

Whitestone REIT
Form S-11/A
June 03, 2010
Table of Contents

Index to Financial Statements

As filed with the Securities and Exchange Commission on June 3, 2010

Registration No. 333-162859

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Amendment No. 1

to

Form S-11

FOR REGISTRATION UNDER THE SECURITIES ACT OF 1933

OF SECURITIES OF CERTAIN REAL ESTATE COMPANIES

Whitestone REIT

(Exact name of registrant as specified in governing instruments)

2600 South Gessner, Suite 500

Houston, Texas 77063

Edgar Filing: Whitestone REIT - Form S-11/A

(713) 827-9595

(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

James C. Mastandrea

President and Chief Executive Officer

Whitestone REIT

2600 South Gessner, Suite 500

Houston, Texas 77063

(713) 827-9595

(Name, address, including zip code, and telephone number, including area code, of agent for service)

Copies to:

**John A. Good, Esq.
Eric J. Loumeau, Esq.
Bass, Berry & Sims PLC
The Tower at Peabody Place
100 Peabody Place, Suite 900
Memphis, TN 38103
(901) 543-5900**

**David C. Wright, Esq.
Douglas M. Berman, Esq.
Hunton & Williams LLP
Riverfront Plaza, East Tower
951 East Byrd Street
Richmond, VA 23219
(804) 788-8200**

Approximate date of commencement of proposed sale to the public: As soon as practicable after the effective date of this Registration Statement.

If any of the Securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act, check the following box: "

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. "

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration number of the earlier effective registration statement for the same offering. "

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. "

Edgar Filing: Whitestone REIT - Form S-11/A

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box.

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

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

The registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the registration statement shall become effective on such dates as the Commission, acting pursuant to said Section 8(a), may determine.

Table of Contents

Index to Financial Statements

The information in this prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

Subject to completion, dated June 3, 2010

Class B Common Shares

Whitestone REIT is a fully integrated, internally managed real estate company founded in 1998 that seeks to own and operate Community Centered Properties, which we define as visibly located properties in established or developing, culturally diverse neighborhoods in our target markets. We conduct our operations so as to qualify as a real estate investment trust, or REIT, for federal income tax purposes.

We are selling all of the Class B common shares of beneficial interest offered by this prospectus. We currently expect the public offering price to be between \$ and \$ per share. Our Class B common shares are currently not listed or traded on an exchange or in any other public market. Our Class B common shares have been approved for listing on the NYSE Amex, subject to official notice of issuance, under the symbol WSR.

Our declaration of trust contains certain restrictions relating to the ownership and transfer of our Class B common shares, including, subject to certain exceptions, a limit on ownership of more than 9.8% in value or number of shares, whichever is more restrictive, of our outstanding Class B common shares. See Description of Securities Restrictions on Ownership and Transfer.

Investing in our Class B common shares involves a high degree of risk. See Risk Factors beginning on page 15 of this prospectus for a discussion of the following and other risks that you should consider before investing:

Recent market disruptions have continued to adversely affect our occupancy, rental rates and access to capital and may significantly and negatively affect our financial condition and results of operations in the future.

Current conditions in the credit markets could adversely affect our ability to refinance existing indebtedness or obtain additional financing on acceptable terms or at all.

Current lack of geographic diversification of our portfolio leaves us vulnerable to an economic downturn in Texas, and particularly the Houston metropolitan area.

We lease our properties to approximately 800 tenants and face the risk of non-renewal on approximately 10% to 20% of our leases which expire each year, along with the corresponding cost of re-leasing that space.

If we fail to maintain our status as a REIT for federal income tax purposes, our distributions to shareholders will not be deductible by us, and we will pay substantial corporate-level income and excise taxes, reducing our earnings available for distribution.

There can be no assurance that we will be able to pay or maintain cash dividends or that dividends will increase over time.

	Per Share	Total
Public offering price	\$	\$
Underwriting discount and commissions	\$	\$
Net proceeds to us, before expenses	\$	\$

We have granted the underwriters an option to purchase up to an additional _____ Class B common shares from us at the public offering price within 30 days after the date of this prospectus solely to cover over-allotments, if any.

The underwriters expect to deliver the Class B common shares on or about _____, 2010.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

Wunderlich Securities

Ladenburg Thalmann & Co. Inc.

J.J.B. Hilliard, W.L. Lyons, LLC

Southwest Securities, Inc.

The date of this prospectus is _____, 2010.

Table of Contents

Index to Financial Statements

TABLE OF CONTENTS

	Page
<u>Prospectus Summary</u>	2
<u>Risk Factors</u>	15
<u>Forward-Looking Statements</u>	32
<u>Use of Proceeds</u>	33
<u>Reclassification of Common Shares</u>	34
<u>Distribution Policy</u>	35
<u>Capitalization</u>	37
<u>Dilution</u>	38
<u>Selected Consolidated Financial and Other Data</u>	40
<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	43
<u>Business and Properties</u>	60
<u>Policies With Respect To Certain Activities</u>	77
<u>Management</u>	84
<u>Principal Shareholders</u>	102
<u>Certain Relationships and Related Transactions</u>	104
<u>The Operating Partnership Agreement</u>	106
<u>Description of Securities</u>	110
<u>Certain Provisions of Maryland Law and of our Declaration of Trust and Bylaws</u>	115
<u>Shares Eligible for Future Sale</u>	121
<u>Material U.S. Federal Income Tax Considerations</u>	123
<u>ERISA Considerations</u>	145
<u>Underwriting</u>	149
<u>Legal Matters</u>	152
<u>Experts</u>	152
<u>Where You Can Find More Information</u>	152
<u>Index To Consolidated Financial Statements</u>	F-1

You should rely only on the information contained in this prospectus. We have not authorized anyone to provide you with information that is different from that contained in this prospectus. We are offering to sell Class B common shares and seeking offers to buy Class B common shares only in jurisdictions where offers and sales are permitted. The information contained in this prospectus is accurate only as of the date of this prospectus, regardless of the time of delivery of this prospectus or of any sale of Class B common shares.

Table of Contents

Index to Financial Statements

PROSPECTUS SUMMARY

You should read the following summary together with the more detailed information regarding our company and the financial statements appearing elsewhere in this prospectus, including under the caption Risk Factors. Unless the context suggests otherwise, references in this prospectus to our company, we, us, and our mean Whitestone REIT, a Maryland real estate investment trust, and its consolidated subsidiaries, including Whitestone REIT Operating Partnership, L.P., a Delaware limited partnership, of which we are the sole general partner and to which we refer in this prospectus as our Operating Partnership. Unless otherwise indicated, the information included in this prospectus assumes (1) the effectiveness of our Articles of Amendment to our declaration of trust, or the Articles of Amendment, to change the name of our common shares to Class A common shares, (2) the effectiveness of our Articles Supplementary to our declaration of trust, or the Articles Supplementary, to create a new class of common shares entitled Class B common shares, (3) no exercise by the underwriters of the over-allotment option to purchase up to an additional Class B common shares, (4) that the Class B common shares to be sold in this offering are sold at \$ per share, which is the midpoint of the range indicated on the front cover of this prospectus, and (5) that the per unit value of the units of partnership interest in our Operating Partnership, or OP units, that we will purchase with the proceeds of this offering is equal to one-third of the public offering price per share of the Class B common shares indicated on the front cover of this prospectus. Each OP unit is redeemable at the election of the holder for cash, or, at our option, one of our Class A common shares. For more information on our classes of common shares, see Reclassification of Common Shares below.

Overview

We are a fully integrated real estate company that owns and operates commercial properties in culturally diverse markets in major metropolitan areas. Founded in 1998, we are internally managed with a portfolio of 36 commercial properties in Texas, Arizona and Illinois.

In October 2006, our current management team joined the company and adopted a strategic plan to acquire, redevelop, own and operate Community Centered Properties. We define Community Centered Properties as visibly located properties in established or developing culturally diverse neighborhoods in our target markets. We market, lease, and manage our centers to match tenants with the shared needs of the surrounding neighborhood. Those needs may include specialty retail, grocery, restaurants and medical, educational and financial services. Our goal is for each property to become a Whitestone-branded business center or retail community that serves a neighboring five-mile radius around our property. We employ and develop a diverse group of associates who understand the needs of our multicultural communities and tenants.

Our current portfolio is concentrated in Houston, with additional properties in the Phoenix, Chicago, Dallas and San Antonio metropolitan areas. According to the United States Census Bureau's *Estimates of Population Change for Metropolitan Statistical Areas and Rankings: July 1, 2008 to July 1, 2009*, Dallas and Houston ranked first and second, respectively, in population growth out of 366 metropolitan statistical areas, and Phoenix, Chicago and San Antonio ranked seventh, eighth and sixteenth, respectively. We believe the management infrastructure and capacity we have built can accommodate substantial growth in those markets. We also believe that those cities have expanding multi-cultural neighborhoods, providing us with excellent opportunities to execute our strategic plan in those markets.

We believe that over the next three years we will have opportunities to acquire quality properties at historically attractive prices. Many of these properties will be distressed due to over-leverage, mismanagement or the lack of liquidity in the financial markets. We have extensive relationships with community banks, attorneys, title companies and others in the real estate industry which we believe will enable us to take advantage of these market opportunities and maintain an active acquisition pipeline.

Table of Contents

Index to Financial Statements

Our Strengths

We believe a number of factors differentiate us from other commercial real estate owners in our markets, including:

Investment Focus. We seek to invest in properties that are or can become Community Centered Properties from which our tenants deliver needed services to the surrounding community. We focus on niche properties with smaller rental spaces that present opportunities for attractive returns. We target properties that: (1) typically require relatively low capital investment, are management and leasing intensive and do not draw the interest of larger national real estate companies; (2) can be redeveloped at a low cost utilizing our internal management capabilities; and/or (3) can be Whitestone-branded and re-tenanted, resulting in lower tenant turnover and higher occupancy and rental rates, together with corresponding increases in tenant reimbursement of operating expenses.

Multi-Cultural Community Focus. Our multi-cultural community focus sets us apart from traditional commercial real estate operators. We value diversity in our team and maintain in-house leasing, property management, marketing, construction and maintenance departments with culturally diverse and multi-lingual associates who understand the particular needs of our tenants and neighborhoods.

Proactive Marketing and Leasing. Our proactive marketing and leasing programs are designed to utilize market research to determine the common and distinctive characteristics and needs of the neighborhood and attract tenants who meet those needs. Our in-depth local knowledge in each of our major markets and in-house research capabilities allow us to quickly access and analyze neighborhood demographics and cultural nuances, market rental trends and valuation metrics. Our streamlined and efficient leasing process allows us to attract tenants and to lease spaces quickly. We typically market and lease our properties to smaller tenants who rent on average less than 3,000 square feet. As of March 31, 2010, our average rent per square foot for our smaller tenants represents a 40% premium over rent paid by our larger tenants.

Proven Real Estate and Turn-Around Track Record. Our eight-person senior management team has more than 125 years of collective experience acquiring, developing, redeveloping, owning, managing and operating commercial real estate properties, portfolios and companies. Our senior management team has extensive national real estate contacts and investment expertise in our target markets. In particular, our management team has significant expertise in turning around properties with complex problems. Our team executes a coordinated strategy, utilizing our corporate branding, philosophy and culture, operational systems and experience to renovate and re-tenant properties, with an intention to increase their net operating income and value.

Commitment to Associate Training and Development. Our annual in-house Real Estate Executive Development, or REED, program is designed to provide us with knowledgeable and well-trained associates to meet our strategic goals and provide continuity in our leadership and management. The 12-month REED program promotes in-depth understanding of all aspects of investing in, owning and operating commercial real estate by providing select associates with detailed training from real estate professionals from both within and outside Whitestone.

Our Strategy

Our primary business objective is to increase shareholder value by acquiring, owning and operating Community Centered Properties. The key elements of our strategy include:

Strategically Acquiring Properties.

Edgar Filing: Whitestone REIT - Form S-11/A

Seeking High Growth Markets. We seek to strategically acquire commercial properties in high-growth markets. Our acquisition targets are located in densely populated, culturally diverse neighborhoods, primarily in and around Phoenix, Chicago, Dallas, San Antonio and Houston, five of the top 20 markets in the United States in terms of population growth.

Table of Contents

Index to Financial Statements

Diversifying Geographically. Our current portfolio is concentrated in Houston. We believe that continued geographic diversification into markets where we have substantial knowledge and experience will help offset the economic risk from a single market concentration. We intend to focus our expansion efforts on the Phoenix, Chicago, Dallas and San Antonio markets. We believe our management infrastructure and capacity can accommodate substantial growth in those markets. We may also pursue opportunities in other Southwestern and Western regions that are consistent with our Community Centered Property strategy.

Capitalizing on Availability of Distressed Assets. We believe that during the next several years there will be excellent opportunities in our target markets to acquire quality properties at historically attractive prices. We intend to acquire distressed assets directly from owners or financial institutions holding foreclosed real estate and debt instruments that are either in default or on bank watch lists. Many of these assets may benefit from our corporate strategy and our management team's experience in turning around distressed properties, portfolios and companies. We have extensive relationships with community banks, attorneys, title companies, and others in the real estate industry with whom we regularly work to identify properties for potential acquisition.

Redeveloping and Re-tenanting Existing Properties. We turn around properties and seek to add value through renovating and re-tenanting our properties to create Whitestone-branded Community Centered Properties. We seek to accomplish this by (1) stabilizing occupancy, with per property occupancy goals of 90% or higher; (2) adding leasable square footage to existing structures; (3) developing and building on excess land; (4) upgrading and renovating existing structures; and (5) investing significant effort in recruiting tenants whose goods and services meet the needs of the surrounding neighborhood.

Recycling Capital for Greater Returns. We seek to continually upgrade our portfolio by opportunistically selling properties that do not have the potential to meet our Community Centered Property strategy and redeploying the sale proceeds into properties that better fit our strategy. Some of our properties which were acquired prior to the tenure of our current management team may not fit our Community Centered Property strategy, and we may look for opportunities to dispose of these properties as we continue to execute our strategy.

Prudent Management of Capital Structure. We intend to use the net proceeds of this offering to fund acquisitions and selective redevelopment of existing properties. We currently have 15 properties that are not mortgaged. We may seek to add mortgage indebtedness to existing and newly acquired unencumbered properties to provide additional capital for acquisitions. As a general policy, we intend to maintain a ratio of total indebtedness to undepreciated book value of real estate assets that is less than 60%. As of March 31, 2010, our ratio of total indebtedness to undepreciated book value of real estate assets was 53%.

Investing in People. We believe that our people are the heart of our culture, philosophy and strategy. We continually focus on developing associates who are self-disciplined and motivated and display at all times a high degree of character and competence. We provide them with equity incentives to align their interests with those of our shareholders.

Summary Risk Factors

You should carefully consider the risks discussed in the section entitled "Risk Factors" before deciding to invest in our common shares. Some of these risks include:

Recent market disruptions have continued to adversely affect our occupancy, rental rates and access to capital and may significantly and negatively affect our financial condition and results of operations in the future.

Table of Contents

Index to Financial Statements

Current conditions in the credit markets could adversely affect our ability to refinance existing indebtedness or obtain additional financing on acceptable terms or at all, which could adversely affect our ability to grow, our interest costs and our results of operations.

Current lack of geographic diversification of our portfolio leaves us vulnerable to an economic downturn in Texas, and particularly the Houston metropolitan area, which could adversely impact our operations and ability to pay dividends to our shareholders.

We lease our properties to approximately 800 tenants, with approximately 10% to 20% of our leases expiring annually. Each year we face the risk of non-renewal of a material percentage of our leases and the cost of re-leasing a significant amount of our available space, and our failure to meet leasing targets and control the cost of re-leasing our properties could adversely affect our rental revenue, operating expenses and results of operations.

Many of our tenants are small businesses that depend on cash flows from their businesses to pay their rent and are therefore at a higher risk of bankruptcy or insolvency than larger, national tenants. The bankruptcy or insolvency of a number of smaller tenants may have an adverse impact on our income and our ability to pay dividends.

We may not be successful in identifying suitable properties or other assets that meet our acquisition criteria or in consummating acquisitions or investments on satisfactory terms or at all. Failure to identify or consummate acquisitions or investment opportunities, or to integrate successfully any acquired properties without substantial expense, delay or other operational or financial problems, would slow our growth, which could in turn adversely affect our Class B common share price.

Our acquisition strategy is focused on distressed and foreclosed commercial real estate, and we could face significant competition from other investors, such as publicly-traded REITs, hedge funds, private equity funds and other private real estate investors with greater financial resources and access to capital than us. This could result in competition for accretive acquisition opportunities and delay our business plan, our ability to successfully invest the proceeds of this offering and our ability to maintain our current dividend rate.

Our Community Centered Property strategy is newly adopted and requires intensive management of a large number of small spaces and small tenant relationships. Lack of market acceptance of our Community Centered Property strategy or our inability to successfully manage a large number of tenant relationships could adversely affect our occupancy rates, operating results and dividend rate.

We depend on key personnel, particularly our eight senior managers, the loss of any of whom could threaten our ability to execute our strategy and operate our business successfully.

If we fail to maintain our status as a REIT for federal income tax purposes, our distributions to shareholders will not be deductible by us, and we will pay substantial corporate-level income and excise taxes, reducing our earnings available for distribution.

There can be no assurance that we will be able to pay or maintain cash dividends or that dividends will increase over time. The amount of cash available for dividends will be affected by many factors, such as our ability to buy properties, the yields on securities of other real estate programs that we invest in, and our operating expense levels, as well as many other variables.

Reclassification of Common Shares

Edgar Filing: Whitestone REIT - Form S-11/A

Our Board of Trustees, or our Board, has approved Articles of Amendment to our declaration of trust that change the name of all of our common shares to Class A common shares. In addition, our Board has approved Articles Supplementary to our declaration of trust that creates a new class of shares entitled Class B common shares. The rights of the Class A common shareholders will not change with the change in the title of the class. Each Class B common share will have the following rights:

the right to vote together with Class A common shareholders on all matters submitted to our shareholders;

Table of Contents**Index to Financial Statements**

three votes on all matters voted upon by our shareholders;

the right to receive dividends equal to three times any dividends declared on the Class A common shares; and

liquidation rights equal to three times the liquidation rights of each Class A common share.

In this prospectus, we refer to Class A and Class B common shares collectively as our common shares. We are offering our Class B common shares in this offering, and our Class B common shares have been approved for listing on the NYSE Amex subject to official notice of issuance. We do not intend to list our Class A common shares on a national securities exchange. We do intend to conduct one or more exchange offers in the future, no earlier than , 2010, which is six months from the date of this prospectus, that will allow for the exchange of three Class A common shares into one Class B common share. For more information, see Shares Eligible for Future Sale Exchange Offers. The terms of our Class A and Class B common shares are described more fully under Description of Securities in this prospectus.

The Articles of Amendment and the Articles Supplementary will be filed with the State Department of Assessments and Taxation of Maryland prior to the closing of this offering. Unless otherwise indicated, all information in this prospectus assumes the redesignation of the common shares into Class A common shares and the creation of the Class B common shares.

Our Properties

We currently own 36 commercial properties, including 31 properties in Houston, two properties in Dallas, one property in Windcrest, Texas, a suburb of San Antonio, one property in Carefree, Arizona, which is adjacent to North Scottsdale in the Phoenix metropolitan statistical area, and one property in Buffalo Grove, Illinois, a suburb of Chicago. While we are examining prospective acquisitions, we have not contracted to acquire any property with the proceeds of this offering, nor are we at a stage of negotiations with respect to the acquisition of any property such that the acquisition of any property is probable.

Our tenants consist of national, regional and local businesses. Our properties generally attract a mix of tenants who provide basic staples, convenience items and services tailored to the specific cultures, needs and preferences of the surrounding community. These types of tenants are the core of our strategy of creating Whitestone-brand Community Centered Properties. We also believe daily sales of these basic items are less sensitive to fluctuations in the business cycle than higher priced retail items. We typically market and lease our properties to smaller tenants who rent on average less than 3,000 square feet. Our largest tenant represented less than 3% of total revenues for the three months ended March 31, 2010.

We directly manage the operations and leasing of our properties. Substantially all of our revenues consist of base rents received under leases that generally have terms that range from month-to-month to over 15 years. Approximately 73% of our existing leases as of March 31, 2010 contain step up rental clauses that provide for increases in the base rental payments. We estimate that approximately 14% of our properties have expandable redevelopment potential to add approximately 300,000 revenue producing square feet. The following table summarizes certain information relating to our properties as of March 31, 2010:

	Leasable Square Feet	Average Occupancy as of 3/31/10	Annualized Base Rental Revenue (in thousands) ⁽¹⁾	Average Annualized Base Rental Revenue Per Sq. Ft. ⁽²⁾
Commercial Properties				
Retail	1,180,751	81%	\$ 9,783	\$ 10.23
Office/Flex	1,201,672	84%	8,152	8.08
Office	631,841	78%	7,971	16.17
Total	3,014,264	82%	\$ 25,906	\$ 10.51

Table of Contents

Index to Financial Statements

- (1) Calculated as the tenant's actual March 31, 2010 base rent multiplied by 12. Excludes vacant space as of March 31, 2010. Because annualized base rental revenue is not derived from historical results that were accounted for in accordance with generally accepted accounting principles, historical results differ from the annualized amounts.
- (2) Calculated as annualized base rent divided by net rentable square feet leased at March 31, 2010. Excludes vacant space at March 31, 2010.

Our Ownership Structure

Our properties are owned and substantially all of our business is conducted through Whitestone REIT Operating Partnership, L.P., a Delaware limited partnership organized in 1998, which we refer to as our Operating Partnership, and its wholly-owned subsidiaries. Whitestone REIT is the sole general partner of the Operating Partnership. As of March 31, 2010, we owned approximately a 65% interest in our Operating Partnership, and other limited partners collectively own approximately a 35% limited partnership interest. Each unit of limited partnership interest in our Operating Partnership, which we call an OP unit, are redeemable at the election of the holder for cash or, at our option, one of our Class A common shares. This operating structure is sometimes referred to as an Umbrella Partnership Real Estate Investment Trust, or UPREIT. Our UPREIT structure enables a seller to contribute property to our Operating Partnership on a tax-deferred basis in exchange for OP units while affording us the opportunity to issue equity on an efficient basis without commissions and without a lag period to invest the equity proceeds in productive assets. We believe this structure allows us to pursue acquisition opportunities that might not otherwise be available if the only consideration that could be offered to the seller was cash. See The Operating Partnership Agreement.

The following chart illustrates our operating structure and ownership as of March 31, 2010:

- (1) Whitestone REIT is the 65% owner and the general partner of our Operating Partnership. This percentage will increase to _____% after completion of this offering.
- (2) Management and Board ownership of Class A common shares and OP units currently represents 9.9% of all Class A common shares assuming conversion of all OP units, excluding OP units held by Whitestone REIT.

Table of Contents

Index to Financial Statements

Restriction on Ownership and Transfer

Our Articles of Amendment and Restatement, or our declaration of trust, with certain exceptions, authorize our trustees to take such actions as are necessary and desirable to preserve our qualification as a REIT. Unless exempted by our Board, no person or entity may beneficially own, or be deemed to own by virtue of the applicable constructive ownership provisions of the Internal Revenue Code of 1986, as amended, or the Code, more than 9.8% (by value or by number of shares, whichever is more restrictive) of our outstanding Class A or Class B common shares or more than 9.8% (by value or by number of shares, whichever is more restrictive) of the outstanding shares of any class or series of our preferred shares. See [Description of Securities](#) [Restrictions on Ownership and Transfer](#). These restrictions on transferability and ownership will not apply if our Board determines that it is no longer in our best interests to continue to qualify as a REIT.

With certain limited exceptions, our OP units may not be transferred, in whole or in part, without our written consent as the general partner, which consent we may withhold at our sole discretion. We may not consent to any transfer that would cause our Operating Partnership to be treated as a corporation for federal income tax purposes.

Our Tax Status

We elected to be treated as a REIT for federal income tax purposes commencing with our taxable year ended December 31, 1999. To maintain our REIT status, we must meet a number of organizational and operational requirements, including a requirement that we annually distribute to our shareholders at least 90% of our REIT taxable income, determined without regard to the dividends paid deduction and excluding any net capital gains. As a REIT, we generally are not subject to federal income tax on our REIT taxable income that we distribute currently to our shareholders. If we fail to maintain our status as a REIT in any taxable year, we will be subject to federal income tax (including any applicable alternative minimum tax) on our taxable income at regular corporate rates. Even if we qualify for taxation as a REIT, we may be subject to some federal, state and local taxes on our income or property. See [Material U.S. Federal Income Tax Considerations](#).

Our REIT status depends upon our ability to meet, for each taxable year, various requirements imposed under the Code. Those requirements involve the percentage of income that we earn from specified sources, the percentage of our assets that falls within specified categories, the diversity of our share ownership, and the percentage of our earnings that we distribute. For a discussion of the tax consequences of our failure to qualify as a REIT, see [Material U.S. Federal Income Tax Considerations](#) [Requirements for Qualification as a REIT](#) [Failure to Qualify as a REIT](#).

Our REIT status also depends upon our Operating Partnership continuing to be treated as a partnership for federal income tax purposes and not as a publicly traded partnership taxable as a corporation under the Code. This treatment is dependent upon at least 90% of our Operating Partnership's gross income for each taxable year being specified passive income including real property rents, gains from the sale or other disposition of real property, interest and dividends. If our Operating Partnership fails to qualify for taxation as a partnership, we will fail certain asset and income tests required for REIT status.

Our Distribution Policy

In order to maintain our status as a REIT, we must annually distribute to our shareholders an amount at least equal to: (i) 90% of our REIT taxable income, determined without regard to the dividends paid deduction and excluding any net capital gains; plus (ii) 90% of the excess of our net income from foreclosure property over the tax imposed on such income by the Code; less (iii) any excess non-cash income, as determined under Section 857 of the Code.

Table of Contents**Index to Financial Statements**

We declared the following distributions to our shareholders and holders of OP units with respect to 2007, 2008, 2009 and the five months ended May 31, 2010:

	Distributions Per Share⁽¹⁾/OP Unit
2007	
First Quarter	\$ 0.1500
Second Quarter	0.1500
Third Quarter	0.1500
Fourth Quarter	0.1500
2008	
First Quarter	\$ 0.1500
Second Quarter	0.1500
Third Quarter	0.1125
Fourth Quarter	0.1125
2009	
First Quarter	\$ 0.1125
Second Quarter	0.1125
Third Quarter	0.1125
Fourth Quarter	0.1125
2010	
First Quarter	\$ 0.1125
April	0.0375
May	0.0375

⁽¹⁾ Distributions paid with respect to Class A common shares. Each Class B common share will be entitled to dividends equal to three times the dividends paid with respect to each Class A common share.

The timing and frequency of all distributions will be authorized by our Board and declared by us based upon a number of factors, including:

our funds from operations;

our debt service requirements;

our capital expenditure requirements for our properties;

our taxable income, combined with the annual distribution requirements necessary to maintain REIT qualification;

requirements of Maryland law;

our overall financial condition; and

other factors deemed relevant by our Board.

Effective with the quarterly dividend declared for the third quarter 2008, we lowered our quarterly distribution rate to \$0.1125 per share and OP unit from \$0.1500 per share and OP unit in the prior quarter. Our distribution rate for the year ended December 31, 2009 was approximately 80% of our funds from operations per share. We currently declare our distributions quarterly and pay our distributions in three equal monthly installments. For the first quarter of 2010, we declared a distribution per share and OP unit of \$0.1125 which was paid as follows: \$0.0375 on January 5, 2010, \$0.0375 on February 5, 2010 and \$0.0375 on March 5, 2010. On March 30, 2010, our Board authorized, and we declared, a distribution per share and OP unit of \$0.0375 that was

Table of Contents

Index to Financial Statements

paid on April 6, 2010. On April 30, 2010, our Board authorized, and we declared, a distribution per share and OP unit of \$0.0375 that was paid on May 6, 2010. In connection with this offering and the reclassification of our common shares, monthly dividends were declared for April and May 2010, and we intend to authorize and declare a monthly dividend for the month of June 2010.

Subsequent to this offering, we intend to revert to our previous practice of declaring regular quarterly dividends, with the distributions being paid in three equal monthly payments to our Class A common shareholders, holders of OP units and our Class B common shareholders, at their respective rates. We intend to pay a pro rata distribution, covering the partial quarter commencing on the closing of this offering and ending on June 30, 2010, to the purchasers of Class B common shares in this offering.

We cannot assure you that our distributions will be made or sustained. Our actual results of operations may differ materially from our current expectations. Our actual results of operations will be affected by a number of factors, including the revenue we receive from our properties, our operating expenses, our ability to attract and retain tenants, interest expense, the ability of our tenants to meet their obligations and unanticipated expenditures. There can be no assurance that we will be able to pay or maintain cash distributions or that distributions will increase over time.

Table of Contents

Index to Financial Statements

The Offering

Class B common shares offered by us

Common shares and OP units outstanding after this offering:

Class A common shares (1)

Class B common shares (2)

OP units (3)

Dividend rights Each Class B common share will be entitled to dividends equal to three times the dividends with respect to each Class A common share.

Voting rights Each Class A common share entitles its holder to one vote on all matters submitted to shareholders, while each Class B common share will entitle its holder to three votes on all matters submitted to shareholders. The Class B common shares will vote together with the Class A common shares as a single class.

Use of proceeds We estimate that the net proceeds from this offering will be approximately \$ million, based upon the assumed price of \$ per Class B common share and after deducting the underwriting discount and estimated offering expenses of \$ million payable by us. If the underwriters' over-allotment option is exercised in full, our net proceeds will be approximately \$ million. We will contribute the net proceeds from this offering to our Operating Partnership in exchange for OP units. Our Operating Partnership intends to use the net proceeds from the offering (1) to acquire commercial properties in our target markets, (2) to acquire loans with the intent to acquire the underlying property through foreclosure or deed in lieu of foreclosure within a short period of time, (3) to redevelop and re-tenant existing properties to create Whitestone-branded Community Centered Properties and (4) for general corporate purposes. Pending these uses, we intend to invest the net offering proceeds in interest-bearing, short-term, marketable investment grade securities or money market accounts that are consistent with our intention to qualify as a REIT.

Proposed NYSE Amex symbol for Class B common shares WSR

Edgar Filing: Whitestone REIT - Form S-11/A

- (1) Excludes Class A common shares available for issuance under our 2008 Long-Term Equity Incentive Ownership Plan.
- (2) Excludes up to Class B common shares that may be issued by us upon exercise of the underwriters over-allotment option.
- (3) OP units are redeemable for cash or, at our option, Class A common shares on a one-for-one basis.

Our Principal Office

Our principal office is located at 2600 South Gessner, Suite 500, Houston, Texas 77063. Our telephone number is (713) 827-9595. We maintain an Internet site at www.whitestonereit.com. Our internet website and the information contained therein or connected thereto do not constitute a part of this prospectus.

Table of Contents**Index to Financial Statements****Summary Consolidated Financial and Other Data**

The following table sets forth our summary historical consolidated financial, operating and other data. You should read the following historical information in conjunction with our historical consolidated financial statements and notes thereto included elsewhere in this prospectus.

Our historical consolidated balance sheet data as of December 31, 2009, 2008 and 2007 and consolidated statement of operations data for the years ended December 31, 2009, 2008 and 2007 have been derived from our audited historical combined financial statements.

Our unaudited historical consolidated balance sheet data as of March 31, 2010 and the unaudited historical consolidated statement of operations data for the three months ended March 31, 2010 and 2009 are derived from our unaudited historical consolidated financial statements. In the opinion of our management, the unaudited historical combined balance sheet data as of March 31, 2010 and the historical consolidated statements of operations for the three months ended March 31, 2010 and 2009 include all adjustments, consisting only of normal and recurring adjustments, necessary for a fair presentation of the results for those periods.

Our historical consolidated financial data included below and set forth elsewhere in this prospectus are not necessarily indicative of our future performance.

You should read the following summary financial and other data together with Business and Properties, Management's Discussion and Analysis of Financial Condition and Results of Operations and our historical financial statements and related notes appearing elsewhere in this prospectus.

	Three Months		Year Ended December 31,		
	Ended March 31, 2010	2009	2009	2008	2007
(in thousands, except per share data and gross leasable area)					
Operating Data:					
Revenues	\$ 7,709	\$ 8,044	\$ 32,685	\$ 31,201	\$ 29,374
Property expenses	2,953	3,186	12,991	12,835	12,236
General and administrative ⁽¹⁾	1,200	1,429	6,072	6,708	6,721
Depreciation and amortization	1,734	1,708	6,958	6,859	6,048
Involuntary conversion		241	(1,542)	358	
Interest expense, net	1,400	1,417	5,713	5,675	4,825
Other expense (income), net					30
Income (loss) from continuing operations before loss on disposal of assets and income taxes	422	63	2,493	(1,234)	(486)
Provision for income taxes	(54)	(54)	(222)	(219)	(217)
Loss on disposal of assets	(33)	(41)	(196)	(223)	(9)
Income (loss) from continuing operations	335	(32)	2,075	(1,676)	(712)
Income (loss) from discontinued operations				(188)	589
Gain on sale of properties from discontinued operations				3,619	
Net income (loss)	335	(32)	2,075	1,755	(123)
Less: net income (loss) attributable to noncontrolling interests	118	(11)	733	621	(46)
Net income (loss) attributable to Whitestone REIT	\$ 217	\$ (21)	\$ 1,342	\$ 1,134	\$ (77)

(1)

Edgar Filing: Whitestone REIT - Form S-11/A

General and administrative expenses for the years ended December 31, 2008 and 2007 include approximately \$1.5 million and \$2.2 million, respectively, of legal costs resulting from litigation with our former CEO and our former external advisor.

Table of Contents**Index to Financial Statements**

	Three Months Ended March 31,		Year Ended December 31,		
	2010	2009	2009	2008	2007
(in thousands, except per share data and gross leasable area)					
Earnings per share basic					
Income (loss) from continuing operations attributable to Whitestone REIT excluding amounts attributable to unvested restricted shares	\$ 0.02	\$ (0.00)	\$ 0.14	\$ (0.11)	\$ (0.04)
Income from discontinued operations attributable to Whitestone REIT				0.23	0.03
Net income (loss) attributable to common shareholders excluding amounts attributable to unvested restricted shares	\$ 0.02	\$ (0.00)	\$ 0.14	\$ 0.12	\$ (0.01)
Earnings per share diluted					
Income (loss) from continuing operations attributable to Whitestone REIT excluding amounts attributable to unvested restricted shares	\$ 0.02	\$ (0.00)	\$ 0.13	\$ (0.11)	\$ (0.04)
Income from discontinued operations attributable to Whitestone REIT				0.23	0.03
Net income (loss) attributable to common shareholders excluding amounts attributable to unvested restricted shares	\$ 0.02	\$ (0.00)	\$ 0.13	\$ 0.12	\$ (0.01)

Earnings Per Share as if all Class A Common Shares Exchanged for Class B Common Shares

	Three Months Ended March 31,		Year Ended December 31,		
	2010	2009	2009	2008	2007
(in thousands, except per share data)					
Earnings per share basic					
Income (loss) from continuing operations attributable to Whitestone REIT excluding amounts attributable to unvested restricted shares	\$ 0.06	\$ (0.01)	\$ 0.42	\$ (0.33)	\$ (0.12)
Income from discontinued operations attributable to Whitestone REIT				0.69	0.09
Net income (loss) attributable to common shareholders excluding amounts attributable to unvested restricted shares	\$ 0.06	\$ (0.01)	\$ 0.42	\$ 0.36	\$ (0.03)
Earnings per share diluted					
Income (loss) from continuing operations attributable to Whitestone REIT excluding amounts attributable to unvested restricted shares	\$ 0.06	\$ (0.01)	\$ 0.39	\$ (0.33)	\$ (0.12)
Income from discontinued operations attributable to Whitestone REIT				0.69	0.09
Net income (loss) attributable to common shareholders excluding amounts attributable to unvested restricted shares	\$ 0.06	\$ (0.01)	\$ 0.39	\$ 0.36	\$ (0.03)

- (1) Amounts shown as if all Class A common shares had been exchanged for Class B common shares. We intend to conduct one or more exchange offers in the future, no earlier than _____, 2010, which is six months from the date of this prospectus, that will allow for the exchange of three Class A common shares into one Class B common share. Class B common shares will have (a) three votes on all matters voted upon by shareholders, (b) the right to receive dividends equal to three times any dividends received by Class A common shares, and (c) liquidation rights equal to three times the liquidation rights of each Class A common share.

Table of Contents**Index to Financial Statements**

	Three Months Ended March 31,		Year Ended December 31,		
	2010	2009	2009	2008	2007
(in thousands, except per share data and gross leasable area)					
Balance Sheet Data:					
Real estate (net)	\$ 157,459	\$ 160,346	\$ 158,398	\$ 150,847	\$ 146,460
Real estate (net), discontinued operations					7,932
Other assets	20,128	27,324	23,602	27,098	20,752
Total assets	\$ 177,587	\$ 187,670	\$ 182,000	\$ 177,945	\$ 175,144
Liabilities	\$ 110,312	\$ 118,362	\$ 115,141	\$ 110,773	\$ 94,262
Whitestone REIT shareholders' equity	44,092	44,946	43,590	45,891	52,843
Noncontrolling interest in subsidiary	23,183	24,362	23,269	21,281	28,039
	\$ 177,587	\$ 187,670	\$ 182,000	\$ 177,945	\$ 175,144

Other Data:

Proceeds from issuance of common shares	\$		\$	\$	\$ 261
Additions to real estate	499	6,868	9,230	5,153	10,205
Dividends and distributions per share ⁽²⁾	0.11	0.11	0.45	0.53	0.60
Funds from operations ⁽³⁾	1,965	1,556	8,618	4,236	6,001
Occupancy at period end	82%	82%	82%	84%	86%
Average aggregate gross leasable area	3,014,264	3,039,044	3,039,044	3,008,085	3,093,063
Average annualized rent per square foot	10.23	10.59	10.76	10.37	9.50

⁽²⁾ The dividends per share represent total cash payments divided by weighted average common shares. Each Class B common share will be entitled to dividends equal to three times the dividends paid with respect to each Class A common share.

⁽³⁾ We believe that Funds From Operations, or FFO, is an appropriate supplemental measure of operating performance because it helps our investors compare our operating performance relative to other REITs. The National Association of Real Estate Investment Trusts, or NAREIT, defines FFO as net income (loss) available to common shareholders computed in accordance with U.S. generally accepted accounting principles, or GAAP, excluding gains or losses from sales of operating properties and extraordinary items, plus depreciation and amortization of real estate assets, including our share of unconsolidated partnerships and joint ventures. We calculate FFO in a manner consistent with the NAREIT definition.

	Three Months Ended March 31,		Year Ended December 31,		
	2010	2009	2009	2008	2007
(in thousands, except per share data and gross leasable area)					
Net income (loss) attributable to Whitestone REIT	\$ 217	\$ (21)	\$ 1,342	\$ 1,134	\$ (77)
Depreciation and amortization of real estate assets ⁽¹⁾	1,597	1,547	6,347	5,877	6,108
(Gain) loss on sale or disposal of assets ⁽¹⁾	33	41	196	(3,396)	16
Net income (loss) attributable to noncontrolling interests	118	(11)	733	621	(46)
FFO	\$ 1,965	\$ 1,556	\$ 8,618	\$ 4,236	\$ 6,001

⁽¹⁾ Including amounts for discontinued operations

Table of Contents

Index to Financial Statements

RISK FACTORS

An investment in our common shares involves risks. In addition to other information contained in this prospectus, you should carefully consider the following factors before acquiring our Class B common shares offered by this prospectus. The occurrence of any of the following risks might cause you to lose all or a part of your investment. Some statements in this prospectus, including statements in the following risk factors, constitute forward-looking statements, as described in the section entitled Forward-Looking Statements.

Risks Associated with Real Estate

The recent market disruptions may significantly and adversely affect our financial condition and results of operations.

The United States is currently in a recession that has resulted in increased unemployment, weakening of tenant financial condition, large-scale business failures and tight credit markets. Our results of operations may be sensitive to changes in overall economic conditions that impact tenant leasing practices. A continuation of ongoing adverse economic conditions affecting tenant income, such as employment levels, business conditions, interest rates, tax rates, fuel and energy costs and other matters, could reduce overall tenant leasing or cause tenants to shift their leasing practices. In addition, periods of economic slowdown or recession, rising interest rates or declining demand for real estate, or the public perception that any of these events may occur, could result in a general decline in rents or an increased incidence of defaults under existing leases. At this time, it is difficult to determine the breadth and duration of the economic and financial market problems and the many ways in which they may affect our tenants and our business in general. A general reduction in the level of tenant leasing could adversely affect our ability to maintain our current tenants and gain new tenants, affecting our growth and profitability. Accordingly, continuation or further worsening of these difficult financial and macroeconomic conditions could have a significant adverse effect on our cash flows, profitability and results of operations.

Real estate property investments are illiquid, and therefore we may not be able to dispose of properties when appropriate or on favorable terms.

Our strategy includes opportunistically selling properties that do not have the potential to meet our Community Centered Property strategy. However, real estate property investments generally cannot be disposed of quickly. In addition, the Code imposes restrictions on the ability of a REIT to dispose of properties that are not applicable to other types of real estate companies. Therefore, we may not be able to vary our portfolio in response to economic or other conditions promptly or on favorable terms, which could cause us to incur extended losses, reduce our cash flows and adversely affect distributions to shareholders.

We cannot predict whether we will be able to sell any property for the price or on the terms set by us or whether any price or other terms offered by a prospective purchaser would be acceptable to us. We also cannot predict the length of time needed to find a willing purchaser and to close the sale of a property. To the extent we are unable to sell any properties for our book value, we may be required to take a non-cash impairment charge or loss on the sale, either of which would reduce our net income.

We may be required to expend funds to correct defects or to make improvements before a property can be sold. We cannot assure you that we will have funds available to correct those defects or to make those improvements. We may agree to transfer restrictions that materially restrict us from selling that property for a period of time or impose other restrictions, such as a limitation on the amount of debt that can be placed or repaid on that property. These transfer restrictions would impede our ability to sell a property even if we deem it necessary or appropriate. These facts and any others that would impede our ability to respond to adverse changes in the performance of our properties may have a material adverse effect on our business, financial condition, results of operations, our ability to make distributions to our shareholders and the trading price of our Class B common shares.

Table of Contents

Index to Financial Statements

Our business is dependent upon our tenants successfully operating their businesses and their failure to do so could have a material adverse effect on our ability to successfully and profitably operate our business.

We depend on our tenants to operate the properties we own in a manner which generates revenues sufficient to allow them to meet their obligations to us, including their obligations to pay rent, maintain certain insurance coverage, pay real estate taxes and maintain the properties in a manner so as not to jeopardize their operating licenses or regulatory status. The ability of our tenants to fulfill their obligations under our leases may depend, in part, upon the overall profitability of their operations. Cash flow generated by certain tenant businesses may not be sufficient for a tenant to meet its obligations to us. Our financial position could be weakened and our ability to fulfill our obligations under our indebtedness could be limited if a number of our tenants were unable to meet their obligations to us or failed to renew or extend their relationship with us as their lease terms expire, or if we were unable to lease or re-lease our properties on economically favorable terms. These adverse developments could arise due to a number of factors, including those described in the risk factors discussed in this prospectus.

Turmoil in capital markets could adversely impact acquisition activities and pricing of real estate assets.

Volatility in capital markets could adversely affect acquisition activities by impacting certain factors, including the tightening of underwriting standards by lenders and credit rating agencies and the significant inventory of unsold collateralized mortgage backed securities in the market. These factors directly affect a lender's ability to provide debt financing as well as increase the cost of available debt financing. As a result, we may not be able to obtain favorable debt financing in the future or at all. This may impair our ability to acquire properties or result in future acquisitions generating lower overall economic returns, which may adversely affect our results of operations and distributions to shareholders. Furthermore, any turmoil in the capital markets could adversely impact the overall amount of capital available to invest in real estate, which may result in price or value decreases of real estate assets.

The value of investments in our common shares will be directly affected by general economic and regulatory factors we cannot control or predict.

Investments in real estate typically involve a high level of risk as the result of factors we cannot control or predict. One of the risks of investing in real estate is the possibility that our properties will not generate income sufficient to meet operating expenses or will generate income and capital appreciation, if any, at rates lower than those anticipated or available through investments in comparable real estate or other investments. The following factors may affect income from properties and yields from investments in properties and are generally outside of our control:

conditions in financial markets;

over-building in our markets;

a reduction in rental income as a result of the inability to maintain occupancy levels;

adverse changes in applicable tax, real estate, environmental or zoning laws;

changes in general economic conditions;

a taking of any of our properties by eminent domain;

adverse local conditions (such as changes in real estate zoning laws that may reduce the desirability of real estate in the area);

Edgar Filing: Whitestone REIT - Form S-11/A

acts of God, such as hurricanes, earthquakes or floods and uninsured losses;

changes in supply of or demand for similar or competing properties in an area;

changes in interest rates and availability of debt capital, which may render the sale of a property difficult or unattractive; and

periods of high interest rates, inflation or tight money supply.

Table of Contents

Index to Financial Statements

Some or all of these factors may affect our properties, which could adversely affect our operations and ability to pay dividends to shareholders.

All of our properties are subject to property taxes that may increase in the future, which could adversely affect our cash flow.

Our properties are subject to property taxes that may increase as property tax rates change and as the properties are assessed or reassessed by taxing authorities. We anticipate that most of our leases will generally provide that the property taxes, or increases therein, are charged to the lessees as an expense related to the properties that they occupy. As the owner of the properties, however, we are ultimately responsible for payment of the taxes to the government. If property taxes increase, our tenants may be unable to make the required tax payments, ultimately requiring us to pay the taxes. In addition, we will generally be responsible for property taxes related to any vacant space in our properties.

Compliance or failure to comply with laws requiring access to our properties by disabled persons could result in substantial cost.

The Americans with Disabilities Act, or ADA, and other federal, state and local laws generally require public accommodations be made accessible to disabled persons. Noncompliance could result in the imposition of fines by the government or the award of damages to private litigants. These laws may require us to modify our existing properties. These laws may also restrict renovations by requiring improved access to such buildings by disabled persons or may require us to add other structural features which increase our construction costs. Legislation or regulations adopted in the future may impose further burdens or restrictions on us with respect to improved access by disabled persons. We may incur unanticipated expenses that may be material to our financial condition or results of operations to comply with ADA and other federal, state and local laws, or in connection with lawsuits brought by private litigants.

We face intense competition, which may decrease, or prevent increases of, the occupancy and rental rates of our properties.

We compete with a number of developers, owners and operators of commercial real estate, many of which own properties similar to ours in the same markets in which our properties are located. If our competitors offer space at rental rates below current market rates, or below the rental rates we currently charge our tenants, we may lose existing or potential tenants and we may be pressured to reduce our rental rates below those we currently charge or to offer more substantial rent abatements, tenant improvements, early termination rights or below-market renewal options in order to retain tenants when our tenants' leases expire. This competitive environment could have a material adverse effect on our ability to lease our properties or any newly developed or acquired property, as well as on the rents charged.

Risks Associated with Our Operations

Because of the current lack of geographic diversification of our portfolio, an economic downturn in the Houston metropolitan area could adversely impact our operations and ability to pay dividends to our shareholders.

The majority of our assets and revenues are currently derived from properties located in the Houston metropolitan area. As of March 31, 2010, we had 79% of our gross leasable square feet in Houston. Our results of operations are directly contingent on our ability to attract financially sound commercial tenants. A significant economic downturn may adversely impact our ability to locate and retain financially sound tenants and could have an adverse impact on our tenants' revenues, costs and results of operations and may adversely affect their ability to meet their obligations to us. Likewise, we may be required to lower our rental rates to attract desirable tenants in such an environment. Consequently, because of the lack of geographic diversity among our current assets, if the Houston metropolitan area experiences an economic downturn, our operations and ability to pay dividends to our shareholders could be adversely impacted.

Table of Contents

Index to Financial Statements

We lease our properties to approximately 800 tenants, with 10% to 20% of our leases expiring annually. Each year we face the risk of non-renewal of a material percentage of our leases and the cost of re-leasing a significant amount of our available space, and our failure to meet leasing targets and control the cost of re-leasing our properties could adversely affect our rental revenue, operating expenses and results of operations.

While the nature of our business model warrants shorter term leases to smaller, non-national tenants, as of March 31, 2010, approximately 44% of the aggregate gross leasable area of our properties is subject to leases that expire prior to December 31, 2012, which includes our largest tenant, which accounted for less than 3% of our total revenues for the three months ended March 31, 2010. We are subject to the risk that:

tenants may choose not to, or may not have the financial resources to, renew these leases;

we may experience significant costs associated with re-leasing a significant amount of our available space;

we may not be able to easily re-lease the space subject to these leases, which may cause us to fail to meet our leasing targets or control the costs of re-leasing; and

the terms of any renewal or re-lease may be less favorable than the terms of the current leases.

If any of these risks materialize, our rental revenue, operating expenses and results of operations could be adversely affected.

Many of our tenants are small businesses, which may have a higher risk of bankruptcy or insolvency.

Many of our tenants are small, local businesses with little capital that depend on cash flows from their businesses to pay their rent and are therefore at a higher risk of bankruptcy or insolvency than larger, national tenants. The bankruptcy or insolvency of a number of smaller tenants may have an adverse impact on our income and our ability to pay dividends.

We receive substantially all of our income as rent payments under leases of our properties. We have no control over the success or failure of our tenants' businesses and, at any time, any of our tenants may experience a downturn in its business that may weaken its financial condition. As a result, our tenants may fail to make rent payments when due or declare bankruptcy. For example, on November 10, 2008, one of our tenants, Circuit City, which leased space at one of our properties and represented approximately 1.3% of our total rent for the year ended December 31, 2008, filed for reorganization under Chapter 11 of the Bankruptcy Code. The tenant elected to reject our lease.

If tenants are unable to comply with the terms of the leases, we may be forced to modify the leases in ways that are unfavorable to us. Alternatively, the failure of a tenant to perform under a lease could require us to declare a default, repossess the space and find a suitable replacement tenant. There is no assurance that we would be able to lease the space on substantially equivalent or better terms than the prior lease, or at all, or successfully reposition the space for other uses.

If any lease expires or is terminated, we could be responsible for all of the operating expenses for that portion of the property until it is re-leased. If we experience a significant number of un-leased spaces, our operating expenses could increase significantly. Any significant increase in our operating expenses may have a material adverse effect on our business, financial condition and results of operations, our ability to make distributions to our shareholders and the trading price of our Class B common shares.

Any bankruptcy filing by or relating to one of our tenants could bar all efforts by us to collect pre-bankruptcy debts from that tenant or seize its property. A tenant bankruptcy could also delay our efforts to collect past due balances under the leases and could ultimately preclude collection of all or a portion of these sums. It is possible that we may recover substantially less than the full value of any unsecured claims we hold, if any, which may have a material adverse effect on our business, financial condition and results of operations, our ability to

Table of Contents

Index to Financial Statements

make distributions to our shareholders and the trading price of our Class B common shares. Furthermore, dealing with a tenant's bankruptcy or other default may divert management's attention and cause us to incur substantial legal and other costs.

If one or more of our tenants files for bankruptcy relief, the Bankruptcy Code provides that a debtor has the option to assume or reject the unexpired lease within a certain period of time. The Bankruptcy Code generally requires that a debtor must assume or reject a contract in its entirety. Thus, a debtor cannot choose to keep the beneficial provisions of a contract while rejecting the burdensome ones; the contract must be assumed or rejected as a whole. However, where under applicable law a contract (even though it is contained in a single document) is determined to be divisible or severable into different agreements, or similarly, where a collection of documents is determined to constitute separate agreements instead of a single, integrated contract, then in those circumstances a debtor/trustee may be allowed to assume some of the divisible or separate agreements while rejecting the others.

Uninsured losses relating to real property or excessively expensive premiums for insurance coverage may adversely affect our returns.

We attempt to adequately insure all of our properties to cover casualty losses. However, there are types of losses, generally catastrophic in nature, such as losses due to wars, acts of terrorism, earthquakes, floods, hurricanes, pollution or environmental matters, which are uninsurable or not economically insurable, or may be insured subject to limitations, such as large deductibles or co-payments. Our current geographic concentration in the Houston metropolitan area potentially increases the risk of damage to our portfolio due to hurricanes. Insurance risks associated with potential terrorism acts could sharply increase the premiums we pay for coverage against property and casualty claims. In some instances, we may be required to provide other financial support, either through financial assurances or self-insurance, to cover potential losses. We cannot assure you that we will have adequate coverage for these losses. Also, to the extent we must pay unexpectedly large insurance premiums, we could suffer reduced earnings that would result in less cash to be distributed to shareholders as dividends.

Discovery of previously undetected environmentally hazardous conditions may adversely affect our operating results.

Under various federal, state and local environmental laws, ordinances and regulations, a current or previous owner or operator of real property may be liable for the cost of removal or remediation of hazardous or toxic substances on, under or in its property. The costs of removal or remediation could be substantial. These laws often impose liability whether or not the owner or operator knew of, or was responsible for, the presence of any hazardous or toxic substances. Environmental laws also may impose restrictions on the manner in which property may be used or businesses may be operated, and these restrictions may require substantial expenditures. Environmental laws provide for sanctions in the event of noncompliance and may be enforced by governmental agencies or, in certain circumstances, by private parties. Certain environmental laws and common law principles could be used to impose liability for release of and exposure to hazardous substances, including asbestos containing materials into the air. In addition, third parties may seek recovery from owners or operators of real properties for personal injury or property damage associated with exposure to released hazardous substances. The cost of defending against claims of liability, of compliance with environmental regulatory requirements, of remediating any contaminated property, or of paying personal injury claims could materially adversely affect our business, assets or results of operations and, consequently, amounts available for payments of dividends to our shareholders.

We may not be successful in identifying and consummating suitable acquisitions or investment opportunities, which may impede our growth and negatively affect our results of operations.

Our ability to expand through acquisitions is integral to our business strategy and requires us to identify suitable acquisition or investment opportunities that meet our criteria and are compatible with our growth strategy. We may not be successful in identifying suitable properties or other assets that meet our acquisition

Table of Contents

Index to Financial Statements

criteria or in consummating acquisitions or investments on satisfactory terms or at all. Failure to identify or consummate acquisitions or investment opportunities, or to integrate successfully any acquired properties without substantial expense, delay or other operational or financial problems, would slow our growth, which could in turn adversely affect our Class B common share price.

Our ability to acquire properties on favorable terms may be constrained by the following significant risks:

competition from other real estate investors with significant capital, including other publicly-traded REITs and institutional investment funds;

competition from other potential acquirers which may significantly increase the purchase price for a property we acquire, which could reduce our growth prospects;

unsatisfactory results of our due diligence investigations or failure to meet other customary closing conditions; and

failure to finance an acquisition on favorable terms or at all.

If any of these risks are realized, our business, financial condition and results of operations, our ability to make distributions to our shareholders and the trading price of our Class B common shares may be materially and adversely affected.

We may face significant competition in our efforts to acquire financially distressed properties and debt.

Our acquisition strategy is focused on distressed commercial real estate, and we could face significant competition from other investors, such as publicly-traded REITs, hedge funds, private equity funds and other private real estate investors with greater financial resources and access to capital than us. Therefore, we may not be able to compete successfully for investments. In addition, the number of entities and the amount of purchasers competing for suitable investments may increase, all of which could result in competition for accretive acquisition opportunities and adversely affect our business plan, our ability to successfully invest the proceeds of this offering and our ability to maintain our current dividend rate.

Our success depends in part on our ability to execute our Community Centered Property strategy.

Our Community Centered Property strategy is newly adopted and requires intensive management of a large number of small spaces and small tenant relationships. Our success will depend in part upon our management's ability to identify potential Community Centered Properties and find and maintain the appropriate tenants to create such a property. Lack of market acceptance of our Community Centered Property strategy or our inability to successfully attract and manage a large number of tenant relationships could adversely affect our occupancy rates, operating results and dividend rate.

Loss of our key personnel, particularly our eight senior managers, could threaten our ability to execute our strategy and operate our business successfully.

We are dependent on the experience and knowledge of our key executive personnel, particularly our eight senior managers who have been instrumental in setting our strategic direction, operating our business, identifying, recruiting and training key personnel and arranging necessary financing. Losing the services of any of these individuals could adversely affect our business until qualified replacements could be found. We also believe that they could not quickly be replaced with managers of equal experience and capabilities and their successors may not be as effective.

Our systems may not be adequate to support our growth, and our failure to successfully oversee our portfolio of properties could adversely affect our results of operations.

Edgar Filing: Whitestone REIT - Form S-11/A

We cannot assure you that we will be able to adapt our portfolio management, administrative, accounting and operational systems, or hire and retain sufficient operational staff, to support any growth we may experience.

Table of Contents

Index to Financial Statements

Our failure to successfully oversee our current portfolio of properties or any future acquisitions or developments could have a material adverse effect on our results of operations and financial condition and our ability to make distributions.

There can be no assurance that we will be able to pay or maintain cash dividends or that dividends will increase over time.

There are many factors that can affect the availability and timing of cash dividends to shareholders. Dividends will be based principally on cash available from our properties, real estate securities, mortgage loans and other investments. The amount of cash available for dividends will be affected by many factors, such as our ability to buy properties, the yields on securities of other real estate programs that we invest in, and our operating expense levels, as well as many other variables. We can give no assurance that we will be able to pay or maintain dividends or that dividends will increase over time. In addition, we can give no assurance that rents from the properties will increase, that the securities we buy will increase in value or provide constant or increased dividends over time, or that future acquisitions of real properties, mortgage loans or our investments in securities will increase our cash available for dividends to shareholders. Our actual results may differ significantly from the assumptions used by our Board in establishing the dividend rate to shareholders.

If we experience decreased cash flows, we may need to use other sources of cash to fund dividends or we may be unable to pay dividends.

Actual cash available for dividends may vary substantially from estimates. If our cash dividends exceed the amount of cash available for dividends, we may need to fund the shortage out of working capital or by obtaining other debt, which would reduce the amount of proceeds available for real estate investments.

Our assets may be subject to impairment charges.

We periodically evaluate our real estate investments and other assets for impairment indicators. The judgment regarding the existence of impairment indicators is based on factors such as market conditions, tenant performance and legal structure. If we determine that a significant impairment has occurred, we would be required to make an adjustment to the net carrying value of the asset, which could have a material adverse effect on our results of operations and funds from operations in the period in which the write-off occurs.

Recent healthcare reform legislation may affect our revenue and financial condition.

On March 23, 2010, the President signed into law the Patient Protection and Affordable Care Act of 2010 and on March 30, 2010, the President signed into law the Health Care and Education Reconciliation Act, which in part modified the Patient Protection and Affordable Care Act. Together, the two Acts serve as the primary vehicle for comprehensive health care reform in the United States. The Acts are intended to reduce the number of individuals in the United States without health insurance and effect significant other changes to the ways in which health care is organized, delivered and reimbursed. The complexities and ramifications of the new legislation are significant, and will be implemented in a phased approach beginning in 2010 and concluding in 2018. At this time, the effects of health care reform and its impact on our business, our revenues and financial condition and those of our tenants are not yet known. Accordingly, the reform could adversely affect the cost of providing healthcare coverage generally and the financial success of our tenants and consequently us.

Table of Contents

Index to Financial Statements

Risks Associated with Our Indebtedness and Financing

Current market conditions could adversely affect our ability to refinance existing indebtedness or obtain additional financing for growth on acceptable terms or at all, which could adversely affect our ability to grow, our interest cost and our results of operations.

The United States credit markets have recently experienced significant dislocations and liquidity disruptions, including the bankruptcy, insolvency or restructuring of certain financial institutions. These circumstances have materially impacted liquidity in the debt markets, making financing terms for borrowers less attractive, and in certain cases have resulted in the unavailability of various types of debt financing. Reductions in our available borrowing capacity, or inability to establish a credit facility when required or when business conditions warrant, could have a material adverse effect on our business, financial condition and results of operations. In addition, we mortgage most of our properties to secure payment of indebtedness. If we are not successful in refinancing our mortgage debt upon maturity, then the property could be foreclosed upon or transferred to the mortgagee, or we might be forced to dispose of some of our properties upon disadvantageous terms, with a consequent loss of income and asset value. A foreclosure or disadvantageous disposal on one or more of our properties could adversely affect our ability to grow, financial condition, interest cost, results of operations, cash flow and ability to pay dividends to our shareholders.

Furthermore, if prevailing interest rates or other factors at the time of refinancing result in higher interest rates upon refinancing, then the interest expense relating to that refinanced indebtedness would increase. Higher interest rates on newly incurred debt may negatively impact us as well. If interest rates increase, our interest costs and overall costs of capital will increase, which could adversely affect our transaction and development activity, financial condition, results of operation, cash flow, our ability to pay principal and interest on our debt and our ability to pay dividends to our shareholders.

If we invest in mortgage loans, such investments may be affected by unfavorable real estate market conditions, including interest rate fluctuations, which could decrease the value of those loans and the return on your investment.

If we invest in mortgage loans, we will be at risk of defaults by the borrowers on those mortgage loans as well as interest rate risks. To the extent we incur delays in liquidating such defaulted mortgage loans, we may not be able to obtain all amounts due to us under the mortgage loans. Further, we will not know whether the values of the properties securing the mortgage loans will remain at the levels existing on the dates of origination of those mortgage loans or the dates of our investment in the loans. If the values of the underlying properties fall, our risk will increase because of the lower value of the security associated with such loans.

We may incur losses on interest rate hedging arrangements.

Periodically, we have entered into agreements to reduce the risks associated with increases in interest rates, and may continue to do so. Although these agreements may partially protect against rising interest rates, they also may reduce the benefits to us if interest rates decline. If a hedging arrangement is not indexed to the same rate as the indebtedness which is hedged, we may be exposed to losses to the extent which the rate governing the indebtedness and the rate governing the hedging arrangement change independently of each other. Finally, nonperformance by the other party to the hedging arrangement may subject us to increased credit risks.

Our failure to hedge effectively against interest rate changes may adversely affect results of operations.

We currently have mortgages that bear interest at a variable rate and we may incur additional variable rate debt in the future. Accordingly, increases in interest rates on variable rate debt would increase our interest expense, which could reduce net earnings and cash available for payment of our debt obligations and distributions to our shareholders.

Table of Contents

Index to Financial Statements

We may seek to manage our exposure to interest rate volatility by using interest rate hedging arrangements, such as interest cap agreements and interest rate swap agreements. These agreements involve risks, such as the risk that counterparties may fail to honor their obligations under these arrangements, that these arrangements may not be effective in reducing our exposure to interest rate changes and that a court could rule that such an agreement is not legally enforceable. In the past, we have used derivative financial instruments to hedge interest rate risks related to our variable rate borrowings. We will not use derivatives for speculative or trading purposes and intend only to enter into contracts with major financial institutions based on their credit rating and other factors, but we may choose to change this practice in the future. We may enter into interest rate swap agreements for our variable rate debt, which totals \$25.9 million as of March 31, 2010. Hedging may reduce the overall returns on our investments. Failure to hedge effectively against interest rate changes may materially adversely affect our results of operations.

We currently have and may incur additional mortgage indebtedness and other borrowings, which may increase our business risks and our ability to make distributions to our shareholders.

If it is determined to be in our best interests, we may, in some instances, acquire real properties by using either existing financing or borrowing new funds. In addition, we may incur or increase our current mortgage debt to obtain funds to acquire additional properties. We may also borrow funds if necessary to satisfy the REIT distribution requirement described above, or otherwise as may be necessary or advisable to assure that we maintain our qualification as a REIT for federal income tax purposes.

We may incur mortgage debt on a particular property if we believe the property's projected cash flow is sufficient to service the mortgage debt. As of March 31, 2010, we had approximately \$101.6 million of mortgage debt secured by 21 of our properties. If there is a shortfall in cash flow, however, the amount available for dividends to shareholders may be affected. In addition, incurring mortgage debt increases the risk of loss because defaults on such indebtedness may result in loss of property in foreclosure actions initiated by lenders. For tax purposes, a foreclosure of any of our properties would be treated as a sale of the property for a purchase price equal to the outstanding balance of the debt secured by the mortgage. If the outstanding balance of the debt secured by the mortgage exceeds our tax basis in the property, we would recognize taxable income on foreclosure, but would not receive any cash proceeds. We may give lenders full or partial guarantees for mortgage debt incurred by the entities that own our properties. When we give a guaranty on behalf of an entity that owns one of our properties, we will be responsible to the lender for satisfaction of the debt if it is not paid by that entity. If any mortgages contain cross-collateralization or cross-default provisions, there is a risk that more than one property may be affected by a default. If any of our properties are foreclosed upon due to a default, our ability to pay cash dividends to our shareholders will be adversely affected. For more discussion, see Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources.

If we set aside insufficient working capital or are unable to secure funds for future tenant improvements, we may be required to defer necessary property improvements, which could adversely impact our ability to pay cash distributions to our shareholders.

When tenants do not renew their leases or otherwise vacate their space, it is possible that, in order to attract replacement tenants, we may be required to expend substantial funds for tenant improvements and tenant refurbishments to the vacated space. If we have insufficient working capital reserves, we will have to obtain financing from other sources. Because most of our leases will provide for tenant reimbursement of operating expenses, we do not anticipate that we will establish a permanent reserve for maintenance and repairs for our properties. However, to the extent that we have insufficient funds for such purposes, we may establish reserves for maintenance and repairs of our properties from gross proceeds of this offering, out of cash flow generated by operating properties or out of non-liquidating net sale proceeds. If these reserves or any reserves otherwise established are insufficient to meet our cash needs, we may have to obtain financing from either affiliated or unaffiliated sources to fund our cash requirements. We cannot assure you that sufficient financing will be

Table of Contents

Index to Financial Statements

available or, if available, will be available on economically feasible terms or on terms acceptable to us. Additional borrowing for working capital purposes will increase our interest expense, and therefore our financial condition and our ability to pay cash distributions to our shareholders may be adversely affected. In addition, we may be required to defer necessary improvements to our properties that may cause our properties to suffer from a greater risk of obsolescence or a decline in value, or a greater risk of decreased cash flow as a result of fewer potential tenants being attracted to our properties. If this happens, we may not be able to maintain projected rental rates for affected properties, and our results of operations may be negatively impacted.

We may structure acquisitions of property in exchange for limited partnership units in our Operating Partnership on terms that could limit our liquidity or our flexibility.

We may acquire properties by issuing limited partnership units in our Operating Partnership in exchange for a property owner contributing property to the Operating Partnership. If we enter into such transactions, in order to induce the contributors of such properties to accept units in our Operating Partnership, rather than cash, in exchange for their properties, it may be necessary for us to provide them with additional incentives. For instance, our Operating Partnership's limited partnership agreement provides that any holder of units may redeem limited partnership units for cash, or, at our option, Class A common shares on a one-for-one exchange basis. We may, however, enter into additional contractual arrangements with contributors of property under which we would agree to redeem a contributor's units for our Class A common shares or cash, at the option of the contributor, at set times. If the contributor required us to redeem units for cash pursuant to such a provision, it would limit our liquidity and thus our ability to use cash to make other investments, satisfy other obligations or pay distributions to you. Moreover, if we were required to redeem units for cash at a time when we did not have sufficient cash to fund the redemption, we might be required to sell one or more properties to raise funds to satisfy this obligation. Furthermore, we might agree that if distributions the contributor received as a limited partner in our Operating Partnership did not provide the contributor with a defined return, then upon redemption of the contributor's units we would pay the contributor an additional amount necessary to achieve that return. Such a provision could further negatively impact our liquidity and flexibility. Finally, in order to allow a contributor of a property to defer taxable gain on the contribution of property to our Operating Partnership, we might agree not to sell a contributed property for a defined period of time or until the contributor redeemed the contributor's units for cash or our Class A common shares. Such an agreement would prevent us from selling those properties, even if market conditions made such a sale favorable to us.

We may issue preferred shares with a preference in distributions over our common shares, and our ability to issue preferred shares and additional common shares may deter or prevent a sale of our common shares in which you could profit.

Our declaration of trust authorizes our Board to issue up to 50,000,000 Class A common shares, 350,000,000 Class B common shares and 50,000,000 preferred shares. Our Board may amend our declaration of trust from time to time to increase or decrease the aggregate number of shares or the number of shares of any class or series that we have authority to issue. In addition, our Board may classify or reclassify any unissued common shares or preferred shares and may set the preferences, rights and other terms of the classified or reclassified shares. The terms of preferred shares could include a preference in distributions over our common shares. If we authorize and issue preferred shares with a distribution preference over our common shares, payment of any distribution preferences of outstanding preferred shares would reduce the amount of funds available for the payment of distributions on our common shares. Further, holders of preferred shares are normally entitled to receive a preference payment in the event we liquidate, dissolve or wind up before any payment is made to our common shareholders, likely reducing the amount our common shareholders would otherwise receive upon such an occurrence. In addition, under certain circumstances, the issuance of preferred shares or a separate class or series of common shares may render more difficult or tend to discourage:

a merger, tender offer or proxy contest;

assumption of control by a holder of a large block of our shares; or

Table of Contents

Index to Financial Statements

removal of incumbent management.

Risks Associated with Income Tax Laws

If we fail to qualify as a REIT, our operations and dividends to shareholders would be adversely impacted.

We intend to continue to be organized and to operate so as to qualify as a REIT under the Code. A REIT generally is not taxed at the corporate level on income it currently distributes to its shareholders. Qualification as a REIT involves the application of highly technical and complex rules for which there are only limited judicial or administrative interpretations. The determination of various factual matters and circumstances not entirely within our control may affect our ability to continue to qualify as a REIT. In addition, new legislation, new regulations, administrative interpretations or court decisions could significantly change the tax laws, possibly with retroactive effect, with respect to qualification as a REIT or the federal income tax consequences of such qualification.

If we were to fail to qualify as a REIT in any taxable year:

we would not be allowed to deduct our distributions to shareholders when computing our taxable income;

we would be subject to federal income tax (including any applicable alternative minimum tax) on our taxable income at regular corporate rates;

we would be disqualified from being taxed as a REIT for the four taxable years following the year during which qualification was lost, unless entitled to relief under certain statutory provisions;

our cash available for dividends to shareholders would be reduced; and

we may be required to borrow additional funds or sell some of our assets in order to pay corporate tax obligations that we may incur as a result of our disqualification.

If the Internal Revenue Service, or IRS, were to determine that (i) we failed the 5% asset test for the first quarter of our 2009 taxable year and (ii) our failure of that test was not attributable to reasonable cause, but rather, willful neglect, we would fail to qualify as a REIT for our 2009 taxable year, which would adversely affect our operations and our shareholders.

We recently discovered that we may have inadvertently violated the 5% asset test for the quarter ended March 31, 2009 as a result of utilizing a certain cash management arrangement with a commercial bank. If this investment in a commercial paper investment account is not treated as cash, and is instead treated as a security for purposes of the quarterly 5% asset test applicable to REITs, then we have failed that test for the first quarter of our 2009 taxable year. We believe, however, that if we in fact failed the test, our failure would be considered due to reasonable cause and not willful neglect and, therefore, we would not be disqualified as a REIT for our 2009 taxable year. We are, however, subject to a tax equal to the greater of \$50,000 or 35% of the net income from the commercial paper investment account during the period in which we failed to satisfy the 5% asset test. The amount of such tax is \$50,000 and we paid such tax on April 27, 2010.

If the IRS were to assert that we failed the 5% asset test for the first quarter of our 2009 taxable year and that such failure was not due to reasonable cause, and the courts were to sustain that position, our status as a REIT would terminate as of December 31, 2008. We would not be eligible to again elect REIT status until our 2014 taxable year. Consequently, we would be subject to federal income tax on our taxable income at regular corporate rates and our cash available for distributions to shareholders would be reduced. See Material U.S. Federal Income Tax Considerations Failure to Qualify as a REIT, which describes the consequences of our failure to qualify as a REIT.

Table of Contents

Index to Financial Statements

We may need to incur additional borrowings to meet the REIT minimum distribution requirement and to avoid excise tax.

In order to maintain our qualification as a REIT, we are required to distribute to our shareholders at least 90% of our annual real estate investment trust taxable income (excluding any net capital gain and before application of the dividends paid deduction). In addition, we are subject to a 4% nondeductible excise tax on the amount, if any, by which certain distributions paid by us with respect to any calendar year are less than the sum of (i) 85% of our ordinary income for that year, (ii) 95% of our net capital gain for that year and (iii) 100% of our undistributed taxable income from prior years. Although we intend to pay dividends to our shareholders in a manner that allows us to meet the 90% distribution requirement and avoid this 4% excise tax, we cannot assure you that we will always be able to do so.

Our income consists almost solely of our share of our Operating Partnership's income, and the cash available for distribution by us to our shareholders consists of our share of cash distributions made by our Operating Partnership. Because we are the sole general partner of our Operating Partnership, our Board determines the amount of any distributions made by it. Our Board may consider a number of factors in authorizing distributions, including:

the amount of the cash available for distribution;

our Operating Partnership's financial condition;

our Operating Partnership's capital expenditure requirements; and

our annual distribution requirements necessary to maintain our qualification as a REIT.

Differences in timing between the actual receipt of income and actual payment of deductible expenses and the inclusion of income and deduction of expenses when determining our taxable income, as well as the effect of nondeductible capital expenditures and the creation of reserves or required debt amortization payments could require us to borrow funds on a short-term or long-term basis or make taxable distributions to our shareholders of our shares or debt securities to meet the REIT distribution requirement and to avoid the 4% excise tax described above. In these circumstances, we may need to borrow funds to avoid adverse tax consequences even if our management believes that the then prevailing market conditions generally are not favorable for borrowings or that borrowings would not be advisable in the absence of the tax consideration.

If our Operating Partnership were classified as a publicly traded partnership taxable as a corporation for federal income tax purposes under the Code, we would cease to qualify as a REIT and would suffer other adverse tax consequences.

We structured our Operating Partnership so that it would be classified as a partnership for federal income tax purposes. In this regard, the Code generally classifies publicly traded partnerships (as defined in Section 7704 of the Code) as associations taxable as corporations (rather than as partnerships), unless substantially all of their taxable income consists of specified types of passive income. In order to minimize the risk that the Code would classify our Operating Partnership as a publicly traded partnership for tax purposes, we placed certain restrictions on the transfer and/or redemption of partnership units in our Operating Partnership. If the IRS were to assert successfully that our Operating Partnership is a publicly traded partnership, and substantially all of its gross income did not consist of the specified types of passive income, the Code would treat our Operating Partnership as an association taxable as a corporation.

These topics are discussed in greater detail in the Material U.S. Federal Income Tax Considerations Tax Aspects of Our Investments in Our Operating Partnership section of this prospectus. In such event, the character of our assets and items of gross income would change and would prevent us from continuing to qualify as a REIT. In addition, the imposition of a corporate tax on our Operating Partnership would reduce our amount of cash available for payment of distributions by us to our shareholders.

Table of Contents

Index to Financial Statements

Complying with REIT requirements may cause us to forego otherwise attractive opportunities or liquidate otherwise attractive investments.

To qualify as a REIT for federal income tax purposes, we must continually satisfy tests concerning, among other things, the sources of our income, the nature and diversification of our assets, the amounts we distribute to our shareholders and the ownership of our shares. In order to meet these tests, we may be required to forego investments we might otherwise make. Thus, compliance with the REIT requirements may hinder our performance.

In particular, we must ensure that at the end of each calendar quarter, at least 75% of the value of our assets consists of cash, cash items, government securities and qualified real estate assets. The remainder of our investment in securities (other than government securities and qualified real estate assets) generally cannot include more than 10% of the outstanding voting securities of any one issuer or more than 10% of the total value of the outstanding securities of any one issuer. In addition, in general, no more than 5% of the value of our assets (other than government securities and qualified real estate assets) can consist of the securities of any one issuer, and no more than 25% of the value of our total assets can be represented by the securities of one or more taxable REIT subsidiaries. If we fail to comply with these requirements at the end of any calendar quarter, we must correct the failure within 30 days after the end of the calendar quarter or qualify for certain statutory relief provisions to avoid losing our REIT qualification and suffering adverse tax consequences. As a result, we may be required to liquidate otherwise attractive investments. These actions could have the effect of reducing our income and amounts available for distribution to our shareholders.

We may be subject to adverse legislative or regulatory tax changes that could reduce the market price of our Class B common shares.

At any time, the federal income tax laws governing REITs or the administrative interpretations of those laws may be amended. We cannot predict when or if any new federal income tax law, regulation, or administrative interpretation, or any amendment to any existing federal income tax law, regulation or administrative interpretation, will be adopted, promulgated or become effective and any such law, regulation, or interpretation may take effect retroactively. We and our shareholders could be adversely affected by any such change in, or any new, federal income tax law, regulation or administrative interpretation.

Dividends payable by REITs do not qualify for the reduced tax rates available for some dividends.

The maximum tax rate applicable to income from qualified dividends payable to U.S. shareholders that are individuals, trusts and estates has been reduced by legislation to 15% (through the end of 2010). Dividends payable by REITs, however, generally are not eligible for the reduced rates. Although this legislation does not adversely affect the taxation of REITs or dividends payable by REITs, the more favorable rates applicable to regular corporate qualified dividends could cause investors who are individuals, trusts and estates to perceive investments in REITs to be relatively less attractive than investments in the stocks of non-REIT corporations that pay dividends, which could adversely affect the value of the shares of REITs, including our common shares.

Complying with REIT requirements may limit our ability to hedge effectively and may cause us to incur tax liabilities.

The REIT provisions of the Code substantially limit our ability to hedge our liabilities. Any income from a hedging transaction that we enter into to manage risk of interest rate changes, price changes or currency fluctuations with respect to borrowings made or to be made to acquire or carry real estate assets does not constitute gross income for purposes of the 75% or 95% gross income tests. To the extent that we enter into other types of hedging transactions, the income from those transactions is likely to be treated as non-qualifying income for purposes of both of the gross income tests. See Material U.S. Federal Income Tax Considerations Gross Income Tests Hedging Transactions. As a result of these rules, we may need to limit our use of advantageous hedging techniques or implement those hedges through taxable REIT subsidiaries. This could

Table of Contents

Index to Financial Statements

increase the cost of our hedging activities because any taxable REIT subsidiary that we may form would be subject to tax on gains or expose us to greater risks associated with changes in interest rates than we would otherwise want to bear. In addition, losses in taxable REIT subsidiaries will generally not provide any tax benefit, except for being carried forward against future taxable income in the taxable REIT subsidiaries.

Risks Related to This Offering and Ownership of our Class B Common Shares

There is currently no public market for our common shares, and an active trading market for our Class B common shares may not develop following this offering.

Prior to this offering, there has been no public market for our common shares. Our Class B common shares have been approved for listing on the NYSE Amex, subject to official notice of issuance, in connection with this offering. We cannot assure you that an active trading market for our Class B common shares will develop or, if one develops, be sustained. Our Class B common shares may have limited trading volume, and many investors may not be interested in owning our Class B common shares because of the inability to acquire or sell a substantial block of our Class B common shares at one time. Such illiquidity could have an adverse effect on the market price of our Class B common shares. In addition, a shareholder may not be able to borrow funds using our Class B common shares as collateral because lenders may be unwilling to accept the pledge of securities having such a limited market.

A substantial sale of our Class B common shares, or the perception that a substantial sale might occur, could cause the market price of our Class B common shares to decline.

The market price and trading volume of our Class B common shares may be volatile following this offering.

Even if an active trading market develops for our Class B common shares after this offering, the market price of our Class B common shares may fluctuate widely. In addition, the trading volume in our Class B common shares may fluctuate and cause significant price variations to occur. If the market price of our Class B common shares declines significantly, you may be unable to resell your Class B common shares at or above the public offering price. We cannot assure you that the market price of our Class B common shares will not fluctuate or decline significantly, including a decline below the public offering price, in the future.

Some of the factors that could negatively affect our share price or result in fluctuations in the market price or trading volume of our Class B common shares include:

actual or anticipated declines in our quarterly operating results or distributions;

reductions in our funds from operations or earnings estimates;

publications of research reports about us or the real estate industry;

increases in market interest rates that lead purchasers of our common shares to demand a higher yield;

changes in market valuations of similar companies;

adverse market reaction to any increased indebtedness we incur in the future;

additions or departures of key management personnel;

actions by institutional shareholders;

speculation in the press or investment community;

the realization of any of the other risk factors presented in this prospectus; and

general market and economic conditions.

The public offering price does not necessarily bear any relationship to our book value or the fair market value of our assets.

Table of Contents

Index to Financial Statements

An increase in market interest rates may have an adverse effect on the market price of our Class B common shares.

One of the factors that investors may consider in deciding whether to buy or sell our Class B common shares is our distribution rate as a percentage of our share price, relative to market interest rates. If market interest rates increase, prospective investors may desire a higher distribution rate on our Class B common shares or seek securities paying higher distributions or interest. The market price of our Class B common shares likely will be based primarily on the earnings that we derive from rental income with respect to our properties and our distributions to shareholders, and not from the underlying appraised value of the properties themselves. As a result, interest rate fluctuations and capital market conditions can affect the market price of our Class B common shares. For instance, if interest rates rise without an increase in our distribution rate, the market price of our Class B common shares could decrease because potential investors may require a higher yield on our Class B common shares as market rates on interest-bearing securities, such as bonds, rise. In addition, rising interest rates would result in increased interest expense on our variable rate debt, thereby adversely affecting cash flow and our ability to service our indebtedness and make distributions to our shareholders.

Broad market fluctuations could negatively impact the market price of our Class B common shares.

The stock market has experienced extreme price and volume fluctuations that have affected the market price of many companies in industries similar or related to ours and that have been unrelated to these companies' operating performances. These broad market fluctuations could reduce the market price of our Class B common shares. Furthermore, our operating results and prospects may be below the expectations of public market analysts and investors or may be lower than those of companies with comparable market capitalizations. Either of these factors could lead to a material decline in the market price of our Class B common shares.

The number of shares available for future sale could adversely affect the market price of our Class B common shares.

We cannot predict whether future issuances of common shares or the availability of shares for resale in the open market will decrease the market price per share of our Class B common shares. Our Class A common shares will not be listed on a national securities exchange. Other than Class A common shares and OP units held by our officers and trustees, none of our outstanding Class A common shares or OP units are subject to any lock-up agreement. We intend to conduct one or more exchange offers in the future, no earlier than _____, 2010, which is six months from the date of this prospectus, that will allow for the exchange of three Class A common shares into one Class B common share and the exchange of three OP units into one Class B common share. Sales of a substantial number of Class B common shares in the public market, or upon exchange of Class A common shares or OP units, or the perception that such sales might occur could materially adversely affect the market price of our Class B common shares. For a more detailed description, see Shares Eligible for Future Sale.

Our trustees and executive officers have agreed with the underwriters not to offer, sell, contract to sell, pledge or otherwise dispose of any common shares or other securities convertible or exchangeable into our common shares for a period of 180 days after the date of this prospectus. If any or all of these holders cause a large number of their shares to be sold in the public market, the sales could reduce the trading price of our Class B common shares and could impede our ability to raise future capital.

The exercise of the underwriters' over-allotment option, the exchange of Class A common shares or OP units for Class B common shares, the exercise of any options granted to certain trustees, executive officers and other employees under our long-term equity incentive plan, the issuance of our common shares or OP units in connection with property, portfolio or business acquisitions and other issuances of our common shares could have an adverse effect on the market price of our Class B common shares, and the existence of OP units, options and common shares reserved for issuance as restricted common shares or upon exchange of Class A common shares or OP units may materially adversely affect the terms upon which we may be able to obtain additional

Table of Contents

Index to Financial Statements

capital through the sale of equity securities. In addition, future sales of our common shares may be dilutive to existing shareholders.

If you purchase shares in this offering, you will experience immediate dilution.

We expect the public offering price of our Class B common shares to be higher than the book value per Class B common share immediately following this offering. Accordingly, if you purchase Class B common shares in this offering, you will experience immediate dilution of approximately \$ in book value per share. This means that investors who purchase shares will likely pay a price per share that exceeds the book value of our assets after subtracting our liabilities.

Maryland takeover statutes may deter others from seeking to acquire us and prevent you from making a profit in such transactions.

The Maryland General Corporation Law, or the MGCL, contains many provisions, such as the business combination statute and the control share acquisition statute, that are designed to prevent, or have the effect of preventing, someone from acquiring control of us. The business combination statute, subject to limitations, prohibits certain business combinations between us and an interested shareholder (defined generally as any person who beneficially owns 10% or more of the voting power of our outstanding voting shares or an affiliate or associate of our company who, at any time within the two-year period prior to the date in question, was the beneficial owner of 10% or more of the voting power of our then outstanding shares) or an affiliate of an interested shareholder for five years after the most recent date on which the person becomes an interested shareholder and thereafter imposes supermajority voting requirements on these combinations. The control share acquisition statute provides that control shares of our company (defined as shares which, when aggregated with other shares controlled by the shareholder (except solely by virtue of a revocable proxy), entitle the shareholder to exercise one of three increasing ranges of voting power in electing trustees) acquired in a control share acquisition (defined as the direct or indirect acquisition of ownership or control of issued and outstanding control shares) have no voting rights except to the extent approved by our shareholders by the affirmative vote of at least two-thirds of all the votes entitled to be cast on the matter, excluding all interested shares.

We are currently subject to the control share acquisition statute, although our Board may amend our bylaws, without shareholder approval, to exempt any acquisition of our shares from the statute. Our Board has adopted a resolution exempting any business combination with any person from the business combination statute. The business combination statute (if our Board revokes the foregoing exemption) and the control share acquisition statute could delay or prevent offers to acquire us and increase the difficulty of consummating any such offers, even if such a transaction would be in our shareholders' best interest.

The MGCL, the Maryland REIT Law and our organizational documents limit your right to bring claims against our officers and trustees.

The MGCL and the Maryland REIT Law provide that a trustee will not have any liability as a trustee so long as he performs his duties in good faith, in a manner he reasonably believes to be in our best interests, and with the care that an ordinarily prudent person in a like position would use under similar circumstances. In addition, our declaration of trust provides that no trustee or officer will be liable to us or to any shareholder for money damages except to the extent that (a) the trustee or officer actually received an improper benefit or profit in money, property or services, for the amount of the benefit or profit in money, property, or services actually received; or (b) a judgment or other final adjudication adverse to the trustee or officer is entered in a proceeding based on a finding in the proceeding that the trustee's or officer's action or failure to act was the result of active and deliberate dishonesty and was material to the cause of action adjudicated in the proceeding. Finally, our declaration of trust authorizes our company to obligate itself, and our bylaws obligate us, to indemnify and advance expenses to our trustees and officers to the maximum extent permitted by Maryland law.

Table of Contents

Index to Financial Statements

Our classified Board may prevent others from effecting a change in the control of our Board.

We believe that classification of our Board will help to assure the continuity and stability of our business strategies and policies as determined by the Board. However, the classified board provision could have the effect of making the replacement of incumbent trustees more time-consuming and difficult. At least two annual meetings of shareholders, instead of one, will generally be required to effect a change in a majority of our Board. Thus, the classified board provision could increase the likelihood that incumbent trustees will retain their positions. The staggered terms of trustees may delay, defer or prevent a transaction or a change in control that might involve a premium price for our common shares or otherwise be in the best interest of the shareholders.

Future offerings of debt, which would be senior to our common shares upon liquidation, and/or preferred equity securities that may be senior to our common shares for purposes of dividends or other distributions or upon liquidation, may adversely affect the market price of our Class B common shares.

In the future, we may attempt to increase our capital resources by making additional offerings of debt or preferred equity securities, including medium-term notes, trust preferred securities, senior or subordinated notes and preferred shares. Upon liquidation, holders of our debt securities and preferred shares and lenders with respect to other borrowings will receive distributions of our available assets prior to the holders of our common shares. Additional equity offerings may dilute the holdings of our existing shareholders or reduce the market price of our common shares, or both. Holders of our common shares are not entitled to preemptive rights or other protections against dilution. Our preferred shares, if issued, could have a preference on liquidating distributions or a preference on dividend payments that could limit our ability to pay a dividend or make another distribution to the holders of our common shares. Because our decision to issue securities in any future offering will depend on market conditions and other factors beyond our control, we cannot predict or estimate the amount, timing or nature of our future offerings. Thus, our Class B common shareholders bear the risk of our future offerings reducing the market price of our Class B common shares and diluting their share holdings in us.

Table of Contents

Index to Financial Statements

FORWARD-LOOKING STATEMENTS

We make statements in this prospectus that are forward-looking statements within the meaning of the federal securities laws. In particular, statements pertaining to our capital resources, portfolio performance and results of operations contain forward-looking statements. Likewise, all of our statements regarding anticipated growth in our funds from operations and anticipated market conditions, demographics and results of operations are forward-looking statements. You can identify forward-looking statements by the use of forward-looking terminology such as believes, expects, may, will, should, could, would, seeks, approximately, intends, plans, pro forma, estimates or any of these words and phrases or similar words or phrases which are predictions of or indicate future events or trends and which do not relate solely to historical matters. You can also identify forward-looking statements by discussions of strategy, plans or intentions.

Forward-looking statements involve numerous risks and uncertainties and you should not rely on them as predictions of future events. Forward-looking statements depend on assumptions, data or methods which may be incorrect or imprecise and we may not be able to realize them. We do not guarantee that the transactions and events described will happen as described (or that they will happen at all). The following factors, among others, could cause actual results and future events to differ materially from those set forth or contemplated in the forward-looking statements:

adverse economic or real estate developments in Texas, Arizona or Illinois;

general economic conditions;

market trends;

projected capital expenditures;

use of the proceeds of this offering;

estimates relating to our ability to make distributions to our shareholders in the future;

our understanding of our competition and our ability to compete effectively;