Douglas Emmett Inc
Form 10-Q
August 05, 2010

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 June 30, 2010

Commission file number 001-33106

DOUGLAS EMMETT, INC.
(Exact name of registrant as specified in its charter)

MARYLAND (State or other jurisdiction of incorporation or organization)	20-3073047 (I.R.S. Employer Identification No.)
808 Wilshire Boulevard, Suite 200, Santa Monica, California (Address of principal executive offices)	90401 (Zip Code)

(310) 255-7700
(Registrant’s telephone number, including area code)

None
(Former name, former address and former fiscal year, 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 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 x No o

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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See 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 o
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

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

Class	Outstanding at July 31, 2010
Common Stock, $0.01 par value per share	122,721,371 shares

DOUGLAS EMMETT, INC.
FORM 10-Q
TABLE OF CONTENTS

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Douglas Emmett, Inc.
Consolidated Balance Sheets
(in thousands, except shares and per share data)

	June 30, 2010	December 31, 2009
	(unaudited)	
Assets		
Investment in real estate:		
Land	$ 851,791	$ 835,407
Buildings and improvements	5,222,779	5,017,569
Tenant improvements and lease intangibles	561,893	534,084
Investment in real estate, gross	6,636,463	6,387,060
Less: accumulated depreciation	(799,146)	(688,893)
Investment in real estate, net	5,837,317	5,698,167
Cash and cash equivalents	21,249	72,740
Tenant receivables, net	1,256	2,357
Deferred rent receivables, net	44,803	40,395
Interest rate contracts	71,268	108,027
Acquired lease intangible assets, net	11,592	11,691
Investment in unconsolidated real estate funds	97,364	97,127
Other assets	26,434	29,428
Total assets	$ 6,111,283	$ 6,059,932
Liabilities		
Secured notes payable, including loan premium	$ 3,425,335	$ 3,273,459
Accounts payable and accrued expenses	62,426	72,893
Security deposits	32,338	32,501
Acquired lease intangible liabilities, net	124,859	139,340
Interest rate contracts	174,566	237,194
Dividends payable	12,263	12,160
Total liabilities	3,831,787	3,767,547
Equity		
Douglas Emmett, Inc. stockholders' equity:		
Common Stock, $0.01 par value 750,000,000 authorized, 122,634,628 and 121,596,427 outstanding at June 30, 2010 and December 31, 2009, respectively	1,226	1,216
Additional paid-in capital	2,308,967	2,290,419
Accumulated other comprehensive income (loss)	(158,919)	(186,255)
Accumulated deficit	(353,761)	(312,017)
Total Douglas Emmett, Inc. stockholders' equity	1,797,513	1,793,363
Noncontrolling interests	481,983	499,022

Total equity		2,279,496		2,292,385
Total liabilities and equity	$	6,111,283	$	6,059,932

See notes to consolidated financial statements.

3

Douglas Emmett, Inc.
Consolidated Statements of Operations
(unaudited and in thousands, except shares and per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
Revenues				
Office rental				
Rental revenues	$ 98,695	$ 99,210	$ 197,442	$ 207,756
Tenant recoveries	7,710	7,134	14,188	15,100
Parking and other income	15,838	16,404	31,389	34,038
Total office revenues	122,243	122,748	243,019	256,894
Multifamily rental				
Rental revenues	15,879	16,007	31,778	32,194
Parking and other income	1,087	1,040	2,199	2,124
Total multifamily revenues	16,966	17,047	33,977	34,318
Total revenues	139,209	139,795	276,996	291,212
Operating Expenses				
Office expense	37,198	36,665	73,312	76,977
Multifamily expense	4,434	4,286	9,002	8,803
General and administrative	5,944	5,959	11,794	12,310
Depreciation and amortization	54,921	55,729	110,253	116,803
Total operating expenses	102,497	102,639	204,361	214,893
Operating income	36,712	37,156	72,635	76,319
Gain on disposition of interest in unconsolidated real estate fund	-	-	-	5,573
Other income (loss)	151	60	397	(507)
(Loss) gain, including depreciation, from unconsolidated real estate funds	(2,200)	(2,128)	(3,704)	675
Interest expense	(45,676)	(44,606)	(90,810)	(93,828)
Acquisition-related expenses	(292)	-	(292)	-
Net loss	(11,305)	(9,518)	(21,774)	(11,768)
Less: Net loss attributable to noncontrolling interests	2,314	2,036	4,496	2,419
Net loss attributable to common stockholders	$ (8,991)	$ (7,482)	$ (17,278)	$ (9,349)
Net loss attributable to common stockholders per share – basic	$ (0.07)	$ (0.06)	$ (0.14)	$ (0.08)

Net loss attributable to common stockholders per share – diluted	$ (0.07)	$ (0.06)	$ (0.14)	$ (0.08)
Dividends declared per common share	$ 0.10	$ 0.10	$ 0.20	$ 0.20
Weighted average shares of common stock outstanding – basic	122,331,803	121,319,121	121,989,652	121,579,011
Weighted average shares of common stock outstanding – diluted	122,331,803	121,319,121	121,989,652	121,579,011

See notes to consolidated financial statements.

Douglas Emmett, Inc.
Consolidated Statements of Cash Flows
(unaudited and in thousands)

	Six Months Ended June 30, 2010	2009
Operating Activities		
Net loss	$ (21,774)	$ (11,768)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Loss (Gain), including depreciation, from unconsolidated real estate funds	3,704	(675)
Depreciation and amortization	110,253	116,803
Net accretion of acquired lease intangibles	(13,927)	(17,940)
Gain on disposition of interest in unconsolidated real estate fund	-	(5,573)
Amortization of deferred loan costs	830	1,090
Amortization of loan premium	(2,624)	(2,476)
Non-cash market value adjustments on interest rate contracts	9,454	9,989
Non-cash amortization of stock-based compensation	3,498	2,333
Non-cash profit sharing allocation to consolidated fund	-	660
Change in working capital components:		
Tenant receivables	1,101	580
Deferred rent receivables	(4,408)	(4,425)
Accounts payable and accrued expenses	(4,677)	4,724
Security deposits	(447)	(648)
Other	2,612	2,990
Net cash provided by operating activities	83,595	95,664
Investing Activities		
Capital expenditures and property acquisitions	(252,226)	(21,339)
Deconsolidation of Douglas Emmett Fund X, LLC	-	(6,625)
Investment in unconsolidated real estate funds	(5,681)	-
Net cash used in investing activities	(257,907)	(27,964)
Financing Activities		
Proceeds from long-term borrowings	-	82,640
Deferred loan costs	(105)	(18)
Repayment of borrowings	-	(106,665)
Net change in short-term borrowings	154,500	(25,275)
Contributions by Douglas Emmett Fund X, LLC investors	-	66,074
Contributions by noncontrolling interests	-	450
Distributions to noncontrolling interests	(6,811)	(9,957)
Distributions of capital to noncontrolling interests	(400)	-
Repurchase of common stock	-	(5,338)
Cash dividends	(24,363)	(35,005)
Net cash provided by (used in) financing activities	122,821	(33,094)
(Decrease) Increase in cash and cash equivalents	(51,491)	34,606
Cash and cash equivalents at beginning of period	72,740	8,655

Cash and cash equivalents at end of period	$	21,249	$	43,261
Noncash transactions:				
Investing activity related to contribution of properties to Douglas Emmett Fund X, LLC	$	-	$	476,852
Financing activity related to contribution of debt and noncontrolling interest to Douglas Emmett Fund X, LLC	$	-	$	(483,477)

See notes to consolidated financial statements.

5

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements
(in thousands, except shares and per share data)

1. Overview

Organization and Description of Business
Douglas Emmett, Inc. is a fully integrated, self-administered and self-managed Real Estate Investment Trust (REIT). The terms "us," "we" and "our" as used in these financial statements refer to Douglas Emmett, Inc. and its subsidiaries. Through our interest in Douglas Emmett Properties, LP (our operating partnership) and its subsidiaries, as well as our investment in our unconsolidated real estate funds, we own or partially own, manage, lease, acquire and develop real estate, consisting primarily of office and multifamily properties. As of June 30, 2010, we own a consolidated portfolio of 50 office properties (including ancillary retail space) and nine multifamily properties, as well as the fee interests in two parcels of land subject to ground leases. We also manage six properties owned by our unconsolidated institutional real estate funds as part of our total portfolio, with a combined 56 office properties. All of these properties are located in Los Angeles County, California and Honolulu, Hawaii.

We are one of the largest owners and operators of high-quality office and multifamily properties in Los Angeles County, California and in Honolulu, Hawaii. Our presence in Los Angeles and Honolulu is the result of a consistent and focused strategy of identifying submarkets that are supply constrained, have high barriers to entry and typically exhibit strong economic characteristics such as population and job growth and a diverse economic base. In our office portfolio, we focus primarily on owning and acquiring a substantial share of top-tier office properties within submarkets located near high-end executive housing and key lifestyle amenities. In our multifamily portfolio, we focus primarily on owning and acquiring select properties at premier locations within these same submarkets. Our properties are concentrated in nine premier Los Angeles County submarkets—Brentwood, Olympic Corridor, Century City, Santa Monica, Beverly Hills, Westwood, Sherman Oaks/Encino, Warner Center/Woodland Hills and Burbank—as well as in Honolulu, Hawaii.

Basis of Presentation
The accompanying consolidated financial statements as of June 30, 2010 and December 31, 2009 and for the three and six months ended June 30, 2010 and 2009 are the consolidated financial statements of Douglas Emmett, Inc. and our subsidiaries including our operating partnership. As described in Note 2 below, the results of the six properties we acquired in March 2008 were included in our consolidated results until the end of February 2009, when we completed the transaction to contribute these properties to an unconsolidated institutional real estate fund we manage in return for an equity interest. All significant intercompany balances and transactions have been eliminated in our consolidated financial statements. Certain prior period amounts have been reclassified to conform with current period presentation.

The accompanying unaudited interim financial statements have been prepared pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in the financial statements prepared in accordance with accounting principles generally accepted in the United States (GAAP) may have been condensed or omitted pursuant to SEC rules and regulations, although we believe that the disclosures are adequate to make their presentation not misleading. The accompanying unaudited financial statements include, in our opinion, all adjustments, consisting of normal recurring adjustments, necessary to present fairly the financial information set forth therein. The results of operations for the interim periods are not necessarily indicative of the results that may be expected for the year ended December 31, 2010. The interim financial statements should be read in conjunction with the consolidated financial statements in our 2009 Annual Report on Form 10-K and notes thereto. Any reference to the number of properties and square footage are unaudited and outside the scope of our independent registered public accounting firm's review of our financial statements in accordance with the standards of the United States Public Company Accounting Oversight Board.

The preparation of financial statements in conformity with GAAP requires us to make certain estimates and assumptions, for example with respect to the allocation of the purchase price of acquisitions among land, buildings, improvements, equipment and any related intangible assets and liabilities. These estimates and assumptions are subjective and affect the reported amounts in the consolidated financial statements and accompanying notes. Actual results could differ materially from those estimates.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)
(in thousands, except shares and per share data)

2. Acquisitions, Dispositions and Other Transfers

On June 29, 2010, we acquired Bishop Square, an office project containing approximately 960,000 square feet located in Honolulu, Hawaii for a contract price of $232 million. Bishop Square is the largest office project in the state of Hawaii, and is comprised of two Class A office towers, an above-ground parking structure and a one-acre park.

The results of operations for each of the acquired properties are included in our consolidated statements of operations only from the date of acquisition. We acquired this building near the end of the quarter, and as such, the following table represents our preliminary purchase price allocation. These amounts are likely to change based on a more thorough calculation to be performed during the one-year purchase accounting period provided under the relevant accounting standards. We did not acquire any properties during the first six months of 2009.

	2010 Acquisitions
Investment in real estate:	
Land	$ 16,384
Buildings and improvements	202,142
Tenant improvements and other in-place lease assets	11,586
Other assets	19
Accounts payable, accrued expenses and tenant security deposits	(1,015)
Acquired lease intangibles	455
Net assets acquired	$ 229,571

During the fourth quarter of 2008, we contributed a portfolio of six Class A office properties and the related $365 million term loan secured by the six properties to an unconsolidated institutional real estate fund we manage. See also Note 13. In exchange, we received an interest in the common equity of that fund. Because the net value of the contributed properties (as valued under the fund’s operating agreement) exceeded our required capital contribution, the fund distributed cash to us for the excess. We received part of the cash in October 2008 and the remainder at the end of February 2009, at which point the fund became an unconsolidated real estate fund in which we retained an equity investment. We recognized a gain of $5,573 on the disposition of the interest in the fund we did not retain.

The results of operations for the contributed properties are included in our consolidated statement of operations only until the end of February 2009, when the properties were deconsolidated from our financial statements. Beginning in February 2009, we have accounted for our interest in the fund under the equity method.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)
(in thousands, except shares and per share data)

3. Segment Reporting

Segment information is prepared on the same basis that our management reviews information for operational decision-making purposes. We operate in two business segments: (i) the acquisition, redevelopment, ownership and management of office real estate and (ii) the acquisition, redevelopment, ownership and management of multifamily real estate. The products for our office segment primarily include rental of office space and other tenant services, including parking and storage space rental. The products for our multifamily segment include rental of apartments and other tenant services, including parking and storage space rental.

Asset information by segment is not reported because we do not use this measure to assess performance and make decisions to allocate resources. Therefore, depreciation and amortization expense is not allocated among segments. Interest and other income, management services, general and administrative expenses, interest expense, depreciation and amortization expense and net derivative gains and losses are not included in segment profit as our internal reporting addresses these items on a corporate level.

Segment profit is not a measure of operating income or cash flows from operating activities as measured by GAAP, and it is not indicative of cash available to fund cash needs and should not be considered an alternative to cash flows as a measure of liquidity. Not all companies may calculate segment profit in the same manner. We consider segment profit to be an appropriate supplemental measure to net income because it assists both investors and management in understanding the core operations of our properties.

The following table represents operating activity within our reportable segments:

	Three Months Ended June 30,		Six Months Ended June 30,	
Office Segment	2010	2009	2010	2009
Rental revenue	$ 122,243	$ 122,748	$ 243,019	$ 256,894
Rental expense	(37,198)	(36,665)	(73,312)	(76,977)
Segment profit	85,045	86,083	169,707	179,917
Multifamily Segment				
Rental revenue	16,966	17,047	33,977	34,318
Rental expense	(4,434)	(4,286)	(9,002)	(8,803)
Segment profit	12,532	12,761	24,975	25,515
Total segments' profit	$ 97,577	$ 98,844	$ 194,682	$ 205,432

The following table is a reconciliation of segment profit to net loss attributable to common stockholders:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
Total segments' profit	$97,577	$98,844	$194,682	$205,432

General and administrative expense	(5,944)