

DUKE REALTY CORP  
Form 10-K  
February 29, 2008

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-K**

(Mark One)

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

For the fiscal year ended **December 31, 2007**

**OR**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE**

**SECURITIES EXCHANGE ACT OF 1934**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_ .

Commission File Number: 1-9044

**DUKE REALTY CORPORATION**

(Exact Name of Registrant as Specified in Its Charter)

**Indiana**

(State or Other Jurisdiction  
of Incorporation or Organization)  
**600 East 96<sup>th</sup> Street, Suite 100**

**35-1740409**

(IRS Employer  
Identification Number)

**46240**

**Indianapolis, Indiana**

(Address of Principal Executive Offices)

(Zip Code)

**Registrant's telephone number, including area code: (317) 808-6000**

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

**Title of Each Class:**

Common Stock (\$.01 par value)  
Depositary Shares, each representing a 1/10 interest in a 6.625%  
Series J Cumulative Redeemable Preferred Share (\$.01 par value)  
Depositary Shares, each representing a 1/10 interest in a 6.5%  
Series K Cumulative Redeemable Preferred Share (\$.01 par value)  
Depositary Shares, each representing a 1/10 interest in a 6.6%  
Series L Cumulative Redeemable Preferred Share (\$.01 par value)  
Depositary Shares, each representing 1/10 interest in a 6.95%

**Name of Each Exchange on Which Registered:**

New York Stock Exchange  
New York Stock Exchange  
New York Stock Exchange  
New York Stock Exchange

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Series M Cumulative Redeemable Preferred Share (\$.01 par value) Depository Shares, each representing 1/10 interest in a 7.25%	New York Stock Exchange
Series N Cumulative Redeemable Preferred Share (\$.01 par value) Depository Shares, each representing a 1/10 interest in an 8.375%	New York Stock Exchange
Series O Cumulative Redeemable Preferred Share (\$.01 par value)	New York Stock Exchange

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

Indicate by check mark whether the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

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

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

The aggregate market value of the voting shares of the registrant's outstanding common shares held by non-affiliates of the registrant is \$4.9 billion based on the last reported sale price on June 30, 2007.

The number of common shares, \$.01 par value outstanding as of February 20, 2008 was 146,303,272.

### DOCUMENTS INCORPORATED BY REFERENCE

Certain portions of Duke Realty Corporation's Definitive Proxy Statement for its 2008 Annual Meeting of Shareholders (the "Proxy Statement") to be filed pursuant to Rule 14a-6 of the Securities Exchange Act of 1934, as amended, are incorporated by reference into this Form 10-K. Other than those portions of the Proxy Statement specifically incorporated by reference pursuant to Items 10 through 14 of Part III hereof, no other portions of the Proxy Statement shall be deemed so incorporated.



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**Cautionary Statement Regarding Forward-Looking Statements**

Certain statements contained in or incorporated by reference into this Report, including, without limitation, those related to our future operations, constitute forward-looking statements within the meaning of Section 27A of the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended. The words believe, estimate, expect, anticipate, intend, plan, seek, may and similar expressions in statements regarding future periods are intended to identify forward-looking statements.

These forward-looking statements involve known and unknown risks, uncertainties and other important factors that could cause our actual results, performance or achievements, or industry results, to differ materially from any predictions of future results, performance or achievements that we express or imply in this Report or in the information incorporated by reference into this Report. Some of the risks, uncertainties and other important factors that may affect future results include, among others:

- Changes in general economic and business conditions, including performance of financial markets;
- Our continued qualification as a real estate investment trust, or REIT, for U.S. federal income tax purposes;
- Heightened competition for tenants and potential decreases in property occupancy;
- Potential increases in real estate construction costs;
- Potential changes in the financial markets and interest rates;
- Volatility in our stock price and trading volume;
- Our continuing ability to raise funds on favorable terms through the issuance of debt and equity in the capital markets;
- Our ability to successfully identify, acquire, develop and/or manage properties on terms that are favorable to us;

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- Our ability to be flexible in the development and operation of joint venture properties;
- Our ability to successfully dispose of properties on terms that are favorable to us;
- Inherent risks in the real estate business, including, but not limited to, tenant defaults, potential liability relating to environmental matters and liquidity of real estate investments; and
- Other risks and uncertainties described herein, as well as, those risks and uncertainties discussed from time to time in our other reports and other public filings with the Securities and Exchange Commission ( SEC ).

This list of risks and uncertainties, however, is only a summary of some of the most important factors and is not intended to be exhaustive. Additional information regarding risk factors that may affect us is included under the caption **Risk Factors** in this Report, and is updated by us from time to time in Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and other filings that we make with the SEC.

Although we presently believe that the plans, expectations and results expressed in or suggested by the forward-looking statements are reasonable, all forward-looking statements are inherently subjective, uncertain and subject to change, as they involve substantial risks and uncertainties beyond our control. New factors emerge from time to time, and it is not possible for us to predict the nature, or assess the potential impact, of each new factor on our business. Given these uncertainties, we caution you not to place undue reliance on these forward-looking statements. We undertake no obligation to update or revise any of our forward-looking statements for events or circumstances that arise after the statement is made, except as otherwise may be required by law.

## PART I

### Item 1. Business

#### Background

We are a self-administered and self-managed real estate investment trust ( REIT ), which began operations upon completion of our initial public offering in February 1986. In October 1993, we completed an additional common shares offering and acquired the rental real estate and service businesses of Duke Associates, whose operations began in 1972. As of December 31, 2007, our diversified portfolio of 726 rental properties (including 38 properties comprising 10.0 million square feet under development) encompass more than 121.1 million rentable square feet and are leased by a diverse and stable base of more than 3,400 tenants whose businesses include manufacturing, retailing, wholesale trade, distribution, healthcare and professional services. We also own or control approximately 7,700 acres of unencumbered land ready for development.

Through our Service Operations, we provide, on a fee basis, leasing, property and asset management, development, construction, build-to-suit and other tenant-related services. See Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations and Item 8, Financial Statements and Supplementary Data for financial information. Our Rental Operations are conducted through Duke Realty Limited Partnership ( DRLP ). In addition, we conduct our Service Operations through Duke Realty Services LLC, Duke Realty Services Limited Partnership and Duke Construction Limited Partnership. In this Form 10-K Report, the terms we, us and our refer to Duke Realty Corporation and subsidiaries (the Company ) and those entities owned or controlled by the Company.

Our headquarters and executive offices are located in Indianapolis, Indiana. In addition, we have 21 regional offices located in Alexandria, Virginia; Atlanta, Georgia; Austin, Texas; Baltimore, Maryland; Cincinnati, Ohio; Columbus, Ohio; Chicago, Illinois; Dallas, Texas; Houston, Texas; Minneapolis, Minnesota; Nashville, Tennessee; Newport Beach, California; Orlando, Florida; Phoenix, Arizona; Raleigh, North Carolina; St. Louis, Missouri; San Antonio, Texas; Savannah, Georgia; Seattle, Washington; Tampa, Florida; and Weston, Florida. We had approximately 1,400 employees as of December 31, 2007.

#### Business Strategy

One of our primary business objectives is to increase Funds From Operations ( FFO ) by (i) maintaining and increasing property occupancy and rental rates through the management of our portfolio of existing properties; (ii) developing and acquiring new properties for our Rental Operations in our existing markets; (iii) expanding geographically by acquiring and developing properties in new markets; (iv) using our construction expertise to act as a general contractor in our existing markets and other domestic markets on a fee basis; (v) developing and repositioning properties in our existing markets and other markets which we will sell through our Service Operations property sale program and (vi) providing a full line of real estate services to our tenants and to third parties. FFO is used by industry analysts and investors as a supplemental operating performance measure of an equity REIT like Duke. FFO is calculated in accordance with the definition that was adopted by the Board of Governors of the National Association of Real Estate Investment Trusts ( NAREIT ). NAREIT created FFO as a supplemental measure of REIT operating performance that excludes historical cost depreciation, among other items, from net income determined in accordance with United States generally accepted accounting principles ( GAAP ). FFO is a non-GAAP financial measure developed by NAREIT to compare the operating performance of REITs. The most comparable GAAP measure is net income (loss). FFO should not be considered as a substitute for net income or any other measures derived in accordance with GAAP and may not be comparable to other similarly

titled measures of other companies.

Historical cost accounting for real estate assets in accordance with GAAP implicitly assumes that the value of real estate assets diminishes predictably over time. Since real estate values instead have historically risen or fallen with market conditions, many industry analysts and investors have considered presentation of operating results for real estate companies that use historical cost accounting to be insufficient by



themselves. FFO, as defined by NAREIT, represents GAAP net income (loss), excluding extraordinary items as defined under GAAP and gains or losses from sales of previously depreciated real estate assets, plus certain non-cash items such as real estate asset depreciation and amortization, and after similar adjustments for unconsolidated partnerships and joint ventures.

Management believes that the use of FFO, combined with the required primary GAAP presentations, improves the understanding of operating results of REITs among the investing public and makes comparisons of REIT operating results more meaningful. Management believes FFO is a useful measure for reviewing comparative operating and financial performance (although FFO should be reviewed in conjunction with net income which remains the primary measure of performance) because by excluding gains or losses related to sales of previously depreciated real estate assets and excluding real estate asset depreciation and amortization, FFO provides a useful comparison of the operating performance of our real estate between periods or as compared to different companies.

As a fully integrated commercial real estate firm, we provide in-house leasing, management, development and construction services which, coupled with our significant base of commercially zoned and unencumbered land in existing business parks, should give us a competitive advantage both as a real estate operator and in future development activities.

We believe that the management of real estate opportunities and risks can be done most effectively at regional or local levels. As a result, we intend to continue our emphasis on increasing our market share and effective rents in the primary markets where we own properties. We also expect to utilize approximately 7,700 acres of unencumbered land and our many business relationships with our more than 3,400 commercial tenants to expand our build-to-suit business (development projects substantially pre-leased to a single tenant) and to pursue other development and acquisition opportunities in our primary markets. We believe that this regional focus will allow us to assess market supply and demand for real estate more effectively as well as to capitalize on the strong relationships with our tenant base. In addition, we seek to further capitalize on strong customer relationships to provide third-party construction and build-for-sale services outside our primary markets and to expand into high growth and seaport markets across the United States.

Our strategy is to seek to develop and acquire primarily Class A commercial properties located in markets with high growth potential for large national and international companies and other quality regional and local firms. Our industrial and suburban office development focuses on business parks and mixed-use developments suitable for multiple projects on a single site where we can create and control the business environment. These business parks and mixed-use developments often include restaurants and other amenities, which we believe will create an atmosphere that is particularly efficient and desirable. As a fully integrated real estate company, we are able to arrange for or provide to our industrial, office and healthcare customers not only well located and well maintained facilities, but also additional services such as build-to-suit construction, tenant finish construction, and expansion flexibility.

All of our properties are located in areas that include competitive properties. Institutional investors, other REITs or local real estate operators generally own such properties; however, no single competitor or small group of competitors is dominant in our current markets. The supply and demand of similar available rental properties may affect the rental rates we will receive on our properties.

## **Financing Strategy**

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We seek to maintain a well-balanced, conservative and flexible capital structure by: (i) extending and sequencing the maturity dates of debt; (ii) borrowing primarily at fixed rates by targeting a variable rate component of total debt less than 20%; (iii) pursuing current and future long-term debt financings and refinancing on an unsecured basis; (iv) maintaining conservative debt service and fixed charge coverage ratios; (v) generating proceeds from the sale of non-strategic properties and (vi) issuing perpetual preferred stock for 5-10% of our total capital structure.

Management believes that these strategies have enabled and should continue to enable us to favorably access capital markets for our long-term requirements such as debt refinancing and financing development and acquisitions of additional rental properties. In addition, as discussed under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, we have a \$1.3 billion unsecured line of credit available for short-term funding of development and acquisition of additional rental properties. Further, we pursue favorable opportunities to dispose of assets that no longer meet our long-term investment criteria and recycle the proceeds into new investments that we believe have excellent long-term growth prospects. Our debt to total market capitalization ratio (total market capitalization is defined as the total market value of all outstanding common and preferred shares and units of limited partnership interest ( Units ) in DRLP plus outstanding indebtedness) at December 31, 2007 was 48.4%. Our ratio of earnings to debt service and ratio of earnings to fixed charges for the year ended December 31, 2007 were 1.58x and 1.47x, respectively. In computing the ratio of earnings to debt service, earnings have been calculated by adding interest expense (excluding amortization of debt issuance costs) to income from continuing operations, less preferred dividends, and minority interest in earnings of DRLP. Debt service consists of interest expense and recurring principal amortization (excluding maturities) and excludes amortization of debt issuance costs. In computing the ratio of earnings to fixed charges, earnings have been calculated by adding interest expense and minority interest in earnings from DRLP to income from continuing operations. Fixed charges consist of interest costs, whether expensed or capitalized, the interest component of rental expense and amortization of debt issuance costs.

## Corporate Governance

Since our inception, we not only have strived to be a top-performer operationally, but also to lead in issues important to investors such as disclosure and corporate governance. Our system of governance reinforces this commitment. Summarized below are the highlights of our Corporate Governance initiatives.

- |                          |   |
|--------------------------|---|
| <b>Board Composition</b> | <ul style="list-style-type: none"> <li>• Board is controlled by supermajority (91.7%) of Independent Directors as of January 30, 2008 and thereafter</li> </ul>   |
| <b>Board Committees</b>  | <ul style="list-style-type: none"> <li>• Board Committee members are all Independent Directors</li> </ul>   |
| <b>Lead Director</b>     | <ul style="list-style-type: none"> <li>• The Chairman of the Corporate Governance Committee serves as Lead Director of the Independent Directors</li> </ul>   |
| <b>Board Policies</b>    | <ul style="list-style-type: none"> <li>• No Shareholder Rights Plan (Poison Pill)</li> <li>• Code of Conduct applies to all Directors and employees, including the Chief Executive Officer and senior financial officers; waivers require the vote of Independent Directors</li> <li>• Effective orientation program for new Directors</li> <li>• Independence of Directors is reviewed annually</li> <li>• Independent Directors meet at least quarterly in executive session</li> <li>• Independent Directors receive no compensation from Duke other than as Directors</li> <li>• Equity-based compensation plans require shareholder approval</li> <li>• Board effectiveness and performance is reviewed annually by the Corporate Governance Committee</li> <li>• Corporate Governance Committee conducts an annual review of the Chief Executive Officer succession plan</li> <li>• Independent Directors and all Board Committees may retain outside advisors, as they deem appropriate</li> <li>• Policy governing retirement age for Directors</li> <li>• Outstanding stock options may not be repriced</li> <li>• Directors required to offer resignation upon job change</li> <li>• Majority voting for election of Directors</li> </ul> |

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### **Ownership**

Minimum Stock Ownership Guidelines apply to all Directors and Executive Officers

Our Code of Conduct (which applies to all Directors and employees, including the Chief Executive Officer and senior financial officers) and the Corporate Governance Guidelines are available in the investor information/corporate governance section of our website at [www.dukerealty.com](http://www.dukerealty.com). A copy of these documents may also be obtained without charge by writing to Duke Realty Corporation, 600 East 96th Street, Suite 100, Indianapolis, Indiana 46240, Attention: Investor Relations.

### **Additional Information**

For additional information regarding our investments and operations, see Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, and Item 8, Financial Statements and Supplementary Data. For additional information about our business segments, see Item 8, Financial Statements and Supplementary Data.

### **Available Information and Exchange Certifications**

In addition to this Annual Report, we file quarterly and special reports, proxy statements and other information with the Securities and Exchange Commission (the SEC). All documents that are filed with the SEC are available free of charge on our corporate website, which is [www.dukerealty.com](http://www.dukerealty.com). You may also read and copy any document filed at the public reference facilities of the SEC at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at (800) SEC-0330 for further information about the public reference facilities. These documents also may be accessed through the SEC's electronic data gathering, analysis and retrieval system (EDGAR) via electronic means, including the SEC's home page on the Internet (<http://www.sec.gov>). In addition, since some of our securities are listed on the New York Stock Exchange, you may read SEC filings at the offices of the New York Stock Exchange, 20 Broad Street, New York, New York 10005.

The New York Stock Exchange (NYSE) requires that the Chief Executive Officer of each listed company certify annually to the NYSE that he or she is not aware of any violation by the company of NYSE corporate governance listing standards as of the date of such certification. We submitted the certification of our Chairman and Chief Executive Officer, Dennis D. Oklak, with our 2007 Annual Written Affirmation to the NYSE on May 16, 2007.

We included the certifications of the Chief Executive Officer and the Chief Financial Officer of the Company required by Section 302 of the Sarbanes-Oxley Act of 2002 and related rules, relating to the quality of the Company's public disclosure, in this report as Exhibits 31.1 and 31.2.

### **Item 1A. Risk Factors**

In addition to the other information contained in this Report, you should carefully consider, in consultation with your legal, financial and other professional advisors, the risks described below, as well as the risk factors and uncertainties discussed in our other public filings with the SEC under the caption Risk Factors in evaluating us and our business before making a decision regarding an investment in our securities.

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The risks contained in this Report are not the only risks faced by us. Additional risks that are not presently known, or that we presently deem to be immaterial, also could have a material adverse effect on our financial condition, results of operations, business and prospects. The trading price of our securities could decline due to the materialization of any of these risks, and our shareholders may lose all or part of their investment.

This Report also contains forward-looking statements that may not be realized as a result of certain factors, including, but not limited to, the risks described herein and in our other public filings with the SEC. Please refer to the section in this Report entitled "Cautionary Notice Regarding Forward-Looking Statements" for additional information regarding forward-looking statements.

**If we were to cease to qualify as a REIT, we and our shareholders would lose significant tax benefits.**

We intend to continue to operate so as to qualify as a REIT under the Internal Revenue Code of 1986, as amended (the "Code"). Qualification as a REIT provides significant tax advantages to us and our shareholders. However, in order for us to continue to qualify as a REIT, we must satisfy numerous requirements established under highly technical and complex Code provisions for which there are only limited judicial and administrative interpretations. Satisfaction of these requirements also depends on various factual circumstances not entirely within our control. The fact that we hold our assets through an operating partnership and its subsidiaries further complicates the application of the REIT requirements. Even a technical or inadvertent mistake could jeopardize our REIT status. Although we believe that we can continue to operate so as to qualify as a REIT, we cannot offer any assurance that we can continue to do so or that legislation, new regulations, administrative interpretations or court decisions will not significantly change the qualification requirements or the federal income tax consequences of qualification. If we were to fail to qualify as a REIT in any taxable year, it would have the following effects:

- We would not be allowed a deduction for distributions to shareholders and would be subject to federal income tax (including any applicable alternative minimum tax) on our taxable income at regular corporate rates;
- Unless we were entitled to relief under certain statutory provisions, we would be disqualified from treatment as a REIT for the four taxable years following the year during which we ceased to qualify as a REIT;
- Our net earnings available for investment or distribution to our shareholders would decrease due to the additional tax liability for the year or years involved; and
- We would no longer be required to make any distributions to shareholders in order to qualify as a REIT.

As such, failure to qualify as a REIT would likely have a significant adverse effect on the value of our securities.

**REIT distribution requirements limit the amount of cash we will have available for other business purposes, including amounts that we need to fund our future growth.**

To maintain our qualification as a REIT under the Code, we must annually distribute to our shareholders at least 90% of our ordinary taxable income, excluding net capital gains. We intend to continue to make distributions to our shareholders to comply with the 90% distribution requirement. However, this requirement limits our ability to accumulate capital for use for other business purposes. If we do not have sufficient cash or other liquid assets to meet the distribution requirements, we may have to borrow funds or sell properties on adverse terms in order to

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meet the distribution requirements. If we fail to make a required distribution, we would cease to qualify as a REIT.

### **U.S. federal income tax developments could affect the desirability of investing in us for individual taxpayers.**

In May 2003, federal legislation was enacted that reduced the maximum tax rate for dividends payable to individual taxpayers generally from 38.6% to 15% (from January 1, 2003 through 2008). However, dividends payable by REITs are not eligible for this treatment, except in limited circumstances. Although

this legislation did not have a direct adverse effect on the taxation of REITs or dividends paid by REITs, the more favorable treatment for non-REIT dividends could cause individual investors to consider investments in non-REIT corporations as more attractive relative to an investment in us as a REIT.

**U.S. federal income tax treatment of REITs and investments in REITs may change, which may result in the loss of our tax benefits of operating as a REIT.**

The present U.S. federal income tax treatment of a REIT and an investment in a REIT may be modified by legislative, judicial or administrative action at any time. Revisions in U.S. federal income tax laws and interpretations of these laws could adversely affect us and the tax consequences of an investment in our common shares.

**Our net earnings available for investment or distribution to shareholders could decrease as a result of factors outside of our control.**

Ou