WASHINGTON REAL ESTATE INVESTMENT TRUST
Form 10-Q
July 31, 2013

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

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For quarterly period ended June 30, 2013
OR
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.
COMMISSION FILE NO. 1-6622
WASHINGTON REAL ESTATE
INVESTMENT TRUST
(Exact name of registrant as specified in its charter)

MARYLAND	53-0261100
(State of incorporation)	(IRS Employer Identification Number)

6110 EXECUTIVE BOULEVARD, SUITE 800, ROCKVILLE, MARYLAND 20852
(Address of principal executive office) (Zip code)
Registrant's telephone number, including area code: (301) 984-9400

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of exchange on which registered
Shares of Beneficial Interest	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

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

Indicate by checkmark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES x NO o

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

Large accelerated filer	x	Accelerated filer	o
Non-accelerated filer	o	Smaller reporting company	o

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

As of July 30, 2013, 66,500,381 common shares were outstanding.

WASHINGTON REAL ESTATE INVESTMENT TRUST
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PART I
FINANCIAL INFORMATION

ITEM 1: FINANCIAL STATEMENTS

The information furnished in the accompanying unaudited Consolidated Balance Sheets, Condensed Consolidated Statements of Income, Consolidated Statement of Shareholders' Equity and Consolidated Statements of Cash Flows reflects all adjustments, consisting of normal recurring items, which are, in the opinion of management, necessary for a fair presentation of the financial position, results of operations and cash flows for the interim periods. The accompanying financial statements and notes thereto should be read in conjunction with the financial statements and notes for the three years ended December 31, 2012 included in WRIT’s 2012 Annual Report on Form 10-K.

WASHINGTON REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS, EXCEPT PER SHARE DATA)

	June 30, 2013 (Unaudited)	December 31, 2012
Assets		
Land	$483,198	$483,198
Income producing property	2,003,826	1,979,348
	2,487,024	2,462,546
Accumulated depreciation and amortization	(646,993)	(604,614)
Net income producing property	1,840,031	1,857,932
Properties under development or held for future development	55,262	49,135
Total real estate held for investment, net	1,895,293	1,907,067
Investment in real estate sold or held for sale, net	—	11,528
Cash and cash equivalents	5,919	19,324
Restricted cash	10,839	14,582
Rents and other receivables, net of allowance for doubtful accounts of $9,585 and $10,958, respectively	60,100	57,076
Prepaid expenses and other assets	108,591	114,541
Other assets related to properties sold or held for sale	—	258
Total assets	$2,080,742	$2,124,376
Liabilities		
Notes payable	$846,450	$906,190
Mortgage notes payable	312,211	342,970
Lines of credit	75,000	—
Accounts payable and other liabilities	51,715	52,823
Advance rents	14,239	16,096
Tenant security deposits	9,899	9,936
Other liabilities related to properties sold or held for sale	—	218
Total liabilities	1,309,514	1,328,233
Equity		
Shareholders’ equity		
Preferred shares; $0.01 par value; 10,000 shares authorized; no shares issued or outstanding	—	—
Shares of beneficial interest; $0.01 par value; 100,000 shares authorized: 66,500 and 66,437 shares issued and outstanding at June 30, 2013 and December 31, 2012, respectively	665	664
Additional paid in capital	1,147,710	1,145,515
Distributions in excess of net income	(381,623)	(354,122)
Total shareholders’ equity	766,752	792,057
Noncontrolling interests in subsidiaries	4,476	4,086
Total equity	771,228	796,143
Total liabilities and equity	$2,080,742	$2,124,376

See accompanying notes to the consolidated financial statements.

WASHINGTON REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Revenue				
Real estate rental revenue	$78,272	$75,590	$155,196	$150,804
Expenses				
Real estate expenses	27,429	25,033	54,520	50,584
Depreciation and amortization	25,582	25,227	51,106	50,809
Acquisition costs	87	254	300	308
General and administrative	4,005	4,164	7,867	7,770
	57,103	54,678	113,793	109,471
Real estate operating income	21,169	20,912	41,403	41,333
Other income (expense)				
Interest expense	(16,152)	(15,470)	(32,670)	(31,301)
Other income	246	252	485	496
	(15,906)	(15,218)	(32,185)	(30,805)
Income from continuing operations	5,263	5,694	9,218	10,528
Discontinued operations:				
Income from operations of properties sold or held for sale	—	314	185	661
Gain on sale of real estate	—	—	3,195	—
Net income	5,263	6,008	12,598	11,189
Less: Net income attributable to noncontrolling interests in subsidiaries	—	—	—	—
Net income attributable to the controlling interests	$5,263	$6,008	$12,598	$11,189
Basic net income per share:				
Continuing operations	$0.08	$0.08	$0.14	$0.15
Discontinued operations	—	0.01	0.05	0.01
Net income per share	$0.08	$0.09	$0.19	$0.16
Diluted net income per share:				
Continuing operations	$0.08	$0.08	$0.14	$0.15
Discontinued operations	—	0.01	0.05	0.01
Net income per share	$0.08	$0.09	$0.19	$0.16
Weighted average shares outstanding – basic	66,405	66,241	66,399	66,218
Weighted average shares outstanding – diluted	66,556	66,380	66,537	66,354
Dividends declared per share	$0.3000	$0.4338	$0.6000	$0.8676

See accompanying notes to the consolidated financial statements.

WASHINGTON REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY
(IN THOUSANDS)
(UNAUDITED)

	Shares Outstanding	Shares of Beneficial Interest at Par Value	Additional Paid in Capital	Distributions in Excess of Net Income Attributable to the Controlling Interests	Total Shareholders' Equity	Noncontrolling Interests in Subsidiaries	Total Equity
Balance, December 31, 2012	66,437	$ 664	$1,145,515	$ (354,122)	$ 792,057	$ 4,086	$796,143
Net income attributable to the controlling interests	—	—	—	12,598	12,598	—	12,598
Contributions from noncontrolling interests	—	—	—	—	—	390	390
Dividends	—	—	—	(40,099)	(40,099)	—	(40,099)
Share grants, net of share grant amortization and forfeitures	63	1	2,195	—	2,196	—	2,196
Balance, June 30, 2013	66,500	$ 665	$1,147,710	$ (381,623)	$ 766,752	$ 4,476	$771,228

See accompanying notes to the consolidated financial statements.

WASHINGTON REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)
(UNAUDITED)

	Six Months Ended June 30, 2013	2012
Cash flows from operating activities		
Net income	$12,598	$11,189
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization, including amounts in discontinued operations	51,106	51,585
Provision for losses on accounts receivable	2,291	2,013
Gain on sale of real estate	(3,195)	—
Amortization of share grants, net	2,390	2,763
Amortization of debt premiums, discounts and related financing costs	1,989	1,885
Changes in operating other assets	(1,515)	(4,609)
Changes in operating other liabilities	(2,671)	2,294
Net cash provided by operating activities	62,993	67,120
Cash flows from investing activities		
Real estate acquisitions, net	—	(52,142)
Net cash received for sale of real estate	15,161	—
Capital improvements to real estate	(25,069)	(21,525)
Development in progress	(6,505)	(2,218)
Real estate deposits	(3,900)	—
Non-real estate capital improvements	(109)	(415)
Net cash used in investing activities	(20,422)	(76,300)
Cash flows from financing activities		
Line of credit borrowings, net	75,000	122,000
Dividends paid	(40,099)	(57,807)
Net contributions from noncontrolling interests	390	88
Financing costs	—	(1,967)
Proceeds from dividend reinvestment program	—	1,345
Principal payments – mortgage notes payable	(31,267)	(2,900)
Notes payable repayments	(60,000)	(50,000)
Net proceeds from exercise of share options	—	23
Net cash (used in) provided by financing activities	(55,976)	10,782
Net (decrease) increase in cash and cash equivalents	(13,405)	1,602
Cash and cash equivalents at beginning of period	19,324	12,765
Cash and cash equivalents at end of period	$5,919	$14,367
Supplemental disclosure of cash flow information:		
Cash paid for interest, net of amounts capitalized	$32,643	$29,995
Decrease (increase) in accrued capital improvements and development costs	$683	$(3,103)

See accompanying notes to the consolidated financial statements.

WASHINGTON REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2013
(UNAUDITED)

NOTE 1: NATURE OF BUSINESS

Washington Real Estate Investment Trust ("WRIT"), a Maryland real estate investment trust, is a self-administered, self-managed equity real estate investment trust, successor to a trust organized in 1960. Our business consists of the ownership and operation of income-producing real estate properties in the greater Washington metro region. We own a diversified portfolio of office buildings, medical office buildings, multifamily buildings and retail centers.

Federal Income Taxes

We believe that we qualify as a real estate investment trust ("REIT") under Sections 856-860 of the Internal Revenue Code and intend to continue to qualify as such. To maintain our status as a REIT, we are required to distribute 90% of our ordinary taxable income to our shareholders. When selling properties, we have the option of (a) reinvesting the sales proceeds of properties sold, allowing for a deferral of income taxes on the sale, (b) paying out capital gains to the shareholders with no tax to WRIT or (c) treating the capital gains as having been distributed to the shareholders, paying the tax on the gain deemed distributed and allocating the tax paid as a credit to the shareholders.

Generally, and subject to our ongoing qualification as a REIT, no provisions for income taxes are necessary except for taxes on undistributed REIT taxable income and taxes on the income generated by our taxable REIT subsidiaries ("TRSs"). Our TRSs are subject to corporate federal and state income tax on their taxable income at regular statutory rates. There were no material income tax provisions or material net deferred income tax items for our TRSs for the three and six months ended June 30, 2013 and 2012.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND BASIS OF PRESENTATION

Significant Accounting Policies

We have prepared our consolidated financial statements using the accounting policies described in our Annual Report on Form 10-K for the year ended December 31, 2012.

Principles of Consolidation and Basis of Presentation

The accompanying unaudited consolidated financial statements include the consolidated accounts of WRIT, our majority-owned subsidiaries and entities in which WRIT has a controlling interest, including where WRIT has been determined to be a primary beneficiary of a variable interest entity ("VIE"). See note 3 for additional information on the properties for which there is a noncontrolling interest. All intercompany balances and transactions have been eliminated in consolidation.

We have prepared the accompanying unaudited financial statements pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and note disclosures normally included in annual financial statements prepared in accordance with U.S. generally accepted accounting principles ("GAAP") have been condensed or omitted pursuant to those rules and regulations, although we believe that the disclosures made are adequate to make the information presented not misleading. In addition, in the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of the results for the periods presented have been included. These unaudited financial statements should be read in conjunction with the financial statements and notes included in our Annual Report on Form 10-K for the year ended December 31, 2012.

Within these notes to the financial statements, we refer to the three months ended June 30, 2013 and June 30, 2012 as the "2013 Quarter" and the "2012 Quarter," respectively, and the six months ended June 30, 2013 and June 30, 2012 as the "2013 Period" and the "2012 Period," respectively.

Use of Estimates in the Financial Statements

The preparation of financial statements in conformity with GAAP requires management to make certain 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 reporting period. Actual results could differ from those estimates.

Reclassifications

Certain prior year amounts have been reclassified to conform to the current year presentation due to the reclassification of certain properties as discontinued operations (see note 3).

NOTE 3: REAL ESTATE

Variable Interest Entities

In June 2011, we executed a joint venture operating agreement with a real estate development company to develop a mid-rise multifamily property at 650 North Glebe Road in Arlington, Virginia. We estimate the total cost of the project to be $49.9 million. During the first quarter of 2013, we secured third-party debt financing for approximately 70% of the project's cost. WRIT is the 90% owner of the joint venture, and will have management and leasing responsibilities when the project is completed and stabilized (defined as 90% of the residential units leased). The real estate development company owns 10% of the joint venture and is responsible for the development and construction of the property. The joint venture currently expects to complete this development project during the fourth quarter of 2014.

In November 2011, we executed a joint venture operating agreement with a real estate development company to develop a high-rise multifamily property at 1225 First Street (formerly 1219 First Street) in Alexandria, Virginia. We estimate the total cost of the project to be $95.3 million, with approximately 70% of the project to be financed with debt. WRIT is the 95% owner of the joint venture and will have management and leasing responsibilities when the project is completed and stabilized. The real estate development company owns 5% of the joint venture and is responsible for the development and construction of the property. During the first quarter of 2013, we decided to delay commencement of construction, due to market conditions and concerns of oversupply, and stopped capitalizing interest costs on this project. We will reassess this project on a periodic basis going forward.

We have determined that the 650 North Glebe Road and 1225 First Street joint ventures are variable interest entities (“VIE's”) primarily based on the fact that the equity investment at risk is not sufficient to permit either entity to finance its activities without additional financial support. We expect that 70% of the total development costs will be financed through debt. We have also determined that WRIT is the primary beneficiary of each VIE due to the fact that WRIT is providing 90% to 95% of the equity contributions and will manage each property after stabilization.

We include the joint venture land acquisitions on our consolidated balance sheets in properties under development or held for future development. As of June 30, 2013 and December 31, 2012, the land and capitalized development costs are as follows (in thousands):

	June 30, 2013	December 31, 2012
650 North Glebe	$19,904	$15,646
1225 First Street	21,576	19,807

As of June 30, 2013 and December 31, 2012, the accounts payable and accrued liabilities related to the joint ventures are as follows (in thousands):

	June 30, 2013	December 31, 2012
650 North Glebe	$1,089	$115
1225 First Street	394	1,676

On February 21, 2013, WRIT, through its consolidated joint venture to develop a mid-rise multifamily property at 650 North Glebe Road, entered into a construction loan agreement with Citizens Bank for $33.0 million. The loan bears interest at LIBOR plus 2.15%, which decreases to LIBOR plus 2.0% upon completion of construction and the joint venture not being in default. The loan matures on February 21, 2016, with two one year extension options exercisable by the joint venture, subject to fees and compliance with certain provisions in the loan agreement. As of June 30, 2013, the consolidated joint venture had $0.4 million outstanding on this construction loan agreement.

Discontinued Operations

We dispose of assets that no longer meet our long-term strategy or return objectives and where market conditions for sale are favorable. The proceeds from the sales may be reinvested into other properties, used to fund development operations or to support other corporate needs, or distributed to our shareholders. Properties are considered held for sale when they meet the criteria specified (see "Discontinued Operations" in note 2 of the consolidated financial statements included in WRIT's Annual Report on Form 10-K for the year ended December 31, 2012). Depreciation on these properties is discontinued at that time, but operating revenues, other operating expenses and interest continue to be recognized until the date of sale.

We classified as held for sale or sold the following properties in 2013 and 2012:

Disposition Date	Property Name	Segment	Rentable Square Feet	Contract Purchase Price (In thousands)
March 19, 2013	Atrium Building	Office	79,000	$15,750
August 31, 2012	1700 Research Boulevard	Office	101,000	$14,250
December 20, 2012	Plumtree Medical Center	Medical Office	33,000	8,750
		Total 2012	134,000	$23,000

Income from operations of properties sold or held for sale for the three and six months ended June 30, 2013 and 2012 were as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Revenues	$—	$1,187	347	2,472
Property expenses	—	(446)	(162)	(908)
Depreciation and amortization	—	(364)	—	(776)
Interest expense	—	(63)	—	(127)
	$—	$314	$185	$661

Income from operations of properties sold or held for sale by property for the three and six months ended June 30, 2013 and 2012 were as follows (in thousands):

		Three Months Ended June 30,		Six Months Ended June 30,	
Property	Segment	2013	2012	2013	2012
1700 Research Boulevard	Office	$—	$74	—	118
Atrium Building	Office	—	225	185	514
Plumtree Medical Center	Medical Office	—	15	—	29
		$—	$314	$185	$661

NOTE 4: MORTGAGE NOTES PAYABLE

On January 11, 2013, we repaid without penalty the remaining $30.0 million of principal on the mortgage note secured by West Gude Drive.

NOTE 5: UNSECURED LINES OF CREDIT PAYABLE

As of June 30, 2013, we maintained a $100.0 million unsecured line of credit maturing in June 2015 ("Credit Facility No. 1") and a $400.0 million unsecured line of credit maturing in July 2016 ("Credit Facility No. 2"). Credit Facilities No. 1 and No. 2 have accordion features that allow us to increase the facilities to $200.0 million and $600.0 million, respectively, subject to additional lender commitments. The amounts of these lines of credit unused and available at June 30, 2013 are as follows (in thousands):

	Credit Facility No. 1	Credit Facility No. 2
Committed capacity	$100,000	$400,000
Borrowings outstanding	(15,000)	(60,000)
Unused and available	$85,000	$340,000

We executed borrowings and repayments on the unsecured lines of credit during the 2013 Period as follows (in thousands):

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	Credit Facility No. 1	Credit Facility No. 2
Balance at December 31, 2012	$—	$—
Borrowings	30,000	60,000
Repayments	(15,000)	—
Balance at June 30, 2013	$15,000	$60,000

We made borrowings during the 2013 Period to pay off the West Gude mortgage note, repay our 5.125% unsecured notes and for general corporate purposes. We made repayments during the 2013 Period using proceeds from the sale of The Atrium Building and cash from operations.

NOTE 6: NOTES PAYABLE

We repaid without penalty the remaining $60.0 million of our 5.125% unsecured notes on their due date of March 15, 2013, using borrowings on our unsecured line of credit.

NOTE 7: STOCK BASED COMPENSATION

WRIT maintains short-term ("STIP") and long-term ("LTIP") incentive plans that allow for stock-based awards to officers and non-officer employees. Stock based awards are provided to officers and non-officer employees, as well as trustees, under the Washington Real Estate Investment Trust 2007 Omnibus Long-Term Incentive Plan which allows for awards in the form of restricted shares, restricted share units, options and other awards up to an aggregate of 2,000,000 shares over the ten year period in which the plan will be in effect. Restricted share units are converted into shares of our stock upon full vesting through the issuance of new shares.

Total Compensation Expense

Total compensation expense recognized in the consolidated financial statements for all outstanding share based awards was $1.4 million and $1.3 million for the 2013 and 2012 Quarters, respectively, and $2.4 million and $2.7 million for the 2013 and 2012 Periods, respectively.

Restricted Share Awards

During the 2013 Period, 102,966 restricted share grants were awarded at a weighted average grant date fair value of $26.98.

The total fair values of restricted share grants vested was $0.7 million and $0.3 million for the 2013 and 2012 Periods, respectively.

The total unvested restricted share awards at June 30, 2013 was 226,475 shares, which had a weighted average grant date fair value of $27.25 per share.

As of June 30, 2013, the total compensation cost related to non-vested restricted share awards was $2.8 million, which we expect to recognize over a weighted average period of 12 months.

During the first quarter of 2013, our president and Chief Executive Officer announced his intention to retire from WRIT at the end of 2013. As such, we have entered into a separation and general release agreement with the executive dated July 23, 2013, the terms of which were previously disclosed on a Current Report on Form 8-K dated January 28, 2013. The agreement includes a modification to certain of his stock awards. In addition, the agreement provides for the payment of consulting fees during 2014 and 2015 totaling $0.5 million, which will be expensed during the fourth quarter of 2013.

NOTE 8: FAIR VALUE DISCLOSURES

Assets and Liabilities Measured at Fair Value

For assets and liabilities measured at fair value on a recurring basis, quantitative disclosures about the fair value measurements are required to be disclosed separately for each major category of assets and liabilities, as follows:

Level 1: Quoted prices in active markets for identical assets

Level 2: Significant other observable inputs
Level 3: Significant unobservable inputs