all of our major insurance policies in 2005. These policies include coverage for acts of terrorism for our properties. We believe that this insurance provides adequate coverage against normal insurance risks and that any loss experienced would not have a significant impact on our liquidity, financial position, or results of operations.

We are subject to various legal proceedings and claims that arise in the ordinary course of business. In the opinion of management, the amount of any ultimate liability with respect to these actions will not materially affect our consolidated financial statements or results of operations.

## Recent Accounting Pronouncements

In December 2004, FASB issued SFAS No. 123 (R), *Share-Based Payment*, which is a revision of SFAS No. 123, *Accounting for Stock Based Compensation*. In April 2005, the SEC delayed the effective date on SFAS No. 123 (R) from July 2005 to January 2006. We have completed our preliminary evaluation of the impact of SFAS No. 123 (R) and have determined that the cumulative effect of a change in accounting principle will be insignificant to our results of operations. We have selected the modified-prospective method for the adoption of SFAS No. 123 (R).

In March 2005, FASB Interpretation No. 47, *Accounting for Conditional Asset Retirement Obligations* ("FIN 47"), was issued for all fiscal years ending after December 15, 2005. This is an interpretation of SFAS No. 143, *Accounting for Asset Retirement Obligation*. Upon evaluation, we have determined that the adoption of FIN 47 did not have a material impact on our financial statements.

In June 2005, FASB ratified the consensus reached in Emerging Issues Task Force ("EITF") No. 04-5, *Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights* ("EITF 04-5"). EITF 04-5 is effective for all newly formed limited partnerships after the consensus was ratified and as of January 2006 for all pre-existing limited partnership agreements. This consensus applies to limited partnerships or similar entities, such as limited liability companies that have governing provisions that are the functional equivalent of a limited partnership. We have evaluated the ownership structure of our existing investments in unconsolidated companies and determined that we do not exercise control over any unconsolidated ventures as defined by EITF 04-5.





# Management's Report on Internal Control

We, as management of Duke Realty Corporation and its subsidiaries ("Duke"), are responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended). Pursuant to the rules and regulations of the Securities and Exchange Commission, internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles and includes those policies and procedure that:

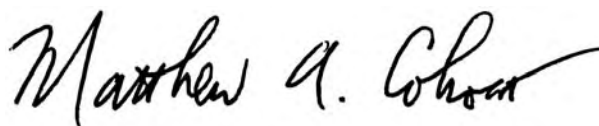
- Pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of assets of the company;
- Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and
- Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

Management has evaluated the effectiveness of its internal control over financial reporting as of December 31, 2005, based on the control criteria established in a report entitled Internal Control – Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on such evaluation, we have concluded that, as of December 31, 2005, our internal control over financial reporting is effective based on these criteria.

The independent registered public accounting firm of KPMG LLP, as auditors of Duke's consolidated financial statements, has issued an attestation report on management's assessment of Duke's internal control over financial reporting.



Dennis D. Oklak  
Chairman and Chief Executive Officer  
(Principal Executive Officer)



Matthew A. Cohoat  
Executive Vice President and Chief Financial Officer  
(Principal Financial Officer)





# Report of Independent Registered Public Accounting Firm

## **The Shareholders and Directors of Duke Realty Corporation:**

We have audited the consolidated balance sheets of Duke Realty Corporation and Subsidiaries (the “Company”) as of December 31, 2005 and 2004, and the related consolidated statements of operations, cash flows and shareholders’ equity for each of the years in the three-year period ended December 31, 2005. These consolidated financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Duke Realty Corporation and Subsidiaries as of December 31, 2005 and 2004, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2005, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Duke Realty Corporation and Subsidiaries’ internal control over financial reporting as of December 31, 2005, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 3, 2006, expressed an unqualified opinion on management’s assessment of, and the effective operation of, internal control over financial reporting.

**KPMG LLP**

Indianapolis, Indiana  
March 3, 2006





# Report of Independent Registered Public Accounting Firm

## **The Shareholders and Directors of Duke Realty Corporation:**

We have audited management's assessment, included in the accompanying Management's Report on Internal Control that Duke Realty Corporation and Subsidiaries (the "Company") maintained effective internal control over financial reporting as of December 31, 2005, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Duke Realty Corporation and Subsidiaries' management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

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

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

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

In our opinion, management's assessment that Duke Realty Corporation and Subsidiaries maintained effective internal control over financial reporting as of December 31, 2005, is fairly stated, in all material respects, based on criteria established in Internal Control-Integrated Framework issued by COSO. Also, in our opinion, Duke Realty Corporation and Subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2005, based on criteria established in Internal Control-Integrated Framework issued by COSO.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Duke Realty Corporation and Subsidiaries as of December 31, 2005 and 2004, and the related consolidated statements of operations, cash flows and shareholders' equity for each of the years in the three-year period ended December 31, 2005, and our report dated March 3, 2006, expressed an unqualified opinion on those consolidated financial statements.

**KPMG LLP**

Indianapolis, Indiana

March 3, 2006





# Consolidated Balance Sheets

(in thousands, except per share amounts)

As of December 31	2005	2004
<b>Assets</b>		
Real estate investments:		
Land and improvements	\$ 675,050	\$ 710,379
Buildings and tenant improvements	4,156,456	4,666,715
Construction in progress	227,066	109,788
Investments in unconsolidated companies	301,322	287,554
Land held for development	429,270	393,650
	<u>5,789,164</u>	<u>6,168,086</u>
Accumulated depreciation	(754,742)	(788,900)
Net real estate investments	5,034,422	5,379,186
Cash and cash equivalents	26,732	5,589
Accounts receivable, net of allowance of \$1,093 and \$1,238	31,342	17,127
Straight-line rent receivable, net of allowance of \$1,538 and \$1,646	95,948	89,497
Receivables on construction contracts, including retentions	50,035	59,342
Deferred financing costs, net of accumulated amortization of \$14,113 and \$9,006	27,118	31,924
Deferred leasing and other costs, net of accumulated amortization of \$112,246 and \$88,888	227,648	203,882
Escrow deposits and other assets	154,315	110,096
	<u>\$ 5,647,560</u>	<u>\$ 5,896,643</u>
<b>Liabilities and Shareholders' Equity</b>		
Indebtedness:		
Secured debt	\$ 167,255	\$ 203,081
Unsecured notes	2,050,396	2,315,623
Unsecured line of credit	383,000	—
	<u>2,600,651</u>	<u>2,518,704</u>
Construction payables and amounts due subcontractors, including retentions	93,137	67,740
Accounts payable	781	526
Accrued expenses:		
Real estate taxes	60,883	55,748
Interest	33,022	36,531
Other	54,878	51,514
Other liabilities	133,920	105,071
Tenant security deposits and prepaid rents	34,924	39,827
Total liabilities	<u>3,012,196</u>	<u>2,875,661</u>
Minority interest	<u>182,566</u>	<u>195,113</u>
Shareholders' equity:		
Preferred shares (\$.01 par value); 5,000 shares authorized; 2,365 shares issued and outstanding	657,250	657,250
Common shares (\$.01 par value); 250,000 shares authorized; 134,697 and 142,894 shares issued and outstanding	1,347	1,429
Additional paid-in capital	2,266,204	2,538,461
Accumulated other comprehensive loss	(7,118)	(6,547)
Distributions in excess of net income	(464,885)	(364,724)
Total shareholders' equity	<u>2,452,798</u>	<u>2,825,869</u>
	<u>\$ 5,647,560</u>	<u>\$ 5,896,643</u>

See accompanying Notes to Consolidated Financial Statements.





# Consolidated Statements of Operations

(in thousands, except per share amounts)

For the Years Ended December 31	2005	2004	2003
<b>Rental Operations</b>			
Revenues:			
Rental income from continuing operations	\$ 676,634	\$ 619,569	\$ 560,715
Equity in earnings of unconsolidated companies	29,549	21,586	23,688
	<u>706,183</u>	<u>641,155</u>	<u>584,403</u>
Operating expenses:			
Rental expenses	158,013	135,049	121,436
Real estate taxes	82,751	70,027	62,825
Interest expense	120,369	109,923	100,664
Depreciation and amortization	226,503	181,443	151,000
	<u>587,636</u>	<u>496,442</u>	<u>435,925</u>
Earnings from continuing rental operations	<u>118,547</u>	<u>144,713</u>	<u>148,478</u>
<b>Service Operations</b>			
Revenues:			
General contractor gross revenue	380,173	357,133	286,689
General contractor costs	(348,263)	(329,545)	(259,930)
Net general contractor revenue	31,910	27,588	26,759
Property management, maintenance and leasing fees	15,925	15,000	14,731
Construction management and development activity income	30,479	25,002	15,486
Other income	3,627	3,213	2,480
Total revenue	81,941	70,803	59,456
Operating expenses	40,922	46,382	37,635
Earnings from service operations	41,019	24,421	21,821
General and administrative expense	(27,835)	(26,278)	(21,980)
Operating income	131,731	142,856	148,319
<b>Other Income (Expense)</b>			
Interest income	5,844	5,213	3,556
Earnings from sale of land, depreciable property and ownership interests in unconsolidated companies, net of impairment adjustments	14,201	10,202	15,752
Other expenses	(1,207)	(567)	(734)
Other minority interest in earnings of subsidiaries	(1,438)	(1,253)	(586)
Minority interest in earnings of common unitholders	(9,378)	(11,619)	(12,429)
Minority interest in earnings of preferred unitholders	—	—	(1,904)
Income from continuing operations	139,753	144,832	151,974
Discontinued operations:			
Net income from discontinued operations, net of minority interest	11,616	19,971	35,506
Gain on sale of discontinued operations, net of impairment adjustments and minority interest	204,293	23,898	11,752
Income from discontinued operations	215,909	43,869	47,258
Net income	355,662	188,701	199,232
Dividends on preferred shares	(46,479)	(33,777)	(37,321)
Adjustments for redemption of preferred shares	—	(3,645)	—
Net income available for common shareholders	<u>\$ 309,183</u>	<u>\$ 151,279</u>	<u>\$ 161,911</u>
Basic net income per common share:			
Continuing operations	\$ .66	\$ .76	\$ .84
Discontinued operations	1.53	.31	.35
Total	<u>\$ 2.19</u>	<u>\$ 1.07</u>	<u>\$ 1.19</u>
Diluted net income per common share:			
Continuing operations	\$ .65	\$ .75	\$ .84
Discontinued operations	1.52	.31	.35
Total	<u>\$ 2.17</u>	<u>\$ 1.06</u>	<u>\$ 1.19</u>
Weighted average number of common shares outstanding	141,508	141,379	135,595
Weighted average number of common and dilutive potential common shares	155,877	157,062	151,141

See accompanying Notes to Consolidated Financial Statements.





# Consolidated Statements of Cash Flows

(in thousands)

For the Years Ended December 31	2005	2004	2003
Cash flows from operating activities:			
Net income	\$ 355,662	\$ 188,701	\$ 199,232
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation of buildings and tenant improvements	204,377	189,119	168,959
Amortization of deferred leasing and other costs	49,793	39,463	27,275
Amortization of deferred financing costs	6,154	4,904	3,626
Minority interest in earnings	31,493	17,184	20,036
Straight-line rent adjustment	(22,519)	(22,436)	(22,387)
Earnings from land and depreciated property sales	(238,060)	(36,449)	(28,776)
Build-for-sale operations, net	(6,295)	(41)	(20,899)
Construction contracts, net	16,196	(11,047)	(3,210)
Other accrued revenues and expenses, net	10,513	(4,306)	15,989
Operating distributions received in excess of (less than) equity in earnings from unconsolidated companies	(3,055)	10,447	8,783
<b>Net cash provided by operating activities</b>	<b>404,259</b>	<b>375,539</b>	<b>368,628</b>
Cash flows from investing activities:			
Development of real estate investments	(209,990)	(145,629)	(129,199)
Acquisition of real estate investments	(285,342)	(204,361)	(201,819)
Acquisition of land held for development and infrastructure costs	(135,771)	(113,433)	(32,944)
Recurring tenant improvements	(60,633)	(58,847)	(35,972)
Recurring leasing costs	(33,175)	(27,777)	(20,932)
Recurring building improvements	(15,232)	(21,029)	(19,544)
Other deferred leasing costs	(19,425)	(16,386)	(17,167)
Other deferred costs and other assets	(15,438)	(15,055)	(25,264)
Proceeds from land and depreciated property sales, net	1,134,667	178,301	167,626
Advances to unconsolidated companies	(31,599)	(3,033)	(5,481)
<b>Net cash provided by (used for) investing activities</b>	<b>328,062</b>	<b>(427,249)</b>	<b>(320,696)</b>
Cash flows from financing activities:			
Payments for repurchases of common shares	(287,703)	—	—
Proceeds from issuance of common shares, net	3,945	12,259	14,026
Proceeds from issuance of preferred shares, net	—	338,360	96,700
Payments for redemption of preferred shares	—	(102,652)	(20)
Redemption of warrants	—	(2,881)	(4,692)
Redemption of limited partner units	(2,129)	—	—
Proceeds from unsecured debt issuance	400,000	690,000	425,000
Payments on unsecured debt	(665,000)	(150,000)	(175,000)
Proceeds from debt refinancing	—	—	38,340
Proceeds from issuance of secured debt	—	—	40,000
Payments on secured indebtedness including principal amortization	(46,675)	(39,430)	(143,542)
Borrowings (payments) on lines of credit, net	383,000	(351,000)	46,105
Payment for redemption of preferred units	—	—	(65,000)
Distributions to common shareholders	(264,980)	(261,061)	(248,100)
Distributions to common shareholders – special dividends	(143,836)	—	—
Distributions to preferred shareholders	(46,479)	(31,828)	(37,321)
Distributions to preferred unitholders	—	—	(4,859)
Distributions to minority interest	(26,653)	(26,941)	(28,484)
Distributions to minority interest – special distributions	(14,069)	—	—
Deferred financing costs	(599)	(30,159)	(5,867)
<b>Net cash provided by (used for) financing activities</b>	<b>(711,178)</b>	<b>44,667</b>	<b>(52,714)</b>
<b>Net increase (decrease) in cash and cash equivalents</b>	<b>21,143</b>	<b>(7,043)</b>	<b>(4,782)</b>
Cash and cash equivalents at beginning of year	5,589	12,632	17,414
Cash and cash equivalents at end of year	<b>\$ 26,732</b>	<b>\$ 5,589</b>	<b>\$ 12,632</b>
Other non-cash items:			
Assumption of debt for real estate acquisitions	\$ 11,743	\$ 29,854	\$ —
Contributions of property to unconsolidated companies	\$ —	\$ —	\$ 5,009
Conversion of Limited Partner units to common shares	\$ 18,085	\$ 25,376	\$ 26,546
Conversion of Series D preferred shares to common shares	\$ —	\$ 130,665	\$ —
Issuance of Limited Partner Units for real estate acquisitions	\$ —	\$ 7,575	\$ 3,187
Common shares repurchased and retired, not settled	\$ 9,357	\$ —	\$ —
Issuance of Limited Partner Units for acquisition of minority interest	\$ 15,000	\$ —	\$ —
Acquisition of partners' interest in unconsolidated companies	\$ —	\$ —	\$ 20,630

See accompanying Notes to Consolidated Financial Statements.





# Consolidated Statements of Shareholders' Equity

(in thousands, except per share data)

	Preferred Stock	Common Stock	Additional Paid-in Capital	Accumulated Other Compre- hensive Income	Distributions In Excess of Net Income	Total
<b>Balance at December 31, 2002</b>	\$ 440,889	\$ 1,350	\$ 2,345,961	\$(2,111)	\$(168,753)	\$ 2,617,336
Comprehensive Income:						
Net income	—	—	—	—	199,232	199,232
Distributions to preferred shareholders	—	—	—	—	(37,321)	(37,321)
Gains (losses) on derivative instruments	—	—	—	2,111	—	2,111
Comprehensive income available for common shareholders						164,022
Issuance of common shares	—	7	14,253	—	—	14,260
Issuance of preferred shares	100,000	—	(3,300)	—	—	96,700
Acquisition of minority interest	—	9	26,537	—	—	26,546
Repurchase of Series D Preferred shares	(20)	—	—	—	—	(20)
Conversion of Series D Preferred shares	(361)	—	361	—	—	—
Redemption of Warrants	—	—	(4,692)	—	—	(4,692)
Tax benefits from employee stock plans	—	—	542	—	—	542
FASB 123 compensation expense	—	—	155	—	—	155
Distributions to common shareholders (\$1.83 per share)	—	—	—	—	(248,100)	(248,100)
<b>Balance at December 31, 2003</b>	\$ 540,508	\$ 1,366	\$ 2,379,817	\$ —	\$(254,942)	\$ 2,666,749
Comprehensive Income:						
Net income	—	—	—	—	188,701	188,701
Distributions to preferred shareholders	—	—	—	—	(33,777)	(33,777)
Adjustment for carrying value of preferred stock redemption	—	—	3,645	—	(3,645)	—
Gains (losses) on derivative instruments	—	—	—	(6,547)	—	(6,547)
Comprehensive income available for common shareholders						148,377
Issuance of common shares	—	6	12,361	—	—	12,367
Issuance of preferred shares	350,000	—	(11,688)	—	—	338,312
Acquisition of minority interest	—	8	25,368	—	—	25,376
Conversion of Series D Preferred Shares	(130,665)	49	130,616	—	—	—
Redemption of Series D Preferred Shares	(2,593)	—	(30)	—	—	(2,623)
Redemption of Series E Preferred Shares	(100,000)	—	(29)	—	—	(100,029)
Exercise of Warrants	—	—	(2,881)	—	—	(2,881)
Tax benefits from employee stock plans	—	—	770	—	—	770
FASB 123 compensation expense	—	—	512	—	—	512
Distributions to common shareholders (\$1.85 per share)	—	—	—	—	(261,061)	(261,061)
<b>Balance at December 31, 2004</b>	\$ 657,250	\$ 1,429	\$ 2,538,461	\$(6,547)	\$(364,724)	\$ 2,825,869
Comprehensive Income:						
Net income	—	—	—	—	355,662	355,662
Distributions to preferred shareholders	—	—	—	—	(46,479)	(46,479)
Gains (losses) on derivative instruments	—	—	—	(571)	—	(571)
Comprehensive income available for common shareholders						308,612
Issuance of common shares	—	2	4,141	—	—	4,143
Acquisition of minority interest	—	6	18,079	—	—	18,085
Tax benefits from employee stock plans	—	—	245	—	—	245
FASB 123 compensation expense	—	—	2,032	—	—	2,032
Dividends on long-term compensation plans	—	—	216	—	(216)	—
Retirement of common shares	—	(90)	(296,970)	—	—	(297,060)
Distributions to common shareholders (\$1.87 per share)	—	—	—	—	(265,076)	(265,076)
Distributions to common shareholders – Special (\$1.05 per share)	—	—	—	—	(144,052)	(144,052)
<b>Balance at December 31, 2005</b>	\$ 657,250	\$ 1,347	\$ 2,266,204	\$(7,118)	\$(464,885)	\$ 2,452,798

See accompanying Notes to Consolidated Financial Statements.





# Notes to Consolidated Financial Statements

## 1—The Company

Our rental operations are conducted through Duke Realty Limited Partnership (“DRLP”). We owned approximately 91.0% of the common partnership interests of DRLP (“Units”) at December 31, 2005. The remaining Units in DRLP are redeemable for shares of our common stock. We conduct Service Operations through Duke Realty Services LLC (“DRS”) and Duke Realty Services Limited Partnership (“DRSLP”), of which we are the sole general partner and of which DRLP is the sole limited partner. We also conduct Service Operations through Duke Construction Limited Partnership (“DCLP”), which is effectively 100% owned by DRLP. The consolidated financial statements include our accounts and our majority-owned or controlled subsidiaries.

## 2—Summary of Significant Accounting Policies

### Principles of Consolidation

The consolidated financial statements include our accounts and our controlled subsidiaries. The equity interests in these controlled subsidiaries not owned by us are reflected as minority interests in the consolidated financial statements. All significant intercompany balances and transactions have been eliminated in the consolidated financial statements. Investments in entities that we do not control through majority voting interest or where the other owner has substantial participating rights are not consolidated and are reflected as investments in unconsolidated companies under the equity method of reporting.

### Reclassifications

Certain 2004 and 2003 balances have been reclassified to conform to the 2005 presentation.

### Real Estate Investments

Rental real property, including land, land improvements, buildings and building improvements, are included in real estate investments and are generally stated at cost. Buildings and land improvements are depreciated on the straight-line method over their estimated life not to exceed 40 and 15 years, respectively, and tenant improvement costs are depreciated using the straight-line method over the term of the related lease.

Direct and certain indirect costs clearly associated with and incremental to the development, construction, leasing or expansion of real estate investments are capitalized as a cost of the property. In addition, all leasing commissions paid to third parties for new leases or lease renewals are capitalized. We capitalize a portion of our indirect costs associated with our construction/development and leasing efforts. In assessing the amount of direct and indirect costs to be capitalized, allocations are made based on estimates of the actual amount of time spent in each activity. We do not capitalize any costs attributable to downtime or to unsuccessful projects of leasing activities.

Within our Rental Operations, direct and indirect costs are capitalized under the guidelines of Statement of Financial

Accounting Standard (“SFAS”) No. 67, *Accounting for Costs and Initial Rental Operations of Real Estate Projects* (“SFAS 67”), and interest costs are capitalized under the guidelines of SFAS No. 34, *Capitalization of Interest Cost* (“SFAS 34”). The Company capitalizes these project costs associated with the initial construction of a property up to the time the property is substantially complete and ready for its intended use. In addition, the Company capitalizes costs, including real estate taxes, insurance, and utilities, that have been allocated to vacant space based on the square footage of the portion of the building not held available for immediate occupancy during the extended lease-up periods after construction of the building shell has been completed if costs are being incurred to ready the vacant space for its intended use. If costs and activities incurred to ready the vacant space cease, then cost capitalization is also discontinued until such activities are resumed. Once necessary work has been completed on a vacant space, project costs are no longer capitalized.

We cease capitalization of all project costs on extended lease-up periods after the shorter of a one-year period after the completion of the building shell or when the property attains 90% occupancy. Tenant improvement costs are generally not incurred on vacant space until a lease is signed and specific improvements are identified in the lease.

Construction in process and land held for development are included in real estate investments and are stated at cost. Real estate investments also include our equity interests in unconsolidated joint ventures that own and operate rental properties and hold land for development. We analyze our investments in joint ventures under Financial Accounting Standards Board (“FASB”) Interpretation No. 46(R), *Consolidation of Variable Interest Entities*, to determine if the joint venture is considered a variable interest entity and would require consolidation. The equity method of accounting is used for these investments in which we have the ability to exercise significant influence, but not control, over operating and financial policies. Any difference between the carrying amount of these investments and the underlying equity in net assets is amortized to equity in earnings of unconsolidated companies over the depreciable life of the property, generally 40 years. Distributions received from unconsolidated joint ventures are generated from the operations of the properties in the joint venture and are reflected as an operating activity in our Consolidated Statement of Cash Flows.

In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long Lived Assets* (“SFAS 144”), properties held for rental are individually evaluated for impairment when conditions exist which may indicate that it is probable that the sum of expected future cash flows (on an undiscounted basis) from a rental property over its anticipated holding period is less than its historical net cost basis. Upon determination that a permanent impairment has occurred, a loss is recorded to reduce the net book value of that property to its





fair market value. Real properties to be disposed of are reported at the lower of net historical cost basis or the estimated fair market value, less the estimated costs to sell. Once a property is designated as held for disposal, no further depreciation expense is recorded.

In accordance with SFAS No. 141, *Business Combinations* ("SFAS 141"), we allocate the purchase price of acquired properties to net tangible and identified intangible assets based on their respective fair values. The allocation to tangible assets (buildings, tenant improvements and land) is based upon management's determination of the value of the property as if it were vacant using discounted cash flow models similar to those used by independent appraisers. Factors considered by management include an estimate of carrying costs during the expected lease-up periods considering current market conditions, and costs to execute similar leases. The remaining purchase price is allocated among three categories of intangible assets consisting of the above or below market component of in-place leases, the value of in-place leases and the value of customer relationships.

The value allocable to the above or below market component of an acquired in-place lease is determined based upon the present value (using a discount rate which reflects the risks associated with the acquired leases) of the difference between (i) the contractual amounts to be paid pursuant to the lease over its remaining term and (ii) management's estimate of the amounts that would be paid using fair market rates over the remaining term of the lease. The amounts allocated to above market leases are included in deferred leasing and other costs in the balance sheet and below market leases are included in other liabilities in the balance sheet; both are amortized to rental income over the remaining terms of the respective leases.

The total amount of intangible assets is further allocated to in-place lease values and to customer relationship values based upon management's assessment of their respective values. These intangible assets are included in deferred leasing and other costs in the balance sheet and are depreciated over the remaining term of the existing lease, or the anticipated life of the customer relationship, as applicable.

#### **Cash Equivalents**

Investments with a maturity of three months or less when purchased are classified as cash equivalents.

#### **Valuation of Receivables**

We reserve the entire receivable balance, including straight-line rent, of any tenant with an amount outstanding over 90 days. Straight-line rent receivables for any tenant with long-term risk, regardless of the status of rent receivables, are reviewed and reserved as necessary.

#### **Deferred Costs**

Costs incurred in connection with obtaining financing are amortized to interest expense on the straight-line method, which approximates a constant spread over the term of the related loan. All direct and indirect costs, including estimated internal costs, associated with the leasing of real estate investments owned by us are capitalized and amortized over the term of the related lease. We account for lease incentive costs, which are payments made to or on behalf of a tenant, as an incentive to sign the lease, in accordance with FASB Technical Bulletin ("FTB") 88-1, *Issues Relating to Accounting for Leases*. These costs are capitalized in deferred leasing costs and amortized on a straight-line basis over the respective lease terms as a reduction of rental revenues. We include as lease incentives amounts funded to construct tenant improvements owned by the tenant. Unamortized costs are charged to expense upon the early termination of the lease or upon early payment of the financing.

#### **Revenues**

##### *Rental Operations*

The timing of revenue recognition under an operating lease is determined based upon ownership of the tenant improvements. If we are the owner of the tenant improvements, revenue recognition commences after the improvements are completed and the tenant takes possession or control of the space. In contrast, if we determine that the tenant allowances we are funding are lease incentives, then we commence revenue recognition when possession or control of the space is turned over to the tenant. Rental income from leases with scheduled rental increases during their terms is recognized on a straight-line basis.

##### *Service Operations*

Management fees are based on a percentage of rental receipts of properties managed and are recognized as the rental receipts are collected. Maintenance fees are based upon established hourly rates and are recognized as the services are performed. Construction management and development fees represent fee based third party contracts and are recognized as earned based on the terms of the contract, which approximates the percentage of completion method.

We recognize income on construction contracts where we serve as a general contractor on the percentage of completion method. Using this method, profits are recorded based on our estimates of the percentage of completion of individual contracts, commencing when the work performed under the contracts reach a point where the final costs can be estimated with reasonable accuracy. The percentage of completion estimates are based on a comparison of the contract expenditures incurred to the estimated final costs. Changes in job performance, job conditions and estimated profitability may result in revisions to costs and income and are recognized in the period in which the revisions are determined.





# Notes to Consolidated Financial Statements

## Property Sales

Gains from sales of depreciated property are recognized in accordance with SFAS No. 66, *Accounting for Sales of Real Estate* ("SFAS 66"), and are included in earnings from sales of land and depreciable property dispositions, net of any impairment adjustments, in the Consolidated Statements of Operations if identified as held-for-sale prior to adoption of SFAS 144 and in discontinued operations if identified as held-for-sale after adoption of SFAS 144. The proceeds from the sale of these held-for-rental properties are classified in the investing activities section of the Consolidated Statements of Cash Flows.

Gains or losses from our sale of properties that were developed with the intent to sell and not for long-term rental are recognized in accordance with SFAS 66 and are included in construction management and development activity income in the Consolidated Statements of Operations. All activities

and proceeds received from the development and sale of these merchant buildings are classified in the operating activities section of the Consolidated Statements of Cash Flows.

## Net Income Per Common Share

Basic net income per common share is computed by dividing net income available for common shares by the weighted average number of common shares outstanding for the period. Diluted net income per common share is computed by dividing the sum of net income available for common shareholders and the minority interest in earnings allocable to Units not owned by us, by the sum of the weighted average number of common shares outstanding, minority Units outstanding and any dilutive potential common shares for the period.

The following table reconciles the components of basic and diluted net income per common share (in thousands):

	2005	2004	2003
Basic net income available for common shareholders	\$ 309,183	\$ 151,279	\$ 161,911
Minority interest in earnings of common unitholders	29,649	14,966	17,546
Diluted net income available for common shareholders	\$ 338,832	\$ 166,245	\$ 179,457
Weighted average number of common shares outstanding	141,508	141,379	135,595
Weighted average partnership units outstanding	13,551	13,902	14,685
Weighted average conversion of Series D preferred shares <sup>(1)</sup>	—	877	—
Dilutive shares for stock-based compensation plans	818	904	861
Weighted average number of common shares and dilutive potential common shares	155,877	157,062	151,141

<sup>(1)</sup> We called for the redemption of the Series D preferred shares as of March 16, 2004. Prior to the redemption date, nearly 5.3 million Series D preferred shares were converted to 4.9 million common shares. These shares represent the weighted effect, assuming the Series D preferred shares had been converted on January 1, 2004.

The Series D Convertible Cumulative Redeemable Preferred Shares were anti-dilutive for the year ended December 31, 2003; therefore, no conversion to common shares was included in weighted average dilutive potential common shares.

A joint venture partner in one of our unconsolidated companies has the option to convert a portion of its ownership to our common shares. The effect of this option on earnings per share was anti-dilutive for the years ended December 31, 2005, 2004 and 2003.

## Federal Income Taxes

We have elected to be taxed as a real estate investment trust ("REIT") under the Internal Revenue Code. To qualify as a REIT, we must meet a number of organizational and operational requirements, including a requirement to distribute at least 90% of our adjusted taxable income to our stockholders. Management intends to continue to adhere to these requirements and to maintain our REIT status. As a

REIT, we are entitled to a tax deduction for some or all of the dividends we pay to shareholders. Accordingly, we generally will not be subject to federal income taxes as long as we distribute an amount equal to or in excess of our taxable income currently to shareholders. A REIT generally is subject to federal income taxes on any taxable income that is not currently distributed to its shareholders. If we fail to qualify as a REIT in any taxable year, we will be subject to federal income taxes and may not be able to qualify as a REIT for four subsequent taxable years.

REIT qualification reduces, but does not eliminate, the amount of state and local taxes we pay. In addition, our financial statements include the operations of taxable corporate subsidiaries that are not entitled to a dividends paid deduction and are subject to corporate federal, state and local income taxes. As a REIT, we may also be subject to certain federal excise taxes if we engage in certain types of transactions.

The following table reconciles our net income to taxable income before the dividends paid deduction for the years ended December 31, 2005, 2004 and 2003 (in thousands):





	2005	2004	2003
Net income	\$ 355,662	\$ 188,701	\$ 199,232
Book/tax differences	116,152	53,817	35,082
Taxable income before adjustments	471,814	242,518	234,314
Less: capital gains	(270,854)	(38,655)	(32,009)
Adjusted taxable income subject to 90% dividend requirement	<u>\$ 200,960</u>	<u>\$ 203,863</u>	<u>\$ 202,305</u>

Our dividends paid deduction is summarized below (in thousands):

	2005	2004	2003
Cash dividends paid	\$ 455,606	\$ 292,889	\$ 284,868
Cash dividends declared and paid in subsequent year that apply to current year	16,208	—	—
Less: Capital gains distribution	(270,854)	(38,655)	(32,009)
Less: Return of capital	—	(46,694)	(46,637)
Total dividends paid deduction attributable to adjusted taxable income	<u>\$ 200,960</u>	<u>\$ 207,540</u>	<u>\$ 206,222</u>

A summary of the tax characterization of the dividends paid for the years ended December 31, 2005, 2004 and 2003 follows:

	2005	2004	2003
<b>Common Shares</b>			
Ordinary income	44.2%	69.3%	69.7%
Return of capital	—	17.5%	19.1%
Capital gains	55.8%	13.2%	11.2%
	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>
<b>Preferred Shares</b>			
Ordinary income	44.2%	86.8%	88.8%
Capital gains	55.8%	13.2%	11.2%
	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

We recorded federal and state income taxes of \$5.6 million, \$5.2 million and \$4.0 million for 2005, 2004 and 2003, respectively, which were primarily attributable to the earnings of our taxable REIT subsidiaries. We paid federal and state income taxes of \$8.7 million, \$6.2 million and \$5.5 million for 2005, 2004 and 2003, respectively. The taxable REIT subsidiaries have no significant deferred income tax items.

#### Stock Based Compensation

For all issuances of stock-based awards prior to 2002, we apply the recognition and measurement provisions of Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations in accounting, for our stock-based compensation.

Accordingly, for stock options granted prior to 2002, no compensation expense is reflected in net income as all options

granted had an exercise price equal to the market value of the underlying common shares on the date of the grant.

Effective January 1, 2002, we prospectively adopted the fair value recognition provisions of FASB Statement No. 123, *Accounting for Stock-Based Compensation* ("SFAS 123"), and applied SFAS 123 to all awards granted after January 1, 2002.

Stock option awards granted under our stock based employee and non-employee compensation plans generally vest over five years at 20% per year. Therefore, the expense related to these plans is less than that which would have been recognized if the fair value method had been applied to all awards since the original effective date of SFAS 123. The following table illustrates the effect on net income and earnings per share if the fair value method had been applied to all outstanding and unvested stock option awards in each period (in thousands, except per share data).





# Notes to Consolidated Financial Statements

	2005	2004	2003
Net income available for common shareholders, as reported	\$ 309,183	\$ 151,279	\$ 161,911
Add: Stock based compensation expense for stock options included in net income determined under fair value method	1,116	455	155
Deduct: Total stock based compensation expense determined under fair value method for all stock option awards	(1,285)	(923)	(778)
Proforma net income available for common shareholders	\$ 309,014	\$ 150,811	\$ 161,288
Basic net income per common share			
As reported	\$ 2.19	\$ 1.07	\$ 1.19
Pro forma	\$ 2.18	\$ 1.07	\$ 1.19
Diluted net income per common share			
As reported	\$ 2.17	\$ 1.06	\$ 1.19
Pro forma	\$ 2.17	\$ 1.06	\$ 1.18

## Derivative Financial Instruments

We periodically enter into certain interest rate protection agreements to effectively convert or cap floating rate debt to a fixed rate, and to hedge anticipated future financing transactions, both of which qualify for cash flow hedge accounting treatment under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended ("SFAS 133"). Net amounts paid or received under these agreements are recognized as an adjustment to the interest expense of the corresponding debt. We do not utilize derivative financial instruments for trading or speculative purposes.

SFAS 133 requires that all derivative instruments be recorded on the balance sheet as assets or liabilities at their fair value. Derivatives that are not hedges must be adjusted to fair value through the recording of income or expense. If a derivative qualifies as a cash flow hedge, the change in fair value of the derivative is recognized in other comprehensive income to the extent the hedge is effective, while the ineffective portion of the derivative's change in fair value is recognized in earnings. We estimate the fair value of derivative instruments using standard market conventions and techniques such as discounted cash flow analysis, option pricing models and termination cost at each balance sheet date. For all hedging relationships, we formally document the hedging relationship and its risk-management objective and strategy for undertaking the hedge, the hedging instrument, the hedged item, the nature of the risk being hedged, how the hedging instrument's effectiveness in offsetting the hedged risk will be assessed prospectively and retrospectively, and a description of the method of measuring ineffectiveness.

## Use Of Estimates

The preparation of the financial statements requires management to make a number of estimates and assumptions that affect the reported amount of assets and liabilities and the

disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates.

## 3—Industrial Portfolio Sale

On September 29, 2005, we completed the sale of a portfolio of 212 real estate properties, consisting of approximately 14.1 million square feet of primarily light distribution and service center properties and approximately 50 acres of undeveloped land (the "Industrial Portfolio Sale"). The purchase price totaled \$983 million, of which we received net proceeds of \$955 million after the settlement of certain liabilities and transaction costs. Portions of the proceeds were used to pay down \$423 million of outstanding debt on our \$500 million unsecured line of credit and the entire outstanding balance on our \$400 million term loan. The operations for 2005, 2004 and 2003 and the gain for 2005 associated with the properties in the Industrial Portfolio Sale have been reclassified to discontinued operations. For further discussion, see Note 6. As a result of the taxable income generated by the sale, a one-time special cash dividend of \$1.05 per share was paid to our common shareholders in the fourth quarter of 2005.

## 4—Related Party Transactions

We provide property management, leasing, construction and other tenant related services to unconsolidated companies in which we have equity interests. For the years ended December 31, 2005, 2004 and 2003, respectively, we received from these unconsolidated companies management fees of \$4.8 million, \$4.9 million and \$4.9 million, leasing fees of \$4.3 million, \$2.6 million and \$2.3 million and construction and development fees of \$2.0 million, \$1.5 million and \$1.4 million. We recorded these fees at market rates and eliminated our ownership percentages of these fees in the consolidated financial statements.





## 5—Investments in Unconsolidated Companies

We analyze our investments in joint ventures under FASB Interpretation No. 46(R), *Consolidation of Variable Interest Entities* (“FIN 46(R)”), to determine if the joint venture is a variable interest entity and would require consolidation. To the extent that our joint ventures do not qualify as variable interest entities, we further assess under the guidelines of Emerging Issues Task Force (“EITF”) Issue No. 04-5, *Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights* (“EITF 04-5”), Statement of Position 78-9, *Accounting for Investments in Real Estate Ventures*; Accounting Research Bulletin No. 51, *Consolidated Financial Statements*, and FASB No. 94, *Consolidation of All Majority-Owned Subsidiaries*, to determine if the venture should be consolidated.

In 2004, we announced a 50/50 joint venture agreement with a medical office developer to develop healthcare facilities. Under the terms of the agreement, we provide the project financing and construction services while our partner provides

the business development, leasing and property management of the co-developed properties. We evaluated this partnership under FIN 46(R) and determined that this joint venture qualifies as a variable interest entity subject to consolidation. We are the primary beneficiary as determined under FIN 46(R) and fully consolidate the joint venture.

At December 31, 2005, there were six properties under development with the joint venture. These properties total nearly 470,000 square feet and have an aggregate construction in-process balance of approximately \$14.9 million that is consolidated into our balance sheet.

We have equity interests ranging from 10%–64% in unconsolidated joint ventures that own and operate rental properties and hold land for development.

Combined summarized financial information for the unconsolidated companies as of December 31, 2005 and 2004, and for the years ended December 31, 2005, 2004, and 2003, are as follows (in thousands):

	2004	2003
Rental revenue	\$ 163,447	\$ 167,803
Net income	\$ 57,561	\$ 41,065
Cash distributions received	\$ 25,446	\$ 30,309
Land, buildings and tenant improvements, net	\$1,121,254	\$ 1,158,068
Land held for development	47,936	50,173
Other assets	73,084	62,190
	<u>\$1,242,274</u>	<u>\$ 1,270,431</u>
Property indebtedness	\$ 515,192	\$ 570,941
Other liabilities	58,225	51,377
	<u>573,417</u>	<u>622,318</u>
Owners' equity	668,857	648,113
	<u>\$1,242,274</u>	<u>\$ 1,270,431</u>

Our share of the scheduled payments of long term debt for the unconsolidated joint ventures for each of the next five years and thereafter as of December 31, 2005, are as follows (in thousands):

Year	Future Repayments
2006	\$ 13,740
2007	46,417
2008	21,588
2009	70,491
2010	100,289
Thereafter	4,411
	<u>\$256,936</u>

The following significant transactions involving the unconsolidated companies have occurred over the past three years:

During 2003, we purchased our partners' interests in three separate joint ventures. We had a 50% interest in each of these ventures prior to their acquisition. We also sold our 50% interest in two separate joint ventures to our partners. In addition, we contributed cash and undeveloped land to a joint venture that owns undeveloped land and an office building in return for a 50% interest.





# Notes to Consolidated Financial Statements

## 6—Real Estate Investments

We have classified operations of 320 buildings as discontinued operations as of December 31, 2005. These 320 buildings consist of 292 industrial, 23 office and five retail properties. Of these properties, 234 were sold during 2005, 41 properties were sold during

2004, 42 properties were sold during 2003 and three operating properties are classified as held-for-sale at December 31, 2005.

The following table illustrates the major classes of operations affected by the 320 buildings identified as discontinued operations for the years ended December 31 (in thousands):

	2005	2004	2003
Revenues	\$ 91,663	\$ 136,412	\$ 158,502
Expenses:			
Operating	28,242	39,499	42,946
Interest	22,901	27,686	30,842
Depreciation and Amortization	27,667	47,139	45,234
General and Administrative	125	154	188
Operating Income	12,728	21,934	39,292
Other Income	—	—	59
Minority interest expense - operating and other income	(1,112)	(1,963)	(3,845)
Net income from discontinued operations, net of minority interest	11,616	19,971	35,506
Gain (loss) on sale of property, net of impairment adjustment	223,858	26,247	13,024
Minority interest expense – gain on sales	(19,565)	(2,349)	(1,272)
Gain on sale of discontinued operations, net of impairment adjustments and minority interest	204,293	23,898	11,752
Income from discontinued operations	\$ 215,909	\$ 43,869	\$ 47,258

The following table illustrates the balance sheet of the three buildings identified as held-for-sale at December 31, 2005 (in thousands):

Real estate investments, net	\$12,699
Other Assets	433
Total Assets	\$13,132
Accrued Expenses	\$ 20
Other Liabilities	66
Equity and minority interest	13,046
Total Liabilities and Equity	\$13,132

We allocate interest expense to discontinued operations as permitted under EITF 87-24, “Allocation of Interest to Discontinued Operations,” and have included such interest expense in computing net income from discontinued operations. Interest expense allocable to discontinued operations includes interest on the debt for the secured properties and an allocable share of our consolidated unsecured interest expense for unencumbered properties. The allocation of unsecured interest expense to discontinued operations was based upon the Gross Book Value of the discontinued operations unencumbered population as it related to our entire unencumbered population.

At December 31, 2005, we had classified as held-for-sale three industrial properties comprising approximately 366,000 square feet. While we have entered into agreements for the sale of these properties, there can be no assurances that such properties actually will be sold.

In 2005, we recorded \$3.7 million of impairment adjustments for two industrial buildings and four office buildings and \$259,000 of impairment adjustments for seven land parcels. These adjustments reflect the write-down of the carrying value of the properties to their projected sales prices, less selling expenses, once it became probable that the properties would be sold. One of the industrial buildings is projected to sell in the first quarter of 2006, while the other five buildings and seven land parcels were sold in 2005.

In 2004, we recorded \$424,000 of impairment adjustments for three land parcels. We also recorded a \$180,000 impairment adjustment for the industrial building classified as held-for-sale at December 31, 2004. The industrial building was sold in the first quarter of 2005. Each of the land parcel properties was sold in 2004.

In 2003, we recorded \$1.1 million of impairment adjustments for one industrial building and three land parcels that were sold in 2003.





## 7—Indebtedness

Indebtedness at December 31 consists of the following (in thousands):

	2005	2004
Fixed rate secured debt, weighted average interest rate of 6.13% at December 31, 2005, and 6.51% at December 31, 2004, maturity dates ranging from 2006 to 2017	\$ 131,732	\$ 163,607
Variable rate secured debt, weighted average interest rate of 5.75% at December 31, 2005, and 3.43% at December 31, 2004, maturity dates ranging from 2006 to 2025	35,523	39,474
Fixed rate unsecured notes, weighted average interest rate of 6.02% at December 31, 2005, and 6.02% at December 31, 2004, maturity dates ranging from 2006 to 2028	1,800,396	2,065,623
Unsecured line of credit, interest rate of 4.83% at December 31, 2005, facility unused at December 31, 2004, maturity date 2007	383,000	—
Variable rate unsecured note, interest rate of 4.76% at December 31, 2005, and 2.78% at December 31, 2004, maturity date of 2006	250,000	250,000
	<b>\$2,600,651</b>	<b>\$ 2,518,704</b>

The fair value of our indebtedness as of December 31, 2005, was \$2.7 billion. This fair value amount was calculated using current market rates and spreads available to us on debt instruments with similar terms and maturities.

As of December 31, 2005, the \$167.3 million of secured debt

was collateralized by rental properties with a carrying value of \$346.5 million and by letters of credit in the amount of \$10.1 million.

We had one unsecured line of credit available at December 31, 2005, summarized as follows (in thousands):

Description	Borrowing Capacity	Maturity Date	Interest Rate	Outstanding at December 31, 2005
Unsecured Line of Credit	\$500,000	January 2007	LIBOR + .60%	\$383,000

The line of credit provides us with an option to obtain borrowings from financial institutions that participate in the line, at rates lower than the stated interest rate, subject to certain restrictions.

In January 2006, we renewed our unsecured revolving credit facility. The new facility provides borrowing capacity up to \$1 billion and, subject to certain conditions, may be increased to \$1.3 billion. Under the new facility, which replaces the previous unsecured line of credit agreement, we reduced the interest rate by 7.5 basis points to LIBOR plus 52.5 basis points, increased the borrowing capacity by \$500 million and extended the maturity date to January 25, 2010.

The line of credit contains various financial covenants that require us to meet defined levels of performance, including variable interest indebtedness, consolidated net worth and debt-to-market capitalization. As of December 31, 2005, we were in compliance with all financial covenants under our line of credit.

We took the following actions during the year ended December 31, 2005, relevant to our indebtedness:

- In January 2005, we retired our \$65.0 million variable-rate term loan.
- In March 2005, we retired \$100.0 million of 6.875% senior unsecured debt that matured.
- In May 2005, we obtained a \$400.0 million unsecured term loan, which was priced at LIBOR + .30%. This unsecured term loan was paid off in full on September 29, 2005 with proceeds from the Industrial Portfolio Sale.
- In September 2005, we retired \$100.0 million of 7.375% senior unsecured debt that matured.
- In September 2005, we paid down the outstanding balance of \$423.0 million on our \$500.0 million unsecured line of credit with proceeds from the Industrial Portfolio Sale.





# Notes to Consolidated Financial Statements

At December 31, 2005, the scheduled amortization and maturities of all indebtedness for the next five years and thereafter were as follows (in thousands):

Year	Amount
2006	\$ 397,343
2007	604,235
2008	274,607
2009	279,926
2010	179,316
Thereafter	865,224
	<u>\$2,600,651</u>

The amount of interest paid in 2005, 2004 and 2003 was \$151.3 million, \$136.2 million and \$130.1 million, respectively. The amount of interest capitalized in 2005, 2004 and 2003 was \$9.5 million, \$6.0 million and \$6.7 million, respectively.

## 8—Segment Reporting

We are engaged in three operating segments, the first two of which consist of the ownership and rental of office and industrial real estate investments (collectively, “Rental Operations”). The third segment consists of our build-to-suit for sale operations and the providing of various real estate services that we provide such as property management, maintenance, leasing, development and construction management to third-party property owners and joint ventures (“Service Operations”). Our reportable segments offer different products or services and are managed separately because each requires different operating strategies and management expertise. During 2005, 2004 and 2003, there were no material intersegment sales or transfers.

Non-segment revenue consists mainly of equity in earnings of unconsolidated companies. Segment FFO (defined below) information is calculated by subtracting operating expenses attributable to the applicable segment from segment revenues. Non-segment assets consist of corporate assets including cash, deferred financing costs and investments in unconsolidated companies. Interest expense and other non-property specific revenues and expenses are not allocated to individual segments in determining our performance measure.

We assess and measure segment operating results based upon an industry performance measure referred to as Funds From Operations (“FFO”), which management believes is a useful indicator of our operating performance. FFO is used by industry analysts and investors as a supplemental operating performance measure of an equity real estate investment trust (“REIT”).

FFO is calculated in accordance with the definition that was adopted by the Board of Governors of the National Association of Real Estate Investment Trusts (“NAREIT”). FFO, as defined by NAREIT, represents net income (loss) determined in accordance with accounting principles generally accepted in the United States of America (“GAAP”), excluding extraordinary items as defined under GAAP and gains or losses from sales of previously depreciated operating real estate assets, plus certain non-cash items such as real estate asset depreciation and amortization, and after similar adjustments for unconsolidated partnerships and joint ventures.

The revenues and FFO for each of the reportable segments for the years ended December 31, 2005, 2004 and 2003, respectively, and the assets of each reportable segment as of December 31, 2005 and 2004, respectively, are summarized as follows (in thousands):





	2005	2004	2003
<b>Revenues</b>			
Rental Operations:			
Office	\$ 491,895	\$ 448,682	\$ 409,071
Industrial	174,963	160,709	142,087
Service Operations	81,941	70,803	59,456
Total Segment Revenues	748,799	680,194	610,614
Non-Segment Revenue	39,325	31,764	33,245
Consolidated Revenue from continuing operations	788,124	711,958	643,859
Discontinued Operations	91,663	136,412	158,502
Consolidated Revenue	\$ 879,787	\$ 848,370	\$ 802,361

### Funds From Operations

Rental Operations:			
Office	\$ 301,692	\$ 287,374	\$ 266,641
Industrial	131,063	123,018	107,000
Services Operations	41,019	24,421	21,821
Total Segment FFO	473,774	434,813	395,462
Non-Segment FFO:			
Interest expense	(120,369)	(109,923)	(100,664)
Interest income	5,844	5,213	3,556
General and administrative expense	(27,835)	(26,278)	(21,980)
Gain on land sales, net of impairment	14,201	10,119	7,135
Impairment charges on depreciable property	(3,656)	(180)	(500)
Other income (expense) on non-segment FFO	1,908	3,533	2,080
Minority interest in earnings of subsidiaries	(1,438)	(1,253)	(586)
Minority interest in earnings of common unitholders	(9,378)	(11,619)	(12,429)
Minority interest in earnings of preferred unitholders	–	–	(1,904)
Minority interest share of FFO adjustments	(3,065)	(19,783)	(18,854)
Joint venture FFO	37,964	40,488	42,526
Dividends on preferred shares	(46,479)	(33,777)	(37,321)
Adjustment for redemption of preferred stock	–	(3,645)	–
Discontinued operations, net of minority interest	19,718	64,761	79,468
Consolidated FFO	341,189	352,469	335,989
Depreciation and amortization on continuing operations	(226,503)	(181,443)	(151,000)
Depreciation and amortization on discontinued operations	(27,667)	(47,139)	(45,234)
Company's share of joint venture adjustments	(19,510)	(18,901)	(18,839)
Earnings from the sale of ownership interest in unconsolidated companies on continuing operations	–	83	8,617
Earnings from depreciated property sales on discontinued operations	227,513	26,427	13,524
Earnings from depreciated property sales – share of joint venture	11,096	–	–
Minority interest share of FFO adjustments	3,065	19,783	18,854
Net income available for common shareholders	\$ 309,183	\$ 151,279	\$ 161,911

December 31,	2005	2004
<b>Assets</b>		
Rental Operations		
Office	\$3,396,985	\$ 3,128,387
Industrial	1,577,631	2,211,509
Service Operations	177,463	131,218
Total Segment Assets	5,152,079	5,471,114
Non-Segment Assets	495,481	425,529
Consolidated Assets	\$5,647,560	\$ 5,896,643





# Notes to Consolidated Financial Statements

In addition to revenues and FFO, we also review our recurring capital expenditures in measuring the performance of our individual Rental Operations segments. These recurring capital expenditures consist of tenant improvements, leasing commissions and building improvements. We review these expenditures to determine the costs associated with re-leasing vacant space and maintaining the condition of our properties. Our recurring capital expenditures by segment are summarized as follows for the years ended December 31, 2005, 2004 and 2003, respectively (in thousands):

	2005	2004	2003
<b>Recurring Capital Expenditures</b>			
Office	\$ 66,890	\$ 68,535	\$ 44,602
Industrial	42,083	39,096	31,711
Non-segment	67	22	135
Total	<u>\$109,040</u>	<u>\$107,653</u>	<u>\$ 76,448</u>

## 9—Leasing Activity

Future minimum rents due to us under non-cancelable operating leases at December 31, 2005, are as follows (in thousands):

Year	Amount
2006	\$ 558,556
2007	544,758
2008	484,239
2009	413,840
2010	344,446
Thereafter	<u>1,105,601</u>
	<u>\$3,451,440</u>

Description	Shares Outstanding	Dividend Rate	Redemption Date	Liquidation Preference	Convertible
Series B Preferred	265	7.990%	September 30, 2007	\$132,250	No
Series I Preferred	300	8.450%	February 6, 2006	75,000	No
Series J Preferred	400	6.625%	August 29, 2008	100,000	No
Series K Preferred	600	6.500%	February 13, 2009	150,000	No
Series L Preferred	800	6.600%	November 30, 2009	200,000	No

The dividend rate on the Series B preferred shares increases to 9.99% after September 12, 2012.

All series of preferred shares require cumulative distributions and have no stated maturity date (although we may redeem them on or following their optional redemption dates).

At our option, we may redeem, in whole or in part, the Series B, Series I, Series J, Series K and Series L preferred shares described in this section.

Pursuant to the \$750 million share repurchase plan that was approved by our board of directors, we paid approximately \$297.1 million for 8,995,775 of our common shares at an average price of \$33.02 per share during the year ended December 31, 2005. From time to time, management may repurchase additional common shares pursuant to our share repurchase

plan. In addition to minimum rents, certain leases require reimbursements of specified operating expenses that amounted to \$151.4 million, \$137.9 million, and \$130.3 million for the years ended December 31, 2005, 2004 and 2003, respectively.

## 10—Employee Benefit Plans

We maintain a 401(k) plan for full-time employees. We make matching contributions up to an amount equal to three percent of the employee's salary and may also make annual discretionary contributions. The total expense recognized for this plan was \$2.3 million, \$1.9 million and \$1.6 million for the years ended 2005, 2004 and 2003, respectively.

We make contributions to a contributory health and welfare plan as necessary to fund claims not covered by employee contributions. The total expense we recognized related to this plan was \$8.1 million, \$7.2 million and \$6.4 million for 2005, 2004 and 2003, respectively. These expense amounts include estimates based upon the historical experience of claims incurred but not reported as of year-end.

## 11—Shareholders' Equity

We periodically access the public equity markets to fund the development and acquisition of additional rental properties or to pay down debt. The proceeds of these offerings are contributed to DRLP in exchange for an additional interest in DRLP.

The following series of preferred stock were outstanding as of December 31, 2005 (in thousands, except percentage data):

plan. The timing and amount of future share repurchases will depend on business and market conditions, as well as legal and regulatory considerations.

In January 2006, we issued \$184 million of 6.95% Series M Cumulative Redeemable Preferred Stock, which replaced our \$75 million 8.45% Series I Cumulative Redeemable Preferred Stock that we redeemed in February 2006.

## 12—Stock Based Compensation

Our stock based employee and non-employee compensation plans are described more fully below. We are authorized to issue up to 11,320,552 shares of our common stock under these compensation plans.





### Fixed Stock Option Plans

We had options outstanding under six fixed stock option plans as of December 31, 2005. Additional grants may be made under one of those plans.

A summary of the status of our fixed stock option plans as of December 31, 2005, 2004 and 2003 and changes during the years ended on those dates follows:

	2005		2004		2003	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding, beginning of year	3,352,469	\$24.51	3,586,360	\$22.65	3,920,198	\$22.09
Granted	812,684	32.27	506,688	32.49	609,390	25.48
Granted for modification of awards	110,351	26.09	—	—	—	—
Exercised	(303,099)	21.78	(728,250)	20.85	(773,625)	21.87
Forfeited	(144,248)	28.58	(12,329)	27.20	(169,603)	23.63
Outstanding, end of year	<u>3,828,157</u>	<u>25.50</u>	<u>3,352,469</u>	<u>24.51</u>	<u>3,586,360</u>	<u>22.65</u>
Options exercisable, end of year	<u>2,116,951</u>		<u>1,844,256</u>		<u>2,014,875</u>	
Weighted-average fair value of options granted during the year <sup>(1)</sup>	<u>\$ 2.55</u>		<u>\$ 2.84</u>		<u>\$ 1.81</u>	

<sup>(1)</sup> The 110,351 options granted for modification of awards represent options granted as a result of modification of the options outstanding at November 9, 2005. The purpose of the modification was to equalize the value of the options before and after the one-time special dividend of \$1.05 per share. This special dividend was paid in December 2005 in order to maintain our compliance with the minimum distribution requirements of a REIT as a result of the significant gain realized on the Industrial Portfolio Sale discussed in Note 3. The weighted-average fair value of options granted during the year, excluding the options granted as a result of the modification, is \$3.04.

The fair values of the options were determined using the Black-Scholes option-pricing model with the following assumptions:

	2005	2004	2003
Dividend yield	6.25%	6.50%	7.25%
Volatility	20.0%	20.0%	20.0%
Risk-free interest rate	3.8%	3.6%	3.2%
Expected life	6 years	6 years	6 years

The options outstanding at December 31, 2005, under the fixed stock option plans have a range of exercise prices from \$18.30 to \$33.16 with a weighted average exercise price of \$25.50 and a weighted average remaining contractual life of 6.09 years. The options exercisable at December 31, 2005 have a weighted average exercise price of \$22.65.

Each option's maximum term is ten years. With limited exceptions, options vest at 20% per year, or, if earlier, upon the death, retirement or disability of the optionee or a change in control of the Company.

### Performance Based Stock Plans

Performance shares are granted under the 2000 Performance Share Plan, with each performance share economically equivalent to one share of our common stock. The performance shares vest over a five-year period with the vesting percentage for a year dependent upon our attainment of certain predefined levels of earnings growth for such year. The value of vested performance shares are payable in cash upon the retirement or termination of employment of the participant. At December 31, 2005, plan

participants had the right to receive up to 183,467 performance shares, of which 84,466 were vested and 99,001 were contingent upon future earnings achievement. Under our 2005 Long-Term Incentive Plan approved in April 2005, additional performance shares may be granted on such terms and conditions as may be selected by our compensation committee, including whether payment will be made in cash, shares of our common stock, DRLP units or other property. There were no such grants made in 2005.

The amount of compensation cost was based upon the intrinsic value of the vested performance shares at the end of each applicable reporting period. The compensation cost that was charged against income for this plan was \$1.3 million, \$1.7 million and \$529,000 for 2005, 2004 and 2003, respectively.

In October 2002, we amended our 1995 Shareholder Value Plan ("SVP Plan") and 1995 Dividend Increase Unit Plans ("DIU Plans") by requiring that all payouts under these two plans to be in cash only. Payments made under this SVP Plan are based upon our cumulative shareholder return for a three-year period as compared to the cumulative total return of the S&P 500 and the NAREIT Equity REIT Total Return indices. Payments under the DIU Plans are based upon increases in our dividend per common share. The total compensation cost that was charged against income for these two plans was \$1.4 million, \$2.3 million and \$1.6 million for 2005, 2004 and 2003, respectively.

Our 2005 Shareholder Value Plan, a sub-plan of our 2005 Long-Term Incentive Plan, was approved by our shareholders in April 2005. Upon vesting, payout of the 2005 Shareholder Value Plan awards will be made in shares of our common stock.





# Notes to Consolidated Financial Statements

Under this plan, shareholder value awards fully vest three years after the date of grant. The number of common shares to be issued will be based upon our total shareholder return for such three-year period as compared to the S & P 500 Index and the NAREIT Real Estate 50 Index. Each index is weighted at 50%. The fair value of awards granted under our 2005 Shareholder Value Plan is \$1.3 million, which was determined using a Monte Carlo simulation. The valuation model was developed to accommodate the unique features of the plan. The total compensation cost that was charged against income for the 2005 Shareholder Value Plan award was \$438,000 for 2005.

## Restricted Stock Units

Under our 2005 Long-Term Incentive Plan and our 2005 Non-Employee Directors Compensation Plan approved by our shareholders in April 2005, restricted stock units ("RSUs") were granted to non-employee directors, executive officers and selected management employees in 2005. An RSU is economically equivalent to one share of our common stock. RSUs vest 20% per year over five years and are payable in shares of our common stock. We recognize the value of the granted RSUs over this vesting period as expense. We granted 177,613 RSUs during 2005, of which 4,702 were forfeited as a result of participant terminations and 816 were issued as a result of participant retirement. The remaining 172,095 unvested RSUs outstanding at December 31, 2005 had a total value of \$5.5 million. Of the total value of the RSUs outstanding, we have recognized \$408,000 as compensation expense for executive officers and selected management employees, and \$71,000 as general and administrative expense for non-employee directors through December 31, 2005.

In addition, all RSUs earn dividend equivalents that are deemed to be reinvested in additional RSUs. Dividend equivalents vest immediately and will be paid in shares of our common stock when the corresponding portion of the original RSU award vests or upon termination of the participant. Dividend equivalents of 6,474 RSUs were earned in 2005 on the RSU awards granted during the year, of which 6,391 were outstanding at December 31, 2005. A charge to retained earnings of \$216,000 was recorded for the value of these dividend equivalents in 2005.

## Directors Stock Payment Plan

Our 2005 Non-Employee Directors Compensation Plan was approved by our shareholders in April 2005 and supercedes our 1996 Directors' Stock Payment Plan and our 1999 Directors' Stock Option and Dividend Increase Unit Plan. Under our 2005 Non-Employee Directors Compensation Plan, non-employee members of our board of directors were entitled to 1,600 shares of our common stock per year as partial compensation for services as a board member. The shares are fully vested when issued and we record the value of the shares as an expense. The

amount of that expense was \$585,000, \$525,000 and \$415,000 for 2005, 2004 and 2003, respectively. On October 26, 2005, our Board of Directors amended our 2005 Non-Employee Directors Compensation Plan to, among other items, determine the number of shares of common stock granted to each non-employee director as this partial compensation by reference to a fixed dollar amount of \$15,000 per quarter, as opposed to a fixed number of shares.

## Employee Stock Purchase Plan

Under our Employee Stock Purchase Plan, employees are entitled to purchase our common stock at a 15% discount through payroll deductions. Under SFAS 123, we are required to record the amount of the discount as compensation expense. The amount of that expense for 2005, 2004 and 2003 was \$305,000, \$255,000 and \$219,000, respectively.

## 13—Financial Instruments

We are exposed to capital market risk, such as changes in interest rates. In order to manage the volatility relating to interest rate risk, we may enter into interest rate hedging arrangements from time to time. We do not utilize derivative financial instruments for trading or speculative purposes. We account for derivative instruments under Statement of Financial Accounting Standard No. 133, *Accounting for Derivative Instruments and Hedging Activities* ("SFAS 133"), as amended by SFAS No. 138, *Accounting for Certain Derivative Instruments and Certain Hedging Activities* ("SFAS 138").

In March 2005, we entered into \$300.0 million of cash flow hedges through forward-starting interest rate swaps to hedge interest rates on \$300.0 million of estimated debt offerings in 2006. The swaps qualify for hedge accounting under SFAS 133, as amended by SFAS 138, with any changes in fair value recorded in Accumulated Other Comprehensive Income ("OCI"). The market value of these interest rate swaps is dependent upon existing market interest rates, which change over time. At December 31, 2005, the estimated fair value of the swaps was a liability of approximately \$6.6 million. The effective rates of the swaps were higher than interest rates at December 31, 2005.

In August 2005, we entered into \$300.0 million of cash flow hedges through forward-starting interest rate swaps to hedge interest rates on \$300.0 million of estimated debt offerings in 2007. The swaps qualify for hedge accounting under SFAS 133, as amended by SFAS 138, with any changes in fair value recorded in OCI. At December 31, 2005, the fair value of these swaps was an asset of \$5.3 million. The effective rates of the swaps were lower than interest rates at December 31, 2005.

In June 2004, we simultaneously entered into three forward-starting interest rate swaps aggregating \$144.3 million, which effectively fixed the rate on financing expected in 2004 at 5.346%, plus our credit spread over the swap rate. The swaps qualified for hedge accounting under SFAS 133; therefore,





changes in the fair value were recorded in OCI. In August 2004, we settled these three swaps when we issued \$250.0 million of unsecured notes with an effective interest rate of 6.33%, due in 2014. We paid \$6.85 million to unwind the swaps, which is amortized from OCI into interest expense over the life of the new 6.33% notes.

In December 2002, we simultaneously entered into two \$50 million forward-starting interest rate swaps as a hedge to effectively fix the rate on unsecured debt financings expected in 2003. Then again in February 2003, we simultaneously entered into two additional \$25 million forward-starting interest rate swaps as a hedge to effectively fix the rate on unsecured debt financings expected in 2003. All four swaps qualified for hedge accounting under SFAS 133; therefore, changes in fair value were recorded in OCI. In July 2003, we terminated the swaps for a net gain of \$643,000, which is included in other revenue in the Statements of Operations. The swaps were terminated because our capital needs were met through the issuance of the Series J Preferred Stock in lieu of the previously contemplated issuance of debt.

In May 2003, the Financial Accounting Standards Board ("FASB") issued SFAS No. 150, *Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity* ("SFAS 150"). SFAS 150 establishes standards for classifying and measuring as liabilities certain financial instruments that embody obligations of the issuer and have characteristics of both liabilities and equity. SFAS 150 was effective for all financial instruments created or modified after May 31, 2003, and otherwise was effective July 1, 2003. We consolidated the operations of one joint venture in our consolidated financial statements at December 31, 2005. This joint venture is partially owned by unaffiliated parties that have noncontrolling interests. SFAS 150 requires the disclosure of the estimated settlement value of these noncontrolling interests. As of December 31, 2005, the estimated settlement value of the noncontrolling interest in this consolidated joint venture was approximately \$1.1 million, as compared to the \$24,000 receivable reported in our financial statements for this joint venture.

#### 14—Recent Accounting Pronouncements

In December 2004, FASB issued SFAS No. 123 (R), *Share-Based Payment*, which is a revision of SFAS No. 123, *Accounting for Stock Based Compensation*. In April 2005, the SEC delayed the effective date on SFAS No. 123 (R) from July 2005 to January 2006. We have completed our preliminary evaluation of the impact of SFAS No. 123 (R) and have determined that the cumulative effect of a change in accounting principle will be insignificant to our results of operations. We have selected the modified-prospective method for the adoption of SFAS No. 123 (R).

In March 2005, FASB Interpretation No. 47, *Accounting for Conditional Asset Retirement Obligations* ("FIN 47"), was issued for all fiscal years ending after December 15, 2005. This is an

interpretation of SFAS No. 143, *Accounting for Asset Retirement Obligation*. Upon evaluation, we have determined that the adoption of FIN 47 did not have a material impact on our financial statements.

In June 2005, FASB ratified the consensus reached in Emerging Issues Task Force ("EITF") No. 04-5, *Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights* ("EITF 04-5"). EITF 04-5 is effective for all newly formed limited partnerships after the consensus was ratified and as of January 2006 for all preexisting limited partnership agreements. This consensus applies to limited partnerships or similar entities, such as limited liability companies that have governing provisions that are the functional equivalent of a limited partnership. We have evaluated the ownership structure of our existing investments in unconsolidated companies and determined that we do not exercise control over any unconsolidated ventures as defined by EITF 04-5.

#### 15—Commitments and Contingencies

In October 2000, we sold or contributed industrial properties and undeveloped land with a fair value of \$487 million to a joint venture (Dugan Realty LLC) in which we have a 50% interest and recognized a net gain of \$35.2 million. This transaction expanded an existing joint venture with an institutional real estate investor. As a result of the total transactions, we received \$363.9 million of proceeds. The joint venture partially financed this transaction with \$350 million of secured mortgage debt, the repayment of which we directly or indirectly guaranteed. The guarantee associated with \$260 million of such debt expired in December 2003 without us being required to satisfy the guarantee. The remaining \$90 million of such debt is still guaranteed by us. In connection with this transaction, the joint venture partners were given an option to put up to a \$50 million interest in the joint venture to us in exchange for our common stock or cash (at our option), subject to certain timing and other restrictions. As a result of this put option, we deferred \$10.2 million of gain on sale of depreciated property and recorded a \$50 million liability.

We have guaranteed the repayment of \$12.3 million of economic development bonds issued by various municipalities in connection with certain commercial developments. We will be required to make payments under our guarantees to the extent that incremental taxes from specified developments are not sufficient to pay the bond debt service. Management does not believe that it is probable that we will be required to make any significant payments in satisfaction of these guarantees.

We also have guaranteed the repayment of a \$2 million mortgage loan encumbering the real estate of one of our unconsolidated joint ventures. At December 31, 2005, the outstanding balance on this loan was approximately \$1.2





# Notes to Consolidated Financial Statements

million. Management believes that the value of the real estate exceeds the loan balance and that we will not be required to satisfy this guarantee.

We evaluated all applicable guarantees under FASB Interpretation 45 ("FIN 45") in order to determine whether there is a need to recognize a liability for the obligations under the guarantees. Based upon our review, no liability was recorded at December 31, 2005.

We have entered into agreements, subject to the completion of due diligence requirements, resolution of certain contingencies and completion of customary closing conditions, for the future acquisition of land totaling \$65.0 million. We also have entered into an agreement to acquire an 18 building portfolio for approximately \$194.1 million, which is expected to close in 2006.

We renewed all of our major insurance policies in 2005. These policies include coverage for acts of terrorism for our properties. We believe that this insurance provides adequate coverage against normal insurance risks and that any loss experienced would not have a significant impact on our liquidity, financial position, or results of operations.

We are subject to various legal proceedings and claims that arise in the ordinary course of business. In the opinion of management, the amount of any ultimate liability with respect to these actions will not materially affect our consolidated financial statements or results of operations.

## 16—Subsequent Events

In January 2006, we announced the acquisition of approximately 5.1 million square feet of bulk industrial properties located at the Port of Savannah for a total purchase price of approximately \$194.1 million. The portfolio consists of 18 buildings and is located near one of the fastest growing ports in the country. The properties are 100% leased with a weighted average lease term

of 7.5 years. This transaction makes us the largest industrial property owner in the Savannah area and complements our industrial holdings across the Southeast. In addition, we have the option to acquire future completed development projects on 400 acres of land in the same market.

In January 2006, we issued \$184 million of 6.95% Series M Cumulative Redeemable Preferred Stock, which replaced our \$75 million 8.45% Series I Cumulative Redeemable Preferred Stock that we redeemed in February 2006.

In January 2006, we renewed our unsecured revolving credit facility. The new facility provides borrowing capacity up to \$1 billion and, subject to certain conditions, may be increased to \$1.3 billion. Under the new facility, which replaces the previous unsecured line of credit agreement, the interest rate has been reduced to LIBOR plus 52.5 basis points, the borrowing capacity has been increased by \$500 million and the maturity date has been extended to January 25, 2010.

In February 2006, we issued \$125.0 million of 5.5% senior notes, due 2016.

In February 2006, we acquired 27 suburban office and light industrial buildings, encompassing more than 2.3 million square feet from the Mark Winkler Company for \$619.0 million. The 27 buildings are part of a 32 building portfolio located in three primary submarkets in Northern Virginia. We will close on the remaining five buildings in the portfolio throughout the first and second quarters of 2006. In addition to the 27 buildings we also closed on approximately 166 acres of undeveloped land located in major business parks that can support the future development of approximately 3.7 million square feet of office and industrial buildings. In connection with the acquisition, we obtained a \$700 million secured term loan priced at LIBOR plus 52.5 basis points with a scheduled maturity date of September 2006. Subject to Lender's approval, the maturity date may be extended to March 2007.





## Selected Quarterly Financial Information (Unaudited)

Selected quarterly information for the years ended December 31, 2005 and 2004 is as follows (in thousands, except per share amounts):

	Quarter Ended			
	December 31	September 30	June 30	March 31
2005				
Revenues from continuing Rental Operations	\$ 185,509	\$ 177,141	\$ 176,930	\$ 166,603
Revenues from continuing Service Operations	13,914	22,584	23,748	21,695
Net income available for common shareholders	30,055	213,348	40,299	25,481
Basic income per common share	\$ 0.22	\$ 1.50	\$ 0.28	\$ 0.18
Diluted income per common share	\$ 0.22	\$ 1.48	\$ 0.28	\$ 0.18
Weighted average common shares	136,855	142,663	143,480	143,089
Weighted average common and dilutive potential common shares	151,145	158,468	157,696	157,720
Funds From Operations <sup>(1)</sup>	\$ 84,548	\$ 87,175	\$ 87,841	\$ 81,625
2004				
Revenues from continuing Rental Operations	\$ 165,982	\$ 163,486	\$ 156,328	\$ 155,359
Revenues from continuing Service Operations	27,195	17,434	14,739	11,435
Net income available for common shareholders	41,150	42,527	34,716	32,886
Basic income per common share	\$ 0.29	\$ 0.30	\$ 0.24	\$ 0.24
Diluted income per common share	\$ 0.29	\$ 0.30	\$ 0.24	\$ 0.23
Weighted average common shares	142,716	142,273	142,104	138,398
Weighted average common and dilutive potential common shares	157,350	157,105	156,828	156,913
Funds From Operations <sup>(1)</sup>	\$ 95,487	\$ 89,277	\$ 86,724	\$ 80,981

<sup>(1)</sup> Funds From Operations ("FFO") is used by industry analysts and investors as a supplemental operating performance measure of an equity real estate investment trust ("REIT"). FFO is calculated in accordance with the definition that was adopted by the Board of Governors of the National Association of Real Estate Investment Trusts ("NAREIT"). FFO, as defined by NAREIT, represents net income (loss) determined in accordance with generally accepted accounting principles ("GAAP"), excluding extraordinary items as defined under GAAP and gains or losses from sales of previously depreciated operating real estate assets, plus certain non-cash items such as real estate asset depreciation and amortization, and after similar adjustments for unconsolidated partnerships and joint ventures.

Historical cost accounting for real estate assets in accordance with GAAP implicitly assumes that the value of real estate assets diminishes predictably over time. Since real estate values instead have historically risen or fallen with market conditions, many industry investors and analysts have considered the presentation of operating results for real estate companies that use historical cost accounting to be insufficient by themselves. Thus, NAREIT created FFO as a supplemental measure of REIT operating performance that excludes historical cost depreciation, among other items, from GAAP net income. Management believes that the use of FFO, combined with the required primary GAAP presentations, has improved the understanding of operating results of REITs among the investing public and made comparisons of REIT operating results more meaningful. Management considers FFO to be a useful measure for reviewing comparative operating and financial performance (although FFO should be reviewed in conjunction with net income which remains the primary measure of performance) because by excluding gains or losses related to sales of previously depreciated operating real estate assets and excluding real estate asset depreciation and amortization, FFO assists in comparing the operating performance of a company's real estate between periods or as compared to different companies.





# Directors and Management

## 2005 Board of Directors Unaffiliated Directors

Barrington H. Branch  
President  
The Branch-Shelton Company

Geoffrey Button  
Independent Real Estate  
and Financing Consultant

William Cavanaugh III  
Chairman  
World Association of  
Nuclear Operators

Ngaire E. Cuneo  
Partner  
Red Associates, LLC

Charles R. Eitel  
Chairman, CEO  
The Simmons Company

Dr. R. Glenn Hubbard  
Dean and Russell L. Carson Professor of  
Finance and Economics  
Columbia University,  
Graduate School of Business

Dr. Martin C. Jischke  
President  
Purdue University

L. Ben Lytle  
Chairman, CEO  
AXIA Health Management, LLC

William O. McCoy  
Partner  
Franklin Street Partners

Jack R. Shaw  
Vice President, Treasurer  
The Regenstrief Foundation

Robert J. Woodward, Jr.  
Chairman  
Palmer-Donavin Manufacturing Co.

## Affiliated Directors

Dennis D. Oklak  
Chairman, CEO

John W. Nelley, Jr.  
Managing Director  
Nashville Operations

## Board Committees

### Audit

Jack R. Shaw (Chair)  
Geoffrey Button  
Ngaire E. Cuneo  
Robert J. Woodward, Jr.

### Executive Compensation

Charles R. Eitel (Chair)  
Barrington H. Branch  
Dr. R. Glenn Hubbard  
Dr. Martin C. Jischke

### Finance

Robert J. Woodward, Jr. (Chair)  
Geoffrey Button  
Ngaire E. Cuneo  
Jack R. Shaw

### Corporate Governance

L. Ben Lytle (Chair and Lead Director)  
William Cavanaugh III  
William O. McCoy

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## Executive Committee

Dennis D. Oklak  
Chairman and  
Chief Executive Officer

Robert M. Chapman  
Senior Executive Vice President  
Head of Real Estate Operations

Matthew A. Cohoat  
Executive Vice President  
Chief Financial Officer

James B. Connor  
Executive Vice President  
Chicago Region

Howard L. Feinsand  
Executive Vice President  
General Counsel and Secretary

Donald J. Hunter  
Executive Vice President  
Indianapolis Region

Steven R. Kennedy  
Executive Vice President  
Construction

Kevin T. Rogus  
Executive Vice President  
Phoenix Region

Chris L. Seger  
Executive Vice President  
National Development/Construction

Denise K. Dank  
Senior Vice President  
Human Resources

Paul R. Quinn  
Senior Vice President  
Chief Information Officer





## Market Price and Dividends

The Company's common shares are listed for trading on the New York Stock Exchange under the symbol "DRE." The following table sets forth the high, low and closing sales prices of the common stock for the periods indicated and the dividend paid per share during such period.

Quarter Ended	2005				2004			
	High	Low	Close	Dividend	High	Low	Close	Dividend
December 31	\$35.09	\$31.22	\$33.40	\$0.470	\$36.00	\$32.78	\$34.14	\$0.465
September 30	34.30	30.77	33.88	0.470	34.70	30.46	33.20	0.465
June 30	32.25	29.28	31.66	0.465	35.16	27.49	31.81	0.460
March 31	34.37	29.45	29.85	0.465	34.73	30.44	34.72	0.460

On January 25, 2006, the Company declared a quarterly cash dividend of \$0.47 per share, payable on February 28, 2006, to common shareholders of record on February 14, 2006.

## Shareholder Information

### Corporate Headquarters

600 East 96th Street, Suite 100  
Indianapolis, IN 46240  
317.808.6000

### Transfer Agent

For Dividend Payments, Address Changes, Account Inquiry and/or Registration Changes, visit [www.amstock.com](http://www.amstock.com), or submit a written request to:

American Stock Transfer & Trust Company  
59 Maiden Lane  
New York, NY 10038  
800.937.5449 or 212.936.5100

### Common Stock Information

Symbol: DRE  
Exchange: NYSE

### Shareholder Contact

For Shareholder Mailings and Company Information:

Duke Realty Corporation  
Attn: Investor Relations  
600 East 96th Street, Suite 100  
Indianapolis, IN 46240  
317.808.6005 or 800.875.3366  
317.808.6770 FAX  
IR@dukerealty.com  
[www.dukerealty.com](http://www.dukerealty.com)

### Shareholder Services

#### Direct Stock Purchase and Dividend Reinvestment Plan

The Duke Direct Stock Purchase Plan offers participants a convenient and economical method to purchase the Company's common stock, and to reinvest their dividends. Specific features of the Plan include:

- Automatic dividend reinvestment
- Optional cash investment availability twice per month
- Automatic purchase program
- Available to first-time investors
- Certificate safekeeping
- No commissions or fees on purchases

Shares sold through this Plan are offered through a prospectus which can be obtained by writing to Investor Relations at the Corporate Headquarters address or by calling American Stock Transfer & Trust Company at 1.800.278.4353 or 1.800.937.5449, or by visiting the Investor Information section of the Company's website at [www.dukerealty.com](http://www.dukerealty.com).

Shares may also be purchased on-line by visiting the Investor Information section of the Company's website or by visiting [www.investpower.com](http://www.investpower.com).

#### Direct Deposit of Dividends

Shareholders who hold their Duke shares in registered or certificate form can have their common stock dividends automatically deposited into their bank accounts. Information about this direct deposit program can be obtained by contacting the Company's Investor Relations department or American Stock Transfer & Trust Company.

### Management Certifications

In accordance with Section 303A.12(a) of the NYSE Listed Company Manual, the CEO of the Company provided a Section 12(a) annual certification, which stated that he was not aware of any violations by the Company of the NYSE corporate governance listing standards. In accordance with Section 302 of the Sarbanes-Oxley Act of 2002, the CEO and CFO of the Company also provided Section 302 certifications, which were filed with the SEC as exhibits to the Company's Annual Report on Form 10-K.

When used in this Annual Report, the word "believes," "expects," "estimates" and similar expressions are intended to identify forward-looking statements. Such statements are subject to certain risks and uncertainties which could cause actual results to differ materially. In particular, among the factors that could cause actual results to differ materially are continued qualification as a real estate investment trust, general business and economic conditions, competition, increases in real estate construction costs, interest rates, accessibility of debt and equity capital markets and other risks inherent in the real estate business including tenant defaults, potential liability relating to environmental matters and liquidity of real estate investments. Readers are advised to refer to Duke's Form 8-K Report as filed with the Securities and Exchange Commission on July 24, 2003 for additional information concerning these risks.





## Indianapolis Headquarters

### Office/National Development/Retail/Medical Office

600 East 96th Street, Suite 100, Indianapolis, IN 46240  
317.808.6000

### Industrial

7225 Woodland Drive, Indianapolis, IN 46278  
317.808.6800

### Atlanta

3950 Shackleford Road, Suite 300  
Duluth, GA 30096  
770.717.3200

### Chicago

6133 North River Road, Suite 200  
Rosemont, IL 60018  
847.232.5400

### Cincinnati

4555 Lake Forest Drive, Suite 400  
Cincinnati, OH 45242  
513.956.4400

### Cleveland

6150 Oak Tree Boulevard, Suite 550  
Cleveland, OH 44131  
216.643.6000

### Columbus

5600 Blazer Parkway, Suite 100  
Dublin, OH 43017  
614.932.6000

### Dallas

5495 Belt Line Road, Suite 360  
Dallas, TX 75254  
972.361.6700

### Houston

1990 Post Oak Boulevard, Suite 2450  
Houston, TX 77056  
713.871.1086

### Indianapolis

600 East 96th Street, Suite 100  
Indianapolis, IN 46240  
317.808.6000

### Minneapolis

1600 Utica Avenue South, Suite 250  
Minneapolis, MN 55416  
952.543.2900

### Nashville

782 Melrose Avenue  
Nashville, TN 37211  
615.884.2300

### Northern Virginia

4900 Seminary Road, Suite 900  
Alexandria, VA 22311  
703.998.0400

### Orlando

4700 Millenia Boulevard, Suite 380  
Orlando, FL 32839  
407.241.0000

### Phoenix

2375 East Camelback Road, 5th Floor  
Phoenix, AZ 85016  
602.387.5143

### Raleigh

1800 Perimeter Park Drive, Suite 200  
Morrisville, NC 27560  
919.461.8000

### South Florida

2400 North Commerce Parkway, Suite 405  
Weston, FL 33326  
954.385.1909

### St. Louis

520 Maryville Centre Drive, Suite 200  
St. Louis, MO 63141  
314.514.6700

### Tampa

10150 Highland Manor Drive, Suite 150  
Tampa, FL 33610  
813.635.8500

