AVALONBAY COMMUNITIES INC
Form 10-Q
November 07, 2011
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2011

Commission file number 1-12672

AVALONBAY COMMUNITIES, INC.

(Exact name of registrant as specified in its charter)

Maryland	**77-0404318**
(State or other jurisdiction of	**(I.R.S. Employer**

incorporation or organization) **Identification No.)**

Ballston Tower

671 N. Glebe Rd, Suite 800

Arlington, Virginia 22203

(Address of principal executive offices, including zip code)

(703) 329-6300

(Registrant s telephone number, including area code)

(Former name, if changed since last report)

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

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

Indicate by check mark whether the Exchange 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 x	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

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

APPLICABLE ONLY TO CORPORATE ISSUERS

Indicate the number of shares outstanding of each of the issuer s classes of common stock as of the latest practicable date:

95,081,836 shares of common stock, par value $0.01 per share, were outstanding as of October 31, 2011

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AVALONBAY COMMUNITIES, INC.

FORM 10-Q

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AVALONBAY COMMUNITIES, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except per share data)

	9-30-11 (unaudited)	12-31-10
ASSETS		
Real estate:		
Land	$ 1,353,869	$ 1,344,946
Buildings and improvements	6,759,026	6,537,187
Furniture, fixtures and equipment	223,494	202,441
	8,336,389	8,084,574
Less accumulated depreciation	(1,825,094)	(1,682,845)
Net operating real estate	6,511,295	6,401,729
Construction in progress, including land	483,007	309,704
Land held for development	263,155	184,150
Operating real estate assets held for sale, net	58,326	60,062
Total real estate, net	7,315,783	6,955,645
Cash and cash equivalents	690,049	305,644
Cash in escrow	68,978	173,343
Resident security deposits	23,779	22,047
Investments in unconsolidated real estate entities	131,314	121,537
Deferred financing costs, net	35,633	33,284
Deferred development costs	72,479	77,253
Prepaid expenses and other assets	150,642	132,735
Total assets	$ 8,488,657	$ 7,821,488
LIABILITIES AND STOCKHOLDERS EQUITY		
Unsecured notes, net	$ 1,629,234	$ 1,820,141
Variable rate unsecured credit facility		
Mortgage notes payable	2,155,859	2,247,516
Dividends payable	84,815	76,676
Payables for construction	36,204	34,433
Accrued expenses and other liabilities	235,293	131,758
Accrued interest payable	23,600	32,248
Resident security deposits	37,550	33,785
Liabilities related to real estate assets held for sale	122,996	115,078
Total liabilities	4,325,551	4,491,635
Redeemable noncontrolling interests	6,844	14,262
Stockholders equity:		
Preferred stock, $0.01 par value; $25 liquidation preference; 50,000,000 shares authorized at both September 30, 2011 and December 31, 2010; zero shares issued and outstanding at September 30, 2011 and December 31, 2010, respectively		

Common stock, $0.01 par value; 140,000,000 shares authorized at both September 30, 2011 and December 31, 2010; 95,015,548 and 85,899,080 shares issued and outstanding at September 30, 2011 and December 31, 2010, respectively	950	859
Additional paid-in capital	4,638,386	3,593,677
Accumulated earnings less dividends	(409,477)	(282,743)
Accumulated other comprehensive loss	(80,866)	(1,175)
Total stockholders equity	4,148,993	3,310,618
Noncontrolling interest	7,269	4,973
Total equity	4,156,262	3,315,591
Total liabilities and stockholders equity	$ 8,488,657	$ 7,821,488

See accompanying notes to Condensed Consolidated Financial Statements.

AVALONBAY COMMUNITIES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

AND OTHER COMPREHENSIVE INCOME

(unaudited)

(Dollars in thousands, except per share data)

	For the three months ended		For the nine months ended	
	9-30-11	9-30-10	9-30-11	9-30-10
Revenue:				
Rental and other income	$ 248,644	$ 223,758	$ 720,535	$ 652,000
Management, development and other fees	2,433	1,800	7,085	5,334
Total revenue	251,077	225,558	727,620	657,334
Expenses:				
Operating expenses, excluding property taxes	70,017	66,569	200,401	190,872
Property taxes	24,535	23,225	73,238	69,191
Interest expense, net	43,970	44,262	134,096	128,260
Depreciation expense	62,262	57,926	185,071	169,819
General and administrative expense	6,087	7,039	21,524	19,975
Impairment loss	14,052		14,052	
Total expenses	220,923	199,021	628,382	578,117
Equity in income (loss) of unconsolidated entities	2,615	(325)	3,513	364
Gain on sale of land	13,716		13,716	
Income from continuing operations	46,485	26,212	116,467	79,581
Discontinued operations:				
Loss from discontinued operations	(1,808)	(2,232)	(5,737)	(4,387)
Gain on sale of real estate assets			7,675	72,220
Total discontinued operations	(1,808)	(2,232)	1,938	67,833
Net income	44,677	23,980	118,405	147,414
Net loss attributable to noncontrolling interests	147	674	132	890
Net income attributable to common stockholders	$ 44,824	$ 24,654	$ 118,537	$ 148,304
Other comprehensive income:				
Unrealized loss on cash flow hedges	(60,270)	(314)	(79,691)	(448)
Comprehensive income (loss)	$ (15,446)	$ 24,340	$ 38,846	$ 147,856

Earnings per common share - basic:				
Income from continuing operations attributable to common stockholders	$ 0.51	$ 0.32	$ 1.32	$ 0.96
Discontinued operations attributable to common stockholders	(0.02)	(0.03)	0.02	0.81
Net income attributable to common stockholders	$ 0.49	$ 0.29	$ 1.34	$ 1.77
Earnings per common share - diluted:				
Income from continuing operations attributable to common stockholders	$ 0.51	$ 0.32	$ 1.31	$ 0.95
Discontinued operations attributable to common stockholders	(0.02)	(0.03)	0.02	0.81
Net income attributable to common stockholders	$ 0.49	$ 0.29	$ 1.33	$ 1.76
Dividends per common share:	$ 0.8925	$ 0.8925	$ 2.6775	$ 2.6775

See accompanying notes to Condensed Consolidated Financial Statements.

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AVALONBAY COMMUNITIES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)

(Dollars in thousands)

	For the nine months ended 9-30-11	9-30-10
Net income	$ 118,405	$ 147,414
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation expense	185,071	169,819
Depreciation expense from discontinued operations	1,884	2,508
Amortization of deferred financing costs and debt premium/discount	4,888	5,944
Amortization of stock-based compensation	5,390	4,536
Equity in (income) loss of unconsolidated entities and noncontrolling interests, net of eliminations	(1,177)	852
Impairment loss	14,052	
Gain on sale of real estate assets	(21,391)	(72,220)
Expensed acquisition costs	1,010	
Increase in cash in operating escrows	(2,553)	(294)
Increase in resident security deposits, prepaid expenses and other assets	(17,683)	(25,221)
Increase in accrued expenses, other liabilities and accrued interest payable	7,116	1,041
Net cash provided by operating activities	295,012	234,379
Cash flows from investing activities:		
Development/redevelopment of real estate assets including land acquisitions and deferred development costs	(456,965)	(330,251)
Acquisition of real estate assets	(46,275)	
Capital expenditures - existing real estate assets	(14,838)	(9,683)
Capital expenditures - non-real estate assets	(7,911)	(517)
Proceeds from exchange/sale of real estate, net of selling costs	55,479	186,058
Increase (decrease) in payables for construction	1,770	(11,917)
Decrease in cash in construction escrows	13,421	32,940
Acquisition of mortgage note		(24,000)
Increase in investments in unconsolidated real estate entities	(14,163)	(20,977)
Net cash used in investing activities	(469,482)	(178,347)
Cash flows from financing activities:		
Issuance of common stock	1,037,630	322,257
Dividends paid	(233,427)	(222,081)
Repayments of mortgage notes payable	(42,648)	(29,433)
Repayment of unsecured notes	(189,900)	
Payment of deferred financing costs	(5,996)	(3,149)
Acquisition of joint venture partner equity interest	(6,570)	
Distributions to DownREIT partnership unitholders	(20)	(42)
Distributions to joint venture and profit-sharing partners	(194)	(164)
Net cash provided by financing activities	558,875	67,388

Net (decrease) increase in cash and cash equivalents	384,405	123,420
Cash and cash equivalents, beginning of period	305,644	105,691
Cash and cash equivalents, end of period	$ 690,049	$ 229,111
Cash paid during the period for interest, net of amount capitalized	$ 129,005	$ 125,190

See accompanying notes to Condensed Consolidated Financial Statements.

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CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)

Supplemental disclosures of non-cash investing and financing activities (amounts in whole dollars):

During the nine months ended September 30, 2011:

As described in Note 4, Stockholders Equity, 499,461 shares of common stock valued at $63,147,000 were issued in connection with stock grants primarily associated with the Company s 2008 deferred stock performance plan, as discussed in Note 9, Stock Based Compensation Plans ; 2,548 shares valued at $310,000 were issued through the Company s dividend reinvestment plan; 129,176 shares valued at $14,825,000 were withheld to satisfy employees tax withholding and other liabilities; and 505 shares valued at $16,000 were forfeited. In addition, the Company granted 144,827 options for common stock at a value of $4,258,000.

7,500 units of limited partnership, valued at $365,000, were presented for redemption to the DownREIT partnerships that issued such units and were acquired by the Company in exchange for an equal number of shares of the Company s common stock.

The Company recorded an increase to accrued expenses and other liabilities and a corresponding decrease to other comprehensive income of $79,691,000; and recorded a decrease to prepaid expenses and other assets of $1,324,000, with a corresponding offset to the basis of unsecured notes, net to record the impact of the Company s hedge accounting activity (as described in Note 5, Derivative Instruments and Hedging Activities).

Common dividends declared but not paid totaled $84,815,000.

The Company recorded an increase of $2,306,000 in redeemable noncontrolling interests with a corresponding decrease to accumulated earnings less dividends to adjust the redemption value associated with the put options held by joint venture partners and DownREIT partnership units. For further discussion of the nature and valuation of these items, see Note 11, Fair Value .

The Company repaid all amounts due under a $93,440,000 variable-rate, tax-exempt bond financing using the proceeds which were held in escrow.

The Company assumed a 4.75% coupon fixed-rate mortgage loan with an outstanding balance of $44,044,000 in conjunction with the acquisition of Fairfax Towers.

As part of an asset exchange in April 2011, the Company assumed a $55,400,000 fixed-rate mortgage loan with a 5.24% interest rate and relinquished a $55,800,000 mortgage loan with a 5.86% fixed rate.

The Company entered into a ground lease that is considered a capital lease associated with a development community, recording a capital lease obligation of $14,500,000 in accrued expenses and other liabilities with a corresponding offset to construction in progress including land.

The Company recorded an increase in noncontrolling interest of $3,350,000 associated with the consolidation of a development joint venture.

During the nine months ended September 30, 2010:

102,984 shares of common stock valued at $7,777,000 were issued in connection with stock grants; 4,716 shares valued at $419,000 were issued through the Company s dividend reinvestment plan; 46,852 shares valued at $3,990,000 were withheld to satisfy employees tax withholding and other liabilities; 1,300 shares valued at $39,000 were forfeited; and 61,055 shares valued at $3,322,000 were issued to members of the board of directors in fulfillment of deferred stock awards for a net value of $7,489,000. In addition, the Company granted 126,484 options for common stock at a value of $2,460,000.

25 units of limited partnership, valued at $3,000, were presented for redemption to the DownREIT partnerships that issued such units and were acquired by the Company in exchange for an equal number of shares of the Company s stock.

The Company recorded an increase to other liabilities and a corresponding decrease to other comprehensive income of $448,000 and recorded an increase to prepaid expenses and other assets of $2,181,000, with a corresponding offset to the basis of unsecured notes, net to record the impact of the Company s hedge accounting activity.

Common dividends declared but not paid totaled $76,127,000.

The Company recorded an increase of $5,305,000 in redeemable noncontrolling interests with a corresponding decrease to accumulated earnings less dividends to adjust the redemption value associated with the put options held by joint venture partners and DownREIT partnership units.

The Company recognized $4,812,000 in noncontrolling interest in conjunction with the consolidation of a Fund I subsidiary.

AVALONBAY COMMUNITIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

1. Organization, Basis of Presentation and Significant Accounting Policies

Organization and Basis of Presentation

AvalonBay Communities, Inc. (the Company, which term, unless the context otherwise requires, refers to AvalonBay Communities, Inc. together with its consolidated subsidiaries), is a Maryland corporation that elected to be taxed as a real estate investment trust (REIT) under the Internal Revenue Code of 1986 (the Code). The Company focuses on the development, acquisition, ownership and operation of apartment communities in high barrier to entry markets of the United States. These markets are located in the New England, Metro New York/New Jersey, Mid-Atlantic, Midwest, Pacific Northwest, and Northern and Southern California regions of the country.

At September 30, 2011, the Company owned or held a direct or indirect ownership interest in 184 operating apartment communities containing 53,826 apartment homes in ten states and the District of Columbia, of which eight communities containing 2,377 apartment homes were under reconstruction. In addition, the Company owned or held a direct or indirect ownership interest in 15 communities under construction that are expected to contain an aggregate of 3,600 apartment homes when completed. The Company also owned or held a direct or indirect ownership interest in land or rights to land in which the Company expects to develop an additional 29 communities that, if developed as expected, will contain an estimated 8,679 apartment homes.

The interim unaudited financial statements have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and in conjunction with the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in financial statements required by GAAP have been condensed or omitted pursuant to such rules and regulations. These unaudited financial statements should be read in conjunction with the financial statements and notes included in the Company s 2010 Annual Report on Form 10-K. The results of operations for the three and nine months ended September 30, 2011 are not necessarily indicative of the operating results for the full year. Management believes the disclosures are adequate to ensure the information presented is not misleading. In the opinion of management, all adjustments and eliminations, consisting only of normal, recurring adjustments necessary for a fair presentation of the financial statements for the interim periods, have been included.

All capitalized terms have the meaning as provided elsewhere in this Form 10-Q.

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Earnings per Common Share

Basic earnings per share is computed by dividing net income attributable to common stockholders by the weighted average number of shares outstanding during the period. All outstanding unvested restricted share awards contain rights to non-forfeitable dividends and participate in undistributed earnings with common shareholders and, accordingly, are considered participating securities that are included in the two-class method of computing basic earnings per share (EPS). Both the unvested restricted shares and other potentially dilutive common shares, and the related impact to earnings, are considered when calculating earnings per share on a diluted basis. The Company s earnings per common share are determined as follows (dollars in thousands, except per share data):

	For the three months ended		For the nine months ended	
	9-30-11	9-30-10	9-30-11	9-30-10
Basic and diluted shares outstanding				
Weighted average common shares - basic	91,388,357	84,968,804	88,312,930	83,385,833
Weighted average DownREIT units outstanding	7,707	15,346	8,559	15,349
Effect of dilutive securities	944,304	784,546	878,009	728,712
Weighted average common shares - diluted	92,340,368	85,768,696	89,199,498	84,129,894
Calculation of Earnings per Share - basic				
Net income attributable to common stockholders	$ 44,824	$ 24,654	$ 118,537	$ 148,304
Net income allocated to unvested restricted shares	(206)	(68)	(406)	(429)
Net income attributable to common stockholders, adjusted	$ 44,618	$ 24,586	$ 118,131	$ 147,875
Weighted average common shares - basic	91,388,357	84,968,804	88,312,930	83,385,833
Earnings per common share - basic	$ 0.49	$ 0.29	$ 1.34	$ 1.77
Calculation of Earnings per Share - diluted				
Net income attributable to common stockholders	$ 44,824	$ 24,654	$ 118,537	$ 148,304
Add: noncontrolling interests of DownREIT unitholders in consolidated partnerships, including discontinued operations	7	14	20	41
Adjusted net income attributable to common stockholders	$ 44,831	$ 24,668	$ 118,557	$ 148,345
Weighted average common shares - diluted	92,340,368	85,768,696	89,199,498	84,129,894
Earnings per common share - diluted	$ 0.49	$ 0.29	$ 1.33	$ 1.76

Certain options to purchase shares of common stock in the amounts of 320,698 and 1,039,724 were outstanding at September 30, 2011 and 2010, respectively, but were not included in the computation of diluted earnings per share because such options were anti-dilutive.

The Company is required to estimate the forfeiture of stock options and recognize compensation cost net of the estimated forfeitures. The estimated forfeitures included in compensation cost are adjusted to reflect actual forfeitures at the end of the vesting period. The forfeiture rate at September 30, 2011 is based on the average forfeiture activity over a period equal to the estimated life of the stock options, and was 0.9%. The application of estimated forfeitures did not materially impact compensation expense for the three and nine months ended September 30, 2011 or 2010.

Abandoned Pursuit Costs and Impairment of Long-Lived Assets

The Company performs a quarterly qualitative analysis to determine if there are changes in circumstances that suggest the carrying value of a long-lived asset or investment in an unconsolidated joint venture may not be recoverable. If an indication of impairment exists for long-lived assets, the Company then determines if its net book value is not considered recoverable based upon an analysis of its estimated undiscounted future cash flows, and if so, the Company will recognize an impairment loss to write the carrying basis in those assets down to their estimated fair value. In the case of its investments in unconsolidated joint ventures, the Company will recognize an impairment loss if the fair value is less than book value and when the decline in value is considered other than temporary.

In the third quarter of 2011, the Company concluded that the carrying basis of two land parcels being held for investment were not fully recoverable. In addition, the Company determined that its investment in an unconsolidated development joint venture was not recoverable and that the impairment was other than temporary. As a result, the Company recognized an aggregate charge of $14,052,000 for the impairment of these land parcels and the investment in the unconsolidated joint venture. The Company had previously recognized an impairment loss of $9,952,000 associated with the land parcels in 2008 when the Company determined that it no longer intended to pursue development of the assets. At that time, the Company had the intent and ability to hold the assets for the foreseeable future. In the third quarter of 2011, the Company decided it would pursue the sale of these land parcels.

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The Company s change in intent to pursue disposition of these assets rather than holding for investment triggered the determination that a further impairment of the basis for the land parcels existed. The Company also concluded that because the market for for-sale housing development has not improved as expected, its investment in the development joint venture was impaired, and that impairment was other than temporary. The joint venture currently holds undeveloped land and has an outstanding construction loan for $1,860,000. The Company valued its investment in the joint venture as the expected proceeds that it would receive if the entity were dissolved and the net assets were liquidated. Given the current zoning for residential development and the Company s knowledge of multifamily residential development, the fair value of the land parcel was determined using an internal discounted cash flow model. The Company valued the two impaired undeveloped land parcels using third party pricing. The third party pricing incorporated significant other unobservable inputs and are therefore classified as Level 3 prices in the fair value hierarchy.

The Company capitalizes pre-development costs incurred in pursuit of new development opportunities for which the Company currently believes future development is probable (Development Rights). Future development of these Development Rights is dependent upon various factors, including zoning and regulatory approval, rental market conditions, construction costs and the availability of capital. Initial pre-development costs incurred for pursuits for which future development is not yet considered probable are expensed as incurred. In addition, if the status of a Development Right changes, making future development by the Company no longer probable, any capitalized pre-development costs are written off with a charge to expense. The Company expensed costs related to abandoned pursuits, which includes the abandonment of Development Rights as well as costs incurred in pursuing the disposition of assets for which the disposition did not occur, in the amounts of $581,000 and $737,000 for the three months ended September 30, 2011 and 2010, respectively, and $1,627,000 and $1,685,000 for the nine months ended September 30, 2011 and 2010, respectively. These costs are included in operating expenses, excluding property taxes on the accompanying Condensed Consolidated Statements of Operations and Other Comprehensive Income. Abandoned pursuit costs can vary greatly, and the costs incurred in any given period may be significantly different in future periods.

Legal and Other Contingencies

The Company accounts for recoveries from legal matters as a reduction in the legal and related costs incurred associated with the matter, with recoveries in excess of these costs reported as a gain or, where appropriate, a reduction in the basis of a community to which the suit related. During the nine months ended September 30, 2010, the Company recognized receipt of settlement proceeds of $3,300,000 related to environmental contamination matters pursued by the Company. The Company reported $1,200,000 of these recoveries as a reduction in the legal and professional fees related to costs incurred in pursuit of the matters during 2010 and years prior as a component of general and administrative expense, with the remainder of the recovery reported as a reduction in the associated capitalized basis of the related communities. The Company did not have any material recoveries from legal matters in 2011.

The Company is involved in various claims and/or administrative proceedings that arise in the ordinary course of the Company s business. While no assurances can be given, the Company does not believe that any of these outstanding litigation matters, individually or in the aggregate, will have a material adverse effect on the Company s operations.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make certain estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenue and expenses during the reporting periods. Actual results could differ from those estimates.

Reclassifications

Certain reclassifications have been made to amounts in prior period financial statements to conform to current period presentations.

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2. Interest Capitalized

The Company capitalizes interest during the development and redevelopment of real estate assets. Capitalized interest associated with the Company s development or redevelopment activities totaled $8,946,000 and $7,774,000 for the three months ended September 30, 2011 and 2010, respectively, and $22,962,000 and $27,265,000 for the nine months ended September 30, 2011 and 2010, respectively.

3. Notes Payable, Unsecured Notes and Credit Facility

The Company s mortgage notes payable, unsecured notes, New Credit Facility and Cancelled Credit Facility, as of September 30, 2011 and December 31, 2010, are summarized below (dollars in thousands). The following amounts and discussion do not include the mortgage notes related to the communities classified as held for sale, if any, as of September 30, 2011 and December 31, 2010, as shown in the Condensed Consolidated Balance Sheets (see Note 7, Real Estate Disposition Activities).

	9-30-11	12-31-10
Fixed rate unsecured notes [1]	$ 1,556,001	$ 1,595,901
Variable rate unsecured notes [1]	75,000	225,000
Fixed rate mortgage notes payable - conventional and tax-exempt [2]	1,681,348	1,651,135
Variable rate mortgage notes payable - conventional and tax-exempt	473,481	596,381
Total notes payable and unsecured notes	3,785,830	4,068,417
New/Cancelled Credit Facility		
Total mortgage notes payable, unsecured notes and New/Cancelled Credit Facility	$ 3,785,830	$ 4,068,417

(1) Balances at September 30, 2011 and December 31, 2010 exclude $1,952 and $2,269, respectively, of debt discount, and $185 and $1,509, respectively, for basis adjustments, as reflected in unsecured notes on the Company s Condensed Consolidated Balance Sheets.

(2) Balance at September 30, 2011 excludes $ 1,030 of debt premium as reflected in mortgage notes payable on the Company s Condensed Consolidated Balance Sheet.

The following debt activity occurred during the nine months ended September 30, 2011:

In March 2011, the Company repaid a variable rate secured mortgage note in the amount of $28,785,000 in accordance with its scheduled maturity date.

As part of an asset exchange in April 2011, the Company assumed a $55,400,000 fixed-rate mortgage loan with a 5.24% interest rate, and relinquished a $55,800,000 mortgage loan with a 5.86% fixed-rate.

In conjunction with the acquisition of Fairfax Towers in April 2011, the Company assumed a $44,044,000 principal balance, 4.75% fixed-rate mortgage loan that matures in August 2015.

In April 2011, the Company repaid $93,440,000 in variable rate tax-exempt borrowings related to a Development Right. The bonds were repaid using the original issue proceeds, which were held in escrow.

In August 2011, the Company repaid a 7.25% fixed rate secured mortgage note in the amount of $7,191,000 in advance of its October 2011 scheduled maturity date at par.

In September 2011, the Company repaid $189,900,000 principal amount of its unsecured notes in accordance with their scheduled maturity. The notes had an all-in interest rate of 6.67%.

In September 2011, the Company entered into a new variable rate unsecured credit facility (the New Credit Facility) with an available borrowing capacity of $750,000,000 and a 4-year term, plus a one year extension option. We may elect to expand the facility to $1,300,000,000, provided that one or more banks (whether or not part of the current syndicate of banks) voluntarily agree to provide the additional commitment. No member of the syndicate of banks can prohibit the increase, which will only be effective to the extent banks from the syndicate or otherwise choose to commit to lend additional funds. The New Credit Facility was entered into with a syndicate of commercial banks to whom the Company pays an annual facility fee of approximately $1,313,000 and bears interest at varying levels based on the London Interbank Offered Rate (LIBOR), rating levels achieved on the Company s unsecured notes and on a maturity schedule selected by the Company. The current stated pricing is LIBOR plus 1.075% per annum (1.31% at September 30, 2011). The stated spread over LIBOR can vary from LIBOR plus 1.00% to LIBOR plus 1.85% based on the Company s credit ratings. In addition, the New Credit Facility includes a competitive bid option, which

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allows banks that are part of the lender consortium to bid to make loans to the Company at a rate that is lower than the stated rate provided by the New Credit Facility for up to $487,500,000. The competitive bid option may result in lower pricing than the stated rate if market conditions allow. The Company did not have any borrowings outstanding under the New Credit Facility and had $52,945,000 outstanding in letters of credit that reduced the borrowing capacity as of September 30, 2011. The New Credit Facility replaced the Company s prior $1,000,000,000 variable rate unsecured credit facility (the Cancelled Credit Facility) which was scheduled to expire in November 2011. At December 31, 2010, there were no amounts outstanding under the Cancelled Credit Facility and $44,105,000 outstanding in letters of credit.

In the aggregate, secured notes payable mature at various dates from May 2012 through July 2066, and are secured by certain apartment communities and improved land parcels (with a net carrying value of $1,713,916,000 as of September 30, 2011).

As of September 30, 2011, the Company has guaranteed approximately $273,128,000 of mortgage notes payable held by wholly owned subsidiaries; all such mortgage notes payable are consolidated for financial reporting purposes. The weighted average interest rate of the Company s fixed rate mortgage notes payable (conventional and tax-exempt) was 5.7% both at September 30, 2011 and at December 31, 2010. The weighted average interest rate of the Company s variable rate mortgage notes payable and its New Credit Facility, including the effect of certain financing related fees, was 2.4% at September 30, 2011 and the weighted average interest rate mortgage of the Company s variable rate mortgage notes payable and its Cancelled Credit Facility was 2.2% at December 31, 2010.

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Scheduled payments and maturities of mortgage notes payable and unsecured notes outstanding at September 30, 2011 are as follows (dollars in thousands):

Year	Secured notes payments (1)	Secured notes maturities	Unsecured notes maturities	Stated interest rate of unsecured notes
2011	$ 3,885	$	$	
2012	15,508	14,661	104,400	5.500%
			201,601	6.125%
			75,000	4.323%(2)
2013	15,134	318,045	100,000	4.950%
2014	16,031	33,100	150,000	5.375%
2015	13,867	405,613		
2016	14,690		250,000	5.750%
2017	15,568	18,300	250,000	5.700%
2018	16,498			
2019	2,588	651,973		
2020	2,761		250,000	6.100%
Thereafter	357,975	238,635	250,000	3.950%
	$ 474,502	$ 1,680,327	$ 1,631,001	

(1) Secured note payments are comprised of the principal pay downs for amortizing mortgage notes.
(2) The weighted average interest rate for the swapped unsecured notes as of September 30, 2011.

The Company was in compliance at September 30, 2011 with certain customary financial and other covenants under the New Credit Facility and the Company s unsecured notes.

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4. Stockholders Equity

The following summarizes the changes in stockholders equity for the nine months ended September 30, 2011 (dollars in thousands):

	Common stock	Additional paid-in capital	Accumulated earnings less dividends	Accumulated other comprehensive loss	Total AvalonBay stockholders' equity	Noncontrolling interests	Total equity
Balance at December 31, 2010	$ 859	$ 3,593,677	$ (282,743)	$ (1,175)	$ 3,310,618	$ 4,973	$ 3,315,591
Net income attributable to common stockholders			118,537		118,537		118,537
Unrealized loss on cash flow hedges				(79,691)	(79,691)		(79,691)
Change in redemption value of redeemable noncontrolling interest			(2,306)		(2,306)		(2,306)
Noncontrolling interests						2,296	2,296
Dividends declared to common stockholders			(241,876)		(241,876)		(241,876)
Issuance of common stock, net of withholdings	91	1,024,097	(1,089)		1,023,099		1,023,099
Amortization of deferred compensation		20,612			20,612		20,612
Balance at September 30, 2011	$ 950	$ 4,638,386	$ (409,477)	$ (80,866)	$ 4,148,993	$ 7,269	$ 4,156,262

During the nine months ended September 30, 2011, the Company:

(i) issued 7,922,933 shares of common stock through public offerings;

(ii) issued 813,707 shares of common stock in connection with stock options exercised;

(iii) issued 2,548 common shares through the Company s dividend reinvestment plan;

(iv) issued 499,461 common shares in connection with stock grants;

(v) issued 7,500 common shares for Down REIT OP units conversion;

(vi) withheld 129,176 common shares to satisfy employees tax withholding and other liabilities; and

(vii) redeemed 505 shares of restricted common stock upon forfeiture.

In addition, the Company granted 144,827 options for common stock to employees. Any deferred compensation related to the Company s stock option and restricted stock grants during the nine months ended September 30, 2011 is not reflected on the Company s Condensed Consolidated Balance Sheet as of September 30, 2011, and will not be reflected until earned as compensation cost.

In August 2011, the Company issued 5,865,000 shares of its common stock at a net price of $128.25 per share. Net proceeds after underwriting discounts of approximately $725,850,000 are expected to be used for working capital, capital expenditures and other general corporate purposes, which may include development, redevelopment and acquisitions of operating communities and refinancing of debt.

In November 2010, the Company commenced a second continuous equity program (CEP II), under which the Company may sell up to $500,000,000 of its common stock from time to time during a 36-month period. During the three months ended September 30, 2011, the Company sold 256,167 shares at an average sales price of $127.90 per share, for net proceeds of $32,271,000. During the nine months ended September 30, 2011, the Company sold 2,057,933 shares at an average sales price of $121.39 per share, for aggregate net proceeds of $246,065,000. From program inception in November 2010 through September 30, 2011, the Company sold 2,490,765 shares at an average sales price of $119.84 per share for aggregate net proceeds of $294,000,000.

5. Derivative Instruments and Hedging Activities

The Company enters into interest rate swap and interest rate cap agreements (collectively, the Hedging Derivatives) for interest rate risk management purposes and in conjunction with certain variable rate secured debt to satisfy lender requirements. The Company does not enter into derivative transactions for trading or other speculative purposes. In April 2011, the Company entered into $430,000,000 of forward starting interest rate swaps where the Company has agreed to pay a fixed rate of interest in exchange for a floating rate of interest at a future date. These swaps were transacted to reduce the Company s exposure to fluctuations in interest rates on future debt issuances, and are not expected to impact the Company s 2011 Net Income.

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The following table summarizes the consolidated Hedging Derivatives at September 30, 2011, excluding derivatives executed to hedge debt on communities classified as held for sale (dollars in thousands):

	Non-designated Hedges Interest Rate Caps	Cash Flow Hedges Interest Rate Caps	Cash Flow Hedges Interest Rate Swaps (2)	Fair Value Hedges Interest Rate Swaps
Notional balance	$ 75,847	$ 195,498	$ 430,000	$ 75,000
Weighted average interest rate (1)	1.1%	2.3%	4.5%	4.3%
Weighted average capped interest rate	7.1%	5.3%	N/A	N/A
Earliest maturity date	Aug-12	Jun-12	Sep-12	Jan-12
Latest maturity date	Mar-14	Jun-15	May-13	Jan-12
Estimated fair value, asset/(liability)	$ 3	$ 147	$ (79,293)	$ 185

(1) For interest rate caps, this represents the weighted average interest rate on the debt.
(2) The fair value of these hedging derivatives at maturity is expected to be recognized over the term of the forecasted hedged transaction.

Excluding derivatives executed to hedge debt on communities classified as held for sale, the Company had seven derivatives designated as cash flow hedges, two derivatives designated as fair value hedges and four derivatives not designated as hedges at September 30, 2011. Fair value changes for derivatives that are not in qualifying hedge relationships are reported as a component of general and administrative expenses on the accompanying Condensed Consolidated Statements of Operations and Other Comprehensive Income. Fair value changes for derivatives not in qualifying hedge relationships for the nine months ended September 30, 2011, were not material. For the derivative positions that the Company has determined qualify as effective cash flow hedges, the Company has recorded the effective portion of cumulative changes in the fair value of the Hedging Derivatives in other comprehensive income. Amounts recorded in other comprehensive income will be reclassified into earnings in the periods in which earnings are affected by the hedged cash flow. To adjust the Hedging Derivatives in qualifying cash flow hedges to their fair value and recognize the impact of hedge accounting, the Company recorded decreases in other comprehensive income of $79,691,000 and $448,000 during the nine months ended September 30, 2011 and 2010, respectively. The amount reclassified into earnings for the nine months ended September 30, 2011, as well as the estimated amount included in accumulated other comprehensive income as of September 30, 2011, expected to be reclassified into earnings within the next twelve months to offset the variability of cash flows of the hedged items during this period are not material. For the derivative positions that the Company has determined qualify as effective fair value hedges, the Company has recorded a decrease in the fair value of $1,324,000 and an increase of $2,181,000 for the nine months ended September 30, 2011 and 2010, respectively. The derivatives fair value is reported as a component of prepaid expenses and other assets, with the associated gain or loss as an adjustment to the carrying amount of the corresponding debt being hedged on the accompanying Condensed Consolidated Balance Sheets as of September 30, 2011.

The Company assesses, both at inception and on an on-going basis, the effectiveness of qualifying cash flow and fair value hedges. Hedge ineffectiveness, reported as a component of general and administrative expenses, did not have a material impact on earnings of the Company for any prior period, and the Company does not anticipate that it will have a material effect in the future. The fair values of the Hedging Derivatives and non-designated derivatives that are in an asset position are recorded in prepaid expenses and other assets. The fair value of derivatives that are in a liability position are included in accrued expenses and other liabilities on the accompanying Condensed Consolidated Balance Sheets.

Derivative financial instruments expose the Company to credit risk in the event of nonperformance by the counterparties under the terms of the Hedging Derivatives. The Company minimizes its credit risk on these transactions by dealing with major, creditworthy financial institutions which have an A+ or better credit rating by the Standard & Poor s Ratings Group. As part of its on-going control procedures, the Company monitors the credit ratings of counterparties and the exposure of the Company to any single entity, thus minimizing credit risk concentration. The Company believes the likelihood of realizing losses from counterparty non-performance is remote. The Company incorporates credit valuation adjustments to appropriately reflect both its own nonperformance risk and the respective counterparty s nonperformance risk in the fair value measurements of its derivative financial instruments. Refer to Note 11, Fair Value, for further discussion.

6. Investments in Real Estate Entities

Investments in consolidated entities

In April 2011, the Company completed an exchange of assets with UDR, Inc. (UDR). The transaction included exchanging a portfolio of three communities and a parcel of land owned by the Company for a portfolio of six UDR communities and $26,000,000 in cash. The Company s portfolio consisted of two properties and a small land parcel located in metropolitan Boston and one property located in San Francisco. The UDR portfolio is located in Southern California (Los Angeles, Orange County and San Diego). The Company accounted for the exchange as a non-monetary transaction based on the carrying value of the assets relinquished by the Company. The Company recognized a partial gain of $7,675,000, related to the monetary consideration received, representing the proportionate share of the assets sold. In addition, the Company assumed a $55,400,000 5.24% fixed-rate mortgage loan that matures in June 2013. In exchange, the Company relinquished a $55,800,000 5.86% fixed-rate mortgage loan that matures in May 2019.

Also in April 2011, the Company acquired Fairfax Towers, located in Falls Church, Virginia. Fairfax Towers contains 415 apartment homes and was acquired for a purchase price of $89,200,000. In conjunction with this acquisition, the Company assumed the existing 4.75% fixed-rate mortgage loan with an outstanding principal amount of $44,044,000 which matures in August 2015.

The Company accounted for the acquisition of Fairfax Towers as a business combination and allocated the purchase price to the acquired assets and assumed liabilities, including identifiable intangibles, based on their fair values. The Company looked to third party pricing for the value of the land, and an internal model to determine the fair value of the real estate assets, in place leases and mortgage loan. Given the heterogeneous nature of multi-family real estate, the fair values for the land, real estate assets and in place leases incorporated significant unobservable inputs and therefore are considered to be Level 3 prices within the fair value hierarchy. The Company used a discounted cash flow analysis on the expected cash flows of the mortgage note to determine its fair value, considering the contractual terms of the instrument and observable market-based inputs. The fair value of the mortgage loan is considered a Level 2 price as the majority of the inputs used fall within Level 2 of the fair value hierarchy.

Transaction costs for the asset exchange and acquisition of Fairfax Towers were $1,010,000. These costs are included in operating expenses, excluding property taxes on the accompanying Condensed Consolidated Statements of Operations and Other Comprehensive Income.

Investment in unconsolidated entities

As of September 30, 2011, the Company had investments in six unconsolidated real estate entities with ownership interest percentages ranging from 15.2% to 50%. The Company accounts for its investments in unconsolidated real estate entities under the equity method of accounting, except as otherwise noted below. The significant accounting policies of the Company s unconsolidated real estate entities are consistent with those of the Company in all material respects.

During the three months ended September 30, 2011, AvalonBay Value Added Fund I, LP (Fund I) sold Avalon Redondo Beach, located in Redondo Beach, CA. The community contains 105 apartment homes and was sold for $33,100,000. This disposition resulted in a gain in accordance with GAAP of approximately $12,445,000, of which $1,743,000 represents the portion attributable to the Company.

In July 2011, AvalonBay Value Added Fund II, LP (Fund II) acquired Captain Parker Arms, a garden-style community consisting of 94 apartment homes located in Lexington, MA. The community was acquired for a purchase price of $20,850,000.

In addition, as discussed in Note 1 Organization, Basis of Presentation and Significant Accounting Policies , the Company recorded an impairment loss related to its investment in an unconsolidated development joint venture, see footnote 8 in the following table.

There were no other changes in the Company s ownership interest in, or presentation of, its investments in unconsolidated real estate entities during the three months ended September 30, 2011.

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Detail of the real estate and associated funding underlying the Company s unconsolidated investments is presented in the following table (unaudited, dollars in thousands):

	Unconsolidated Real Estate Investments	Company Ownership Percentage	# of Apartment Homes	Total Capitalized Cost (1)	Debt Amount (2)	Type	Interest Rate (3)	Maturity Date
Fund I								
1.	Avalon Lakeside - Chicago, IL		204	$ 18,581	$ 12,056	Fixed	5.74%	Mar 2012
2.	Avalon Columbia - Baltimore, MD		170	29,410	22,275	Fixed	5.48%	Apr 2013
3.	Avalon Sunset - Los Angeles, CA		82	20,903	12,750	Fixed	5.41%	Mar 2014
4.	Avalon at Poplar Creek - Chicago, IL		196	28,132	16,500	Fixed	4.83%	Oct 2013
5.	Avalon at Civic Center - Norwalk, CA		192	42,756	27,001	Fixed	5.38%	Aug 2013
6.	Avalon Paseo Place - Fremont, CA		134	25,081	11,800	Fixed	5.74%	Nov 2014
7.	Avalon at Yerba Buena - San Francisco, CA		160	66,811	41,500	Fixed	5.88%	Mar 2014
8.	Avalon at Aberdeen Station - Aberdeen, NJ		290	58,614	39,842	Fixed	5.64%	Sep 2013
9.	The Springs - Corona, CA (4)		320	29,926	23,653	Fixed	6.06%	Oct 2014
10.	Avalon Lombard - Lombard, IL		256	35,323	17,243	Fixed	5.43%	Jan 2014
11.	Avalon Cedar Place - Columbia, MD		156	24,505	12,000	Fixed	5.68%	Feb 2015
12.	Avalon Centerpoint - Baltimore, MD (5)		392	80,257	45,000	Fixed	5.74%	Dec 2014
13.	Middlesex Crossing - Billerica, MA		252	38,406	24,100	Fixed	5.49%	Dec 2014
14.	Avalon Crystal Hill - Ponoma, NY		168	38,645	24,500	Fixed	5.43%	Dec 2014
15.	Avalon Skyway - San Jose, CA		348	78,250	37,500	Fixed	6.11%	Mar 2014
16.	Avalon Rutherford Station - East Rutherford, NJ		108	36,821	19,544	Fixed	6.13%	Sep 2016
17.	South Hills Apartments - West Covina, CA		85	24,756	11,761	Fixed	5.92%	Oct 2014
18.	Weymouth Place - Weymouth, MA		211	25,298	13,455	Fixed	5.12%	Mar 2015
	Total Fund I	15.2%	3,724	$ 702,475	$ 412,480		5.7%	
Fund II								
1.	Avalon Bellevue Park - Bellevue, WA		220	$ 33,993	$ 21,515	Fixed	5.52%	Jun 2019
2.	Avalon Fair Oaks - Fairfax, VA		491	72,164	42,600	Fixed	5.26%	May 2017
3.	Avalon Rothbury - Gaithersburg, MD		203	31,481	18,750	Variable	2.78%	Jun 2017
4.	The Apartments at Briarwood - Owings Mills, MD		348	45,413	26,850	Fixed	3.64%	Nov 2017
5.	Grove Park Apartments - Gaithersburg, MD		684	102,028	63,200	Fixed	5.42%	Jan 2018
6.	Creekside Meadows - Tustin, CA		628	100,462	59,100	Fixed	3.81%	Oct 2017
7.	Canyonwoods - Lake Forest, CA		140	25,459		N/A	N/A	N/A
8.	Fox Run Apartments - Plainsboro, NJ (6)		776	87,288	54,296	Fixed	4.56%	Nov 2014
9.	Waterstone Carlsbad - Carlsbad, CA		448	78,661	46,141	Fixed	4.68%	Feb 2018
10	Yale Village - Rockville, MD		210	49,529	32,131	Fixed	4.26%	Aug 2019
11	Captain Parker Arms - Lexington, MA		94	20,852	13,500	Fixed	3.90%	Sept 2019
	Total Fund II	31.3%	4,242	$ 647,330	$ 378,083		4.5%	
Other Operating Joint Ventures								
1.	Avalon Chrystie Place I - New York, NY (7)	20.0%	361	$ 136,572	$ 117,000	Variable	0.88%	Nov 2036

2.	Avalon at Mission Bay North II - San Francisco, CA (7)	25.0%	313	124,060	105,000	Fixed	6.02%	Dec 2015
3.	Avalon Del Rey - Los Angeles, CA	30.0%	309	70,080	44,464	Variable	3.53%	Apr 2016
Other Development Joint Ventures								
1.	Aria at Hathorne - Danvers, MA (8)	50.0%	64	N/A	1,860	Variable	7.98%	Jun 2010
	Total Other Joint Ventures		1,047	$ 330,712	$ 268,324		3.4%	
	Total Unconsolidated Investments		9,013	$ 1,680,517	$ 1,058,887		4.7%	

(1) Represents total capitalized cost as of September 30, 2011.
(2) The Company has not guaranteed the debt of its unconsolidated investees and bears no responsibility for the repayment, other than the construction and completion and related financing guarantee for Avalon Chrystie Place I associated with the construction completion and occupancy certificate.
(3) Represents weighted average rate on outstanding debt as of September 30, 2011.
(4) Beginning in the third quarter of 2010, the Company consolidated the net assets and results of operations of The Springs.
(5) Borrowing on this community is comprised of three mortgage loans.
(6) Borrowing on this community is comprised of two mortgage loans.
(7) After the venture makes certain threshold distributions to the third-party partner, the Company generally receives 50% of all further distributions.
(8) As of September 30, 2011, the amounts under this borrowing have not been repaid and the lender has declared an event of default with respect to the note and required the venture to pay a default rate of interest, which is not material to the Company. Although the Company has not guaranteed the debt of Aria at Hathorne nor does it have any obligation to fund the debt should the venture be unable to do so, the Company has the right to cure any event of default by the venture. The Company determined that the value of its investment was impaired and this impairment was other than temporary, recognizing a charge in the third quarter of 2011.

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The following is a combined summary of the financial position of the entities accounted for using the equity method, as of the dates presented (dollars in thousands):

	9-30-11 (unaudited)	12-31-10 (unaudited)
Assets:		
Real estate, net	$ 1,493,832	$ 1,393,274
Other assets	82,916	67,278
Total assets	$ 1,576,748	$ 1,460,552
Liabilities and partners capital:		
Mortgage notes payable and credit facility	$ (1,035,234)	$ (965,931)
Other liabilities	(30,390)	(24,835)
Partners capital	(511,124)	(469,786)
Total liabilities and partners capital	$ (1,576,748)	$ (1,460,552)

The following is a combined summary of the operating results of the entities accounted for using the equity method, for the periods presented (dollars in thousands):

	For the three months ended		For the nine months ended	
	9-30-11 (unaudited)	9-30-10 (unaudited)	9-30-11 (unaudited)	9-30-10 (unaudited)
Rental and other income	$ 40,953	$ 28,236	$ 117,407	$ 81,066
Operating and other expenses	(18,829)	(15,488)	(53,474)	(40,290)
Gain on sale of communities	12,445		12,445	
Interest expense, net	(12,818)	(9,958)	(37,596)	(28,548)
Depreciation expense	(12,363)	(9,242)	(35,702)	(26,494)
Net income (loss)	$ 9,388	$ (6,452)	$ 3,080	$ (14,266)

In conjunction with the formation of Fund I and Fund II, as well as the acquisition and development of certain other investments in unconsolidated entities, the Company incurred costs in excess of its equity in the underlying net assets of the respective investments. These costs represent $9,427,000 at September 30, 2011 and $9,566,000 at December 31, 2010 of the respective investment balances.

As part of the formation of Fund I and Fund II, the Company provided separate and distinct guarantees to one of the limited partners in each of the ventures. These guarantees are specific to the respective fund and any impacts or obligation of the Company to perform under one of the guarantees has no impact on the Company s obligations with respect to the other guarantee. The guarantees provide that, if, upon final liquidation of Fund I or Fund II, the total amount of all distributions to the guaranteed partner during the life of the respective fund (whether from operating cash flow or property sales) does not equal the total capital contributions made by that partner, then the Company will pay the guaranteed partner an amount equal to the shortfall, but in no event more than 10% of the total capital contributions made by the guaranteed partner (maximum of approximately $7,500,000 for Fund I and approximately $7,095,000 for Fund II as of September 30, 2011). As of September 30, 2011, the expected realizable values of the real estate assets owned by Fund I and Fund II are considered adequate to cover such potential payments under a liquidation scenario. The estimated fair value of, and the Company s obligation under these guarantees, both at inception and as of September 30, 2011, was not significant and therefore the Company has not recorded any obligation for either of these guarantees as of September 30, 2011.

7. Real Estate Disposition Activities

During the third quarter of 2011, the Company sold three unimproved land parcels in Canoga Park, CA, Kirkland, WA and Danvers, MA. The Company sold these land parcels for $34,475,000, resulting in an aggregate gain in accordance with GAAP of $13,716,000. The Company recorded aggregate impairment charges of approximately $20,200,000 related to two of these assets in prior years when it determined that it would no longer develop the assets.

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As of September 30, 2011, the Company had one community that qualified as discontinued operations and held for sale.

The operations for any real estate assets sold from January 1, 2010 through September 30, 2011 have been presented as income from discontinued operations in the accompanying Condensed Consolidated Statements of Operations and Other Comprehensive Income. Accordingly, certain reclassifications have been made to prior years to reflect discontinued operations consistent with current year presentation.

The following is a summary of income (loss) from discontinued operations for the periods presented (dollars in thousands):

	For the three months ended		For the nine months ended	
	9-30-11 (unaudited)	9-30-10 (unaudited)	9-30-11 (unaudited)	9-30-10 (unaudited)
Rental income	$ 2,111	$ 2,152	$ 6,235	$ 10,182
Operating and other expenses	(3,445)	(3,557)	(10,088)	(12,061)
Depreciation expense	(474)	(827)	(1,884)	(2,508)
Income (loss) from discontinued operations	$ (1,808)	$ (2,232)	$ (5,737)	$ (4,387)

8. Segment Reporting

The Company s reportable operating segments include Established Communities, Other Stabilized Communities, and Development/Redevelopment Communities. Annually as of January 1st, the Company determines which of its communities fall into each of these categories and maintains that classification, unless disposition plans regarding a community change, throughout the year for the purpose of reporting segment operations.

In addition, the Company owns land for future development and has other corporate assets that are not allocated to an operating segment.

The Company s segment disclosures present the measure(s) used by the chief operating decision maker for purposes of assessing each segments performance. The Company s chief operating decision maker is comprised of several members of its executive management team who use net operating income (NOI) as the primary financial measure for Established Communities and Other Stabilized Communities. NOI is defined by the Company as total revenue less direct property operating expenses. Although the Company considers NOI a useful measure of a community s or communities operating performance, NOI should not be considered an alternative to net income or net cash flow from operating activities, as determined in accordance with GAAP. NOI excludes a number of income and expense categories as detailed in the reconciliation of NOI to net income.

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A reconciliation of NOI to net income for the three and nine months ended September 30, 2011 and 2010 is as follows (dollars in thousands):

	For the three months ended		For the nine months ended	
	9-30-11	9-30-10	9-30-11	9-30-10
Net income	$ 44,677	$ 23,980	$ 118,405	$ 147,414
Indirect operating expenses, net of corporate income	7,734	7,189	22,463	22,269
Investments and investment management expense	1,328	1,026	3,860	3,111
Expensed acquisition, development and other pursuit costs	633	737	2,636	1,685
Interest expense, net	43,970	44,262	134,096	128,260
General and administrative expense	6,087	7,039	21,524	19,975
Equity in (income) loss of unconsolidated entities	(2,615)	325	(3,513)	(364)
Depreciation expense	62,262	57,926	185,071	169,819
Impairment loss	14,052		14,052	
Gain on sale of real estate assets	(13,716)		(21,391)	(72,220)
(Income) loss from discontinued operations	1,808	2,232	5,737	4,387
Net operating income	$ 166,220	$ 144,716	$ 482,940	$ 424,336

The primary performance measure for communities under development or redevelopment depends on the stage of completion. While under development, management monitors actual construction costs against budgeted costs as well as lease-up pace and rent levels compared to budget.

The following table provides details of the Company s segment information as of the dates specified (dollars in thousands). The segments are classified based on the individual community s status as of the beginning of the given calendar year. Therefore, each year the composition of communities within each business segment is adjusted. Accordingly, the amounts between years are not directly comparable. Segment information for the three and nine months ended September 30, 2011 and 2010 have been adjusted for the real estate assets that were sold from January 1, 2010 through September 30, 2011, or otherwise qualify as discontinued operations as of September 30, 2011, as described in Note 7, Real Estate Disposition Activities.

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	For the three months ended			For the nine months ended			
	Total revenue	NOI	% NOI change from prior year	Total revenue	NOI	% NOI change from prior year	Gross real estate (1)
For the period ended September 30, 2011							
Established							
New England	$ 43,277	$ 27,560	8.6%	$ 126,387	$ 80,048	8.6%	$ 1,300,019
Metro NY/NJ	49,721	33,707	10.0%	145,912	98,420	7.3%	1,532,296
Mid-Atlantic/Midwest	31,420	22,055	6.1%	92,519	66,102	6.8%	726,938
Pacific Northwest	9,560	6,120	7.1%	28,035	18,609	4.7%	362,806
Northern California	26,132	18,399	11.1%	76,178	53,967	9.3%	930,859
Southern California	19,035	12,699	13.1%	55,997	37,047	7.8%	695,828
Total Established	179,145	120,540	9.3%	525,028	354,193	7.7%	5,548,746
Other Stabilized	35,751	23,309	N/A	101,799	65,604	N/A	1,566,557
Development / Redevelopment	33,748	22,371	N/A	93,708	63,143	N/A	1,627,772
Land Held for Future Development	N/A	N/A	N/A	N/A	N/A	N/A	263,155
Non-allocated (2)	2,433	N/A	N/A	7,085	N/A	N/A	76,321
Total	$ 251,077	$ 166,220	14.9%	$ 727,620	$ 482,940	13.8%	$ 9,082,551
For the period ended September 30, 2010							
Established							
New England	$ 36,291	$ 22,562	(0.1)%	$ 107,138	$ 66,505	(2.3)%	$ 1,099,428
Metro NY/NJ	45,945	29,944	(2.2)%	135,622	90,041	(3.4)%	1,391,159
Mid-Atlantic/Midwest	28,358	19,721	1.9%	83,664	58,666	(1.0)%	668,997
Pacific Northwest	6,593	4,035	(14.7)%	19,824	12,710	(14.6)%	239,936
Northern California	29,754	20,248	(1.4)%	88,707	60,651	(8.0)%	1,113,445
Southern California	14,683	9,328	(2.8)%	44,142	28,466	(6.9)%	468,666
Total Established	161,624	105,838	(1.5)%	479,097	317,039	(4.4)%	4,981,631
Other Stabilized	31,782	19,411	N/A	90,442	54,405	N/A	1,578,660
Development / Redevelopment	30,352	19,467	N/A	82,461	52,892	N/A	1,604,250
Land Held for Future Development	N/A	N/A	N/A	N/A	N/A	N/A	228,496
Non-allocated (2)	1,800	N/A	N/A	5,334	N/A	N/A	74,538
Total	$ 225,558	$ 144,716	4.6%	$ 657,334	$ 424,336	2.4%	$ 8,467,575

(1) Does not include gross real estate assets held for sale of $82,931 and $82,743 as of September 30, 2011 and 2010, respectively.

(2) Revenue represents third party management, asset management and developer fees and miscellaneous income which are not allocated to a reportable segment.

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9. Stock-Based Compensation Plans

Information with respect to stock options granted under the Company s 1994 Stock Option and Incentive Plan (the 1994 Plan) and under the AvalonBay Communities, Inc. 2009 Stock Option and Incentive Plan (the 2009 Plan) are as follows (dollars in thousands, other than per share amounts):

	2009 Plan shares	Weighted average exercise price per share	1994 Plan shares	Weighted average exercise price per share
Options Outstanding, December 31, 2010	126,484	$ 74.20	2,072,217	$ 88.50
Exercised	(18,487)	74.20	(795,220)	82.86
Granted	144,827	115.83		
Forfeited			(21,653)	43.29
Options Outstanding, September 30, 2011	252,824	$ 98.05	1,255,344	$ 92.86
Options Exercisable September 30, 2011	26,138	$ 74.20	1,148,381	$ 96.98

The weighted average fair value of the options granted under the 2009 Plan during the nine months ended September 30, 2011 is estimated at $29.40 per share on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions: dividend yield of 4.0% over the expected life of the option, volatility of 35.00%, risk-free interest rate of 3.0% and an expected life of approximately seven years.

At September 30, 2011, the Company had 421,045 outstanding unvested shares granted under restricted stock awards including activity under the 2008 Plan discussed below. Restricted stock vesting during the nine months ended September 30, 2011 totaled 305,526 shares and had fair values at the grant date ranging from $48.60 to $147.75 per share. The total grant date fair value of shares vested was $34,899,000 and $9,467,000 for the nine months ended September 30, 2011 and 2010, respectively.

Total employee stock-based compensation cost recognized in income was $7,614,000 and $7,709,000 for the nine months ended September 30, 2011 and 2010, respectively, and total capitalized stock-based compensation cost was $4,118,000 and $3,857,000 for the nine months ended September 30, 2011 and 2010, respectively. At September 30, 2011, there was a total of $2,364,000 and $7,736,000 in unrecognized compensation cost for unvested stock options and unvested restricted stock, respectively, which does not include estimated forfeitures. The unrecognized compensation cost for unvested stock options and restricted stock is expected to be recognized over a weighted average period of 2.03 years and 2.62 years, respectively.

Deferred Stock Performance Plan

On June 1, 2011, the measurement period for the Company s 2008 deferred stock performance plan (the 2008 Plan) ended with the maximum award achieved thereunder. This resulted in the Company issuing 397,370 shares of restricted and unrestricted stock valued at $51,153,000. The total cost recognized in earnings in connection with the 2008 Plan was $801,000 and $1,280,000 for the nine months ended September 30, 2011 and 2010, respectively, and total capitalized stock-based compensation cost was $498,000 and $699,000 for the nine months ended September 30, 2011 and 2010, respectively.

10. Related Party Arrangements

Unconsolidated Entities

The Company manages unconsolidated real estate entities for which it receives asset management, property management, development and redevelopment fee revenue. From these entities, the Company received fees of $2,433,000 and $1,800,000 in the three months ended September 30, 2011 and 2010, respectively, and $7,085,000 and $5,334,000 for the nine months ended September 30, 2011 and 2010, respectively. These fees are included in management, development and other fees on the accompanying Condensed Consolidated Statements of Operations and Other Comprehensive Income. In addition, the Company has outstanding receivables associated with its management role of

$5,260,000 and $4,135,000 as of September 30, 2011 and December 31, 2010, respectively.

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Director Compensation

The Company recorded non-employee director compensation expense relating to restricted stock grants and deferred stock awards in the amount of $195,000 and $569,000 for the three and nine months ended September 30, 2011 as a component of general and administrative expense. Deferred compensation relating to these restricted stock grants and deferred stock awards were $579,000 and $312,000 on September 30, 2011 and December 31, 2010, respectively.

11. Fair Value

Financial Instruments Carried at Fair Value

Derivative Financial Instruments

Currently, the Company uses interest rate swap and interest rate cap agreements to manage its interest rate risk. These instruments are carried at fair value in the Company s financial statements. See Note 5, Derivative Instruments and Hedging Activities, for derivative values at September 30, 2011 and a description of where these amounts are recorded in the financial statements. In adjusting the fair value of its derivative contracts for the effect of counterparty nonperformance risk, the Company has considered the impact of its net position with a given counterparty, as well as any applicable credit enhancements, such as collateral postings, thresholds, mutual puts, and guarantees. Although the Company has determined that the majority of the inputs used to value its derivatives fall within Level 2 of the fair value hierarchy, the credit valuation adjustments associated with its derivatives use Level 3 inputs, such as estimates of current credit spreads, to evaluate the likelihood of default by itself and its counterparties. As of September 30, 2011, the Company assessed the significance of the impact of the credit valuation adjustments on the overall valuation of its derivative positions and has determined it is not significant. As a result, the Company has determined that its derivative valuations are classified in Level 2 of the fair value hierarchy.

Redeemable Noncontrolling Interests

Puts The Company provided redemption options (the Puts) that allow two of the Company s joint venture partners to require the Company to purchase their interests in the investments at the future fair market value. In March 2011, the Company acquired the noncontrolling interest associated with a consolidated community for $6,570,000 satisfying its obligation under one of the Puts. The remaining Put is payable in cash or, at the Company s option, common stock of the Company. The Company determines the fair value of the Put based on unobservable inputs considering the assumptions that market participants would make in pricing the obligations. The Company applies discount factors to the estimated future cash flows of the asset underlying the associated joint venture, which in the case of the Put is the NOI from an apartment community, as well as potential disposition proceeds utilizing market capitalization rates, to derive the fair value of the position. Given the significance of the unobservable inputs, the valuations are classified in Level 3 of the fair value hierarchy. At December 31, 2010, the Puts aggregate fair value was $12,106,000. At September 30, 2011, the aggregate fair value of the remaining outstanding Put was $5,529,000.

DownREIT units The Company issued units of limited partnership interest in DownREITs which provide the DownREIT limited partners the ability to present all or some of their units for redemption for a cash amount as determined by the applicable partnership agreement. Under the DownREIT agreements, for each limited partnership unit, the limited partner is entitled to receive cash in the amount equal to the fair value of the Company s common stock on or about the date of redemption. In lieu of cash redemption, the Company may elect to exchange such units for an equal number of shares in the Company s common stock. The limited partnership units in DownREITs are valued using the market price of the Company s common stock, a Level 1 price under the fair value hierarchy. At December 31, 2010, the fair value of the DownREIT units was $1,721,000. At September 30, 2011, the fair value of the DownREIT units was $879,000.

Financial Instruments Not Carried at Fair Value

Cash and Cash Equivalents

Cash and cash equivalent balances are held with various financial institutions within principal protected accounts. The Company monitors credit ratings of these financial institutions and the concentration of cash and cash equivalent balances with any one financial institution and believes the likelihood of realizing material losses related to cash and cash equivalent balances is remote. Cash and cash equivalents are carried at their face amounts, which reasonably approximate their fair values.

Other Financial Instruments

Rents receivable, accounts and construction payable and accrued expenses and other liabilities are carried at their face amounts, which reasonably approximate their fair values.

The Company values its bond indebtedness, notes payable and outstanding amounts under the Credit Facility using a discounted cash flow analysis on the expected cash flows of each instrument. This analysis reflects the contractual terms of the instrument, including the period to maturity, and uses observable market-based inputs, including interest rate curves. The process also considers credit valuation adjustments to appropriately reflect the Company s nonperformance risk. The Company has concluded that the value of its bond indebtedness and notes payable are Level 2 prices as the majority of the inputs used to value its positions fall within Level 2 of the fair value hierarchy. Bond indebtedness, notes payable and outstanding amounts under the New Credit Facility (as applicable) with an aggregate outstanding par amount of approximately $3,785,830,000 had an estimated aggregate fair value of $3,946,337,000 at September 30, 2011. Bond indebtedness, notes payable and outstanding amounts under the Cancelled Credit Facility (as applicable) with an aggregate outstanding par amount of $4,068,417,000 had an estimated aggregate fair value of $4,236,216,000 at December 31, 2010.

12. Subsequent Events

The Company has evaluated subsequent events through the date on which this Form 10-Q was filed, the date on which these financial statements were issued, and identified the following for disclosure.

In October 2011, the Company repaid $54,584,000 in secured debt with an all-in fixed rate of 6.10%, in advance of its scheduled maturity. As part of this transaction, the Company incurred a prepayment penalty of $1,092,000, which will be recognized in the fourth quarter of 2011 as a loss on early retirement of debt.

Also in October 2011, Fund II acquired Highlands at Rancho San Diego, a garden-style community consisting of 676 apartment homes located in San Diego, CA. The community was acquired for a purchase price of $124,000,000. In conjunction with the acquisition, Fund II is extinguishing an outstanding mortgage note secured by the community, incurring a prepayment penalty. The Company s proportionate share of the prepayment penalty is approximately $950,000, which will be recognized in the fourth quarter of 2011 as a component of equity in income (loss) of unconsolidated entities.

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ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Management s Discussion and Analysis of Financial Condition and Results of Operations (MD&A) is intended to help provide an understanding of our business and results of operations. This MD&A should be read in conjunction with our Condensed Consolidated Financial Statements and the accompanying Notes to Condensed Consolidated Financial Statements included elsewhere in this report. This report, including the following MD&A, contains forward-looking statements regarding future events or trends as described more fully under Forward-Looking Statements included in this report. Actual results or developments could differ materially from those projected in such statements as a result of the factors described under Forward-Looking Statements below and the risk factors described in Item 1a, Risk Factors, of our Form 10-K for the year ended December 31, 2010 (our Form 10-K).

All capitalized terms have the meaning as provided elsewhere in this Form 10-Q.

Executive Overview

Business Description

We are primarily engaged in developing, acquiring, owning and operating apartment communities in high barrier to entry markets of the United States. We believe that apartment communities are an attractive long-term investment opportunity compared to other real estate investments because a broad potential resident base should help reduce demand volatility over a real estate cycle. We seek to create long-term shareholder value by accessing capital at cost effective terms; deploying that capital to develop, redevelop and acquire apartment communities in high barrier to entry markets; operating apartment communities; and selling communities when they no longer meet our long-term investment strategy or when pricing is attractive. Barriers to entry in our markets generally include a difficult and lengthy entitlement process with local jurisdictions and dense urban or suburban areas where zoned and entitled land is in limited supply.

We regularly evaluate the allocation of our investments by the amount of invested capital and by product type within our individual markets, which are located in New England, the New York/New Jersey metro area, the Mid-Atlantic, the Midwest, the Pacific Northwest, and the Northern and Southern California regions of the United States. Our strategy is to be leaders in market research and capital allocation, delivering a range of multifamily offerings tailored to serve the needs of the most attractive customer segments in the best-performing submarkets of the United States. Our communities are predominately upscale, which generally command among the highest rents in their markets. However, we also pursue the ownership and operation of apartment communities that target a variety of customer segments and price points, consistent with our goal of offering a broad range of products and services.

Third Quarter 2011 Highlights

- Net income attributable to common stockholders for the quarter ended September 30, 2011 was $44,824,000, an increase of $20,170,000 or 81.8% from the prior year period. The increase is attributable primarily to an increase in NOI from both Established and newly stabilized communities.

- For the quarter ended September 30, 2011, Established Communities NOI increased by $10,230,000 or 9.3% over the prior year period. This year-over-year increase was driven by an increase in rental revenue of 5.8% and a decrease in operating expenses of 0.9% as compared to the prior year period.

- We sold 5,865,000 shares of our common stock at a net price of $128.25 per share before offering costs, in a public offering for net proceeds of approximately $725,850,000.

- At September 30, 2011, we had approximately $759,027,000 in unrestricted cash and cash in escrow.

Financial Outlook

Our portfolio results for the quarter ended September 30, 2011 reflect both year-over-year revenue growth, as well as continued sequential rental revenue growth. The increase in revenues was driven by our portfolio growth and leasing activity for new development as well as an increase in rental rates for our Established Communities. We expect year-over-year revenue growth to continue for the balance of 2011. We believe that the

improvement in fundamentals in the multifamily sector is supported by a

combination of a decline in the homeownership rate, disproportionately greater employment growth in the population segments with the highest propensity to rent and limited supply of new multifamily rental product. We expect revenue growth and favorable operating fundamentals will continue to be driven by home ownership trends, demographic trends, as well as the timing and magnitude of employment growth. We believe continued favorable apartment fundamentals, combined with a capital markets environment that provides for cost effective access to capital, supports our expanded investment activity as further discussed below.

During the quarter ended September 30, 2011, we acquired six land parcels for an aggregate purchase price of approximately $65,270,000 for the development of 1,740 apartment homes with an expected total capitalized cost of $374,650,000. We started or anticipate starting construction within the next three to six months on all six of these land parcels. In addition, we started construction of four communities containing 921 apartment homes that we expect to complete for an aggregate total capitalized cost of $210,100,000. At September 30, 2011, 15 communities were under construction with a total projected capitalized cost of approximately $990,300,000. As of September 30, 2011, approximately $465,900,000 of the capital for this development was invested, with $524,361,000 remaining to invest. At September 30, 2011 our combined development under way and in planning currently is $3,552,300,000, providing us the ability to deliver assets into expected favorable market conditions in 2012 and 2013.

During the three months ended September 30, 2011, we started the redevelopment of three communities: Avalon Foster City, located in Foster City, CA, Avalon at Ballston Washington Towers, located in Arlington, VA, and Avalon Santa Margarita, located in Rancho Santa Margarita, CA. These communities contain 933 apartment homes and will be redeveloped for an estimated total capitalized cost of $28,400,000, excluding costs incurred prior to redevelopment. At September 30, 2011, there were eight communities under redevelopment, with an expected investment of approximately $89,000,000, excluding costs incurred prior to the start of redevelopment, with $47,907,000 remaining to be invested**.**

We expect to increase our redevelopment activity through the end of 2011 and into 2012, taking the opportunity to reinvest and reposition our assets to meet the needs of our residents and to try to position our assets to outperform as the economy fully recovers.

At present, cash on hand and available capital from our New Credit Facility are sufficient to provide the capital necessary to fund our development and redevelopment activities for the balance of 2011. We believe that the strength of our balance sheet, as measured by our current level of indebtedness, our current ability to service interest and other fixed charges and our current limited use of financial encumbrances (such as secured financing), provides adequate access to liquidity from the capital markets through the issuance of corporate securities (which could include unsecured debt and/or common and preferred equity) and secured debt, as well as other sources of liquidity such as from joint ventures or from our retained cash, to meet any reasonably foreseeable liquidity needs as they arise. See the discussion under *Liquidity and Capital Resources*.

While we continue to grow principally through our demonstrated core competency of developing wholly owned assets, we also acquire interests in additional operating assets, either directly by us or through our investment in Fund II, a discretionary real estate investment fund.

We established Fund I and Fund II (collectively the Funds) to engage in acquisition programs through discretionary investment funds. We believe this investment format provides the following attributes: (i) third-party joint venture equity as an additional source of financing to expand and diversify our portfolio; (ii) additional sources of income in the form of property management and asset management fees and, potentially, incentive distributions if the performance of the Funds exceeds certain thresholds; and (iii) visibility into the transactions occurring in multi-family assets that helps us with other investment decisions related to our wholly-owned portfolio.

Fund I has nine institutional investors, including us. One of our wholly owned subsidiaries is the general partner of Fund I and we have made an equity investment of approximately $44,000,000 in Fund I (net of distributions and excluding the purchase by us of a mortgage note secured by a Fund I community), representing a 15.15% combined general partner and limited partner equity interest. Fund I was our principal vehicle for acquiring apartment communities through the close of its investment period in March 2008. Fund I has a term that expires in March 2015, plus two one-year extension options. Subsidiaries of Fund I have 20 loans, including one held by us, as discussed elsewhere in this Form 10-Q, secured by individual assets with amounts outstanding in the aggregate of $412,480,000 with varying maturity dates (or dates after which the loans can be prepaid without penalty), ranging from March 2012 to September 2016. These mortgage loans are secured by the underlying real estate.

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During the three months ended September 30, 2011, Fund I sold Avalon Redondo Beach, located in Redondo Beach, CA. This community contains 105 apartment homes and was sold for $33,100,000. This disposition resulted in a gain in accordance with GAAP of $12,445,000. Our share of the gain in accordance with GAAP was approximately $1,743,000.

Fund II has six institutional investors, including us. One of our wholly owned subsidiaries is the general partner of Fund II and we have total equity commitments of $125,000,000, representing a 31.25% combined general partner and limited partner equity interest. Fund II has a term that expires in August 2018, plus two one-year extension options. Fund II served as the exclusive vehicle, with some exceptions, through which we acquired investment interests in apartment communities until August 2011. We will receive, in addition to any returns on our invested equity, asset management fees, property management fees and redevelopment fees. We will also receive a promoted interest if certain return thresholds are met.

During the three months ended September 30, 2011, a subsidiary of Fund II acquired Captain Parker Arms, a garden-style community consisting of 94 apartment homes located in Lexington, MA. Captain Parker Arms was acquired for a purchase price of $20,850,000. In October 2011, a subsidiary of Fund II acquired Highlands at Rancho San Diego, consisting of 676 apartment homes located in San Diego, CA for a purchase price of $124,000,000. In conjunction with the acquisition, Fund II is extinguishing an outstanding mortgage note secured by the community, incurring a prepayment penalty, of which our proportionate share is approximately $950,000. While the investment period for Fund II closed in August 2011, we may acquire interests in additional apartment communities through Fund II related to active acquisition candidates identified prior to the close of the investment period.

At September 30, 2011, subsidiaries of Fund II have 11 loans secured by individual assets with amounts outstanding in the aggregate of $378,083,000 with varying maturity dates (or dates after which the loans can be prepaid without penalty), ranging from November 2014 to September 2019. These mortgage loans are secured by the underlying real estate.

Communities Overview

Our real estate investments consist primarily of current operating apartment communities, communities in various stages of development (Development Communities) and Development Rights as defined below. Our current operating communities are further distinguished as Established Communities, Other Stabilized Communities, Lease-Up Communities and Redevelopment Communities. The following is a description of each category:

Current Communities are categorized as Established, Other Stabilized, Lease-Up, or Redevelopment according to the following attributes:

Established Communities (also known as Same Store Communities) are consolidated communities where a comparison of operating results from the prior year to the current year is meaningful, as these communities were owned and had stabilized occupancy and operating expenses as of the beginning of the prior year. For the period ended September 30, 2011, the Established Communities are communities that are consolidated for financial reporting purposes, had stabilized occupancy and operating expenses as of January 1, 2010, are not conducting or planning to conduct substantial redevelopment activities and are not held for sale or planned for disposition within the current year. A community is considered to have stabilized occupancy at the earlier of (i) attainment of 95% physical occupancy or (ii) the one-year anniversary of completion of development or redevelopment.

Other Stabilized Communities are all other completed communities that we own or have a direct or indirect ownership interest in, and that have stabilized occupancy, as defined above. Other Stabilized Communities do not include communities that are conducting or planning to conduct substantial redevelopment activities within the current year.

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Lease-Up Communities are communities where construction has been complete for less than one year and where physical occupancy has not reached 95%.

Redevelopment Communities are communities where substantial redevelopment is in progress or is planned to begin during the current year. Redevelopment is considered substantial when capital invested during the reconstruction effort is expected to exceed either $5,000,000 or 10% of the community s pre-redevelopment basis and is expected to have a material impact on the operations of the community, including occupancy levels and future rental rates.

Development Communities are communities that are under construction and for which a certificate of occupancy has not been received. These communities may be partially or fully complete and operating.

Development Rights are development opportunities in the early phase of the development process for which we either have an option to acquire land or enter into a leasehold interest, for which we are the buyer under a long-term conditional contract to purchase land or where we control the land through a ground lease or own land to develop a new community. We capitalize related pre-development costs incurred in pursuit of new developments for which we currently believe future development is probable.

We currently lease our corporate headquarters located in Arlington, Virginia under an operating lease. The lease term ends in 2020, subject to two five year renewal options. All other regional and administrative offices are leased under operating leases.

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As of September 30, 2011, communities that we owned or held a direct or indirect interest in were classified as follows:

	Number of communities	Number of apartment homes
Current Communities		
Established Communities:		
New England	30	7,315
Metro NY/NJ	22	6,981
Mid-Atlantic/Midwest	16	5,950
Pacific Northwest	10	2,533
Northern California	15	4,829
Southern California	15	4,003
Total Established	108	31,611
Other Stabilized Communities:		
New England	7	1,608
Metro NY/NJ	11	3,945
Mid-Atlantic/Midwest	14	4,675
Pacific Northwest	3	828
Northern California	13	3,552
Southern California	18	5,258
Total Other Stabilized	66	19,866
Lease-Up Communities	3	273
Redevelopment Communities (1)	7	2,076
Total Current Communities	184	53,826
Development Communities	15	3,600
Development Rights	29	8,679

(1) The Company commenced the redevelopment of Avalon at Santa Margarita during the third quarter of 2011, however at September 30, 2011, the redevelopment activity is focused on the common area and is not impacting community operations, including occupancy or rental revenue. The community is therefore included in the Established Community portfolio.

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Results of Operations

Our year-over-year operating performance is primarily affected by both overall and individual geographic market conditions and apartment fundamentals and is reflected in changes in NOI of our Established Communities; NOI derived from acquisitions and development completions; the loss of NOI related to disposed communities; and capital market and financing activity. A comparison of our operating results for the three and nine months ended September 30, 2011 and 2010 follows (dollars in thousands):

	For the three months ended				For the nine months ended			
	9-30-11	9-30-10	$ Change	% Change	9-30-11	9-30-10	$ Change	% Change
Revenue:								
Rental and other income	$ 248,644	$ 223,758	$ 24,886	11.1%	$ 720,535	$ 652,000	$ 68,535	10.5%
Management, development and other fees	2,433	1,800	633	35.2%	7,085	5,334	1,751	32.8%
Total revenue	251,077	225,558	25,519	11.3%	727,620	657,334	70,286	10.7%
Expenses:								
Direct property operating expenses, excluding property taxes	57,894	55,835	2,059	3.7%	164,352	158,789	5,563	3.5%
Property taxes	24,535	23,225	1,310	5.6%	73,238	69,191	4,047	5.8%
Total community operating expenses	82,429	79,060	3,369	4.3%	237,590	227,980	9,610	4.2%
Corporate-level property management and other indirect operating expenses	10,162	8,971	1,191	13.3%	29,553	27,287	2,266	8.3%
Investments and investment management expense	1,328	1,026	302	29.4%	3,860	3,111	749	24.1%
Expensed acquisition, development and other pursuit costs	633	737	(104)	(14.1)%	2,636	1,685	951	56.4%
Interest expense, net	43,970	44,262	(292)	(0.7)%	134,096	128,260	5,836	4.6%
Depreciation expense	62,262	57,926	4,336	7.5%	185,071	169,819	15,252	9.0%
General and administrative expense	6,087	7,039	(952)	(13.5)%	21,524	19,975	1,549	7.8%
Impairment loss	14,052		14,052	N/A	14,052		14,052	N/A
Gain on sale of land	(13,716)		(13,716)	N/A	(13,716)		(13,716)	N/A
Total other expenses	124,778	119,961	4,817	4.0%	377,076	350,137	26,939	7.7%
Equity in income (loss) of unconsolidated entities	2,615	(325)	2,940	(904.6)%	3,513	364	3,149	865.1%
Income from continuing operations	46,485	26,212	20,273	77.3%	116,467	79,581	36,886	46.4%
Discontinued operations:								
Loss from discontinued operations	(1,808)	(2,232)	424	(19.0)%	(5,737)	(4,387)	(1,350)	30.8%
Gain on sale of communities								