Extra Space Storage Inc.
Form 10-Q
November 07, 2007

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

x	**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
	For the quarterly period ended September 30, 2007
	or
o	**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: 001-32269

EXTRA SPACE STORAGE INC.

(Exact name of registrant as specified in its charter)

Maryland	**20-1076777**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

2795 East Cottonwood Parkway, Suite 400
Salt Lake City, Utah 84121
(Address of principal executive offices)

Registrant s telephone number, including area code: **(801) 562-5556**

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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x Accelerated filer o Non-accelerated filer 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

The number of shares outstanding of the registrant s common stock, par value $0.01 per share, as of October 31, 2007 was 65,299,160.

EXTRA SPACE STORAGE INC.

TABLE OF CONTENTS

STATEMENT ON FORWARD-LOOKING INFORMATION	3
PART I. FINANCIAL INFORMATION	4
ITEM 1. FINANCIAL STATEMENTS	4
ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	24
ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK	36
ITEM 4. CONTROLS AND PROCEDURES	37
PART II. OTHER INFORMATION	37
ITEM 1. LEGAL PROCEEDINGS	37
ITEM 1A. RISK FACTORS	37
ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS	37
ITEM 3. DEFAULTS UPON SENIOR SECURITIES	38
ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS	38
ITEM 5. OTHER INFORMATION	38
ITEM 6. EXHIBITS	39
SIGNATURES	39

STATEMENT ON FORWARD-LOOKING INFORMATION

Certain information set forth in this report contains forward-looking statements within the meaning of the federal securities laws. Forward-looking statements include statements concerning our plans, objectives, goals, strategies, future events, future revenues or performance, capital expenditures, financing needs, plans or intentions relating to acquisitions and other information that is not historical information. In some cases, forward-looking statements can be identified by terminology such as believes, expects, estimates, may, will, should, anticipates, or the negative of such terms or other comparable terminology, or by discussions of strategy. We may also make additional forward-looking statements from time to time. All such subsequent forward-looking statements, whether written or oral, by us or on our behalf, are also expressly qualified by these cautionary statements.

All forward-looking statements, including without limitation, management s examination of historical operating trends and estimate of future earnings, are based upon our current expectations and various assumptions. Our expectations, beliefs and projections are expressed in good faith and we believe there is a reasonable basis for them, but there can be no assurance that management s expectations, beliefs and projections will result or be achieved. All forward-looking statements apply only as of the date made. We undertake no obligation to publicly update or revise forward-looking statements which may be made to reflect events or circumstances after the date made or to reflect the occurrence of unanticipated events.

There are a number of risks and uncertainties that could cause our actual results to differ materially from the forward-looking statements contained in or contemplated by this report. Any forward-looking statements should be considered in light of the risks referenced in Part II. Item 1A. Risk Factors below and in Part I. Item 1A. Risk Factors included in our most recent Annual Report on Form 10-K. Such factors include, but are not limited to:

changes in general economic conditions and in the markets in which we operate;

the effect of competition from new self-storage facilities or other storage alternatives, which could cause rents and occupancy rates to decline;

potential liability for uninsured losses and environmental contamination;

difficulties in our ability to evaluate, finance and integrate acquired and developed properties into our existing operations and to lease up those properties, which could adversely affect our profitability;

the impact of the regulatory environment as well as national, state, and local laws and regulations including, without limitation, those governing real estate investment trusts, which could increase our expenses and reduce our cash available for distribution;

difficulties in raising capital at reasonable rates, which could impede our ability to grow;

delays in the development and construction process, which could adversely affect our profitability; and

economic uncertainty due to the impact of war or terrorism, which could adversely affect our business plan.

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Extra Space Storage Inc.

Condensed Consolidated Balance Sheets

(in thousands, except share data)

	September 30, 2007 (unaudited)	December 31, 2006
Assets:		
Real estate assets:		
Net operating real estate assets	$ 1,707,384	$ 1,382,055
Real estate under development	49,943	35,336
Net real estate assets	1,757,327	1,417,391
Investments in real estate ventures	89,876	88,115
Cash and cash equivalents	41,830	70,801
Short-term investments	49,200	
Restricted cash	36,642	44,282
Receivables from related parties and affiliated real estate joint ventures	9,447	15,880
Other assets, net	35,253	33,356
Total assets	$ 2,019,575	$ 1,669,825
Liabilities, Minority Interests and Stockholders Equity:		
Notes payable	$ 902,930	$ 828,584
Notes payable to trusts	119,590	119,590
Exchangeable senior notes	250,000	
Line of credit		
Accounts payable and accrued expenses	33,951	25,704
Other liabilities	18,416	17,234
Total liabilities	1,324,887	991,112
Commitments and contingencies		
Minority interest represented by Preferred Operating Partnership units, net of $100,000 note receivable (Note 15)	30,427	
Minority interest in Operating Partnership	36,807	34,841
Other minority interests	164	317
Stockholders equity:		
Preferred stock , $0.01 par value, 50,000,000 shares authorized, no shares issued or outstanding		
Common Stock, $0.01 par value, 300,000,000 and 200,000,000 shares authorized at September 30,2007 and December 31, 2006, respectively, and 65,276,108 and 64,167,098 shares issued and outstanding at September 30, 2007 and December 31, 2006 respectively	653	642
Paid-in capital	825,130	822,181
Accumulated deficit	(198,493)	(179,268)
Total stockholders equity	627,290	643,555
Total liabilities, minority interests and stockholders equity	$ 2,019,575	$ 1,669,825

See accompanying notes to unaudited condensed consolidated financial statements.

Extra Space Storage Inc.
Condensed Consolidated Statements of Operations
(in thousands, except share data)
(unaudited)

	Three months ended September 30, 2007	Three months ended September 30, 2006	Nine months ended September 30, 2007	Nine months ended September 30, 2006
Revenues:				
Property rental	$ 55,209	$ 44,682	$ 149,832	$ 125,877
Management and franchise fees	5,169	5,357	15,520	15,697
Tenant insurance	3,027	716	7,858	2,608
Development fees	97	47	334	272
Other income	324	386	608	635
Total revenues	63,826	51,188	174,152	145,089
Expenses:				
Property operations	19,607	16,613	53,855	46,603
Tenant insurance	1,397	284	3,587	1,506
Unrecovered development and acquisition costs	184	(87)	593	255
General and administrative	9,326	8,598	27,534	26,590
Depreciation and amortization	10,598	9,253	28,517	27,586
Total expenses	41,112	34,661	114,086	102,540
Income before interest, Preferred Operating Partnership, minority interests and equity in earnings of real estate ventures	22,714	16,527	60,066	42,549
Interest expense	(16,079)	(13,429)	(44,912)	(38,198)
Interest income	1,821	175	6,937	805
Interest income on note receivable from Preferred Unit holder	1,280		1,280	
Equity in earnings of real estate ventures	1,304	1,340	3,693	3,566
Fair value adjustment of obligation associated with Preferred Operating Partnership units (Note 15)	1,054		1,054	
Minority interest - Operating Partnership	(869)	(306)	(1,768)	(585)
Minority interests - other	113		153	
Net income	11,338	4,307	26,503	8,137
Fixed distribution paid to Preferred Operating Partnership unit holder (Note 15)	(1,510)		(1,510)	
Net income available to common stockholders	$ 9,828	$ 4,307	$ 24,993	$ 8,137
Net income per common share				
Basic	$ 0.15	$ 0.08	$ 0.39	$ 0.16
Diluted	$ 0.15	$ 0.08	$ 0.38	$ 0.16
Weighted average number of shares				
Basic	64,901,249	52,501,864	64,461,353	51,929,336
Diluted	70,567,078	57,072,838	69,702,837	56,250,164
Cash dividends paid per common share	$ 0.23	$ 0.23	$ 0.68	$ 0.68

See accompanying notes to unaudited condensed consolidated financial statements.

Extra Space Storage Inc.
Condensed Consolidated Statement of Stockholders Equity
(in thousands, except share data)
(unaudited)

	Common Stock		Paid-in	Accumulated	Total Stockholders
	Shares	Par Value	Capital	Deficit	Equity
Balances at December 31, 2006	64,167,098	642	822,181	(179,268)	643,555
Issuance of common stock upon the exercise of options	99,290	1	1,338		1,339
Restricted stock grants issued	119,329	1			1
Restricted stock grants cancelled	(2,607)				
Conversion of Contingent Conversion Shares to common stock	892,998	9			9
Compensation expense related to stock-based awards			1,611		1,611
Fixed distribution paid to Preferred Operating Partnership unit holder				(1,510)	(1,510)
Net income				26,503	26,503
Dividends paid on common stock at $0.6825 per share				(44,218)	(44,218)
Balances at September 30, 2007	65,276,108	$ 653	$ 825,130	$ (198,493)	$ 627,290

See accompanying notes to unaudited condensed consolidated financial statements.

Extra Space Storage Inc.
Condensed Consolidated Statements of Cash Flows
(in thousands)
(unaudited)

	Nine months ended September 30, 2007	2006
Cash flows from operating activities:		
Net income	$ 26,503	$ 8,137
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	28,517	27,586
Amortization of deferred financing costs	2,457	2,111
Fair value adjustment of obligation associated with Preferred Operating Partnership units (Note 15)	(1,054)	
Stock compensation expense	1,611	1,377
Income allocated to minority interests	1,615	585
Distributions from operations of real estate ventures in excess of earnings	3,454	3,423
Changes in operating assets and liabilities:		
Receivables from related parties	4,835	16,619
Other assets	5,045	3,607
Accounts payable and accrued expenses	8,247	(6,485)
Other liabilities	(2,378)	3,756
Net cash provided by operating activities	78,852	60,716
Cash flows from investing activities:		
Acquisition of real estate assets	(144,347)	(127,826)
Development and construction of real estate assets	(31,495)	(26,301)
Proceeds from sale of real estate assets	1,999	728
Investments in real estate ventures	(4,769)	(5,104)
Net purchases of short-term investments	(49,200)	
Change in restricted cash	7,640	1,451
Principal payments received on notes receivable		123
Purchase of equipment and fixtures	(835)	(1,217)
Net cash used in investing activities	(221,007)	(158,146)
Cash flows from financing activities:		
Proceeds from exchangeable senior notes	250,000	
Proceeds from notes payable, notes payable to trusts and line of credit	50,102	129,126
Principal payments on notes payable and line of credit	(31,135)	(65,213)
Deferred financing costs	(7,740)	(899)
Loan to Preferred OP unit holder	(100,000)	
Redemption of Operating Partnership units held by minority interest	(775)	
Proceeds from issuance of common shares, net		194,901
Net proceeds from exercise of stock options	1,339	565
Dividends paid on common stock	(44,218)	(35,407)
Distributions to Operating Partnership units held by minority interest	(4,389)	(2,610)
Net cash provided by financing activities	113,184	220,463
Net increase (decrease) in cash and cash equivalents	(28,971)	123,033
Cash and cash equivalents, beginning of the period	70,801	28,653
Cash and cash equivalents, end of the period	$ 41,830	$ 151,686

	Nine months ended September 30, 2007	2006
Supplemental schedule of cash flow information		
Interest paid, net of amounts capitalized	$ 37,756	$ 35,379
Supplemental schedule of noncash investing and financing activities:		
Acquisitions:		
Real estate assets acquired	$ 190,185	$ 27,091
Notes payable acquired	(54,350)	(10,878)
Notes receivable		(10,298)
Preferred Operating Partnership units issued as consideration	(131,499)	
Investment in real estate ventures	(502)	(2,785)
Minority interest in Operating Partnership	(3,834)	(3,130)
Conversion of Operating Parntership Units held by minority interests for common stock		1,811

See accompanying notes to unaudited condensed consolidated financial statements.

Extra Space Storage Inc.

Notes to Condensed Consolidated Financial Statements (unaudited)

Amounts in thousands, except share data

1. ORGANIZATION

Extra Space Storage Inc. (the Company) is a fully-integrated, self-administered and self-managed real estate investment trust (REIT), formed as a Maryland corporation on April 30, 2004 to own, operate, manage, acquire and develop self-storage facilities located throughout the United States. The Company continues the business of Extra Space Storage LLC and its subsidiaries, which had engaged in the self-storage business since 1977. The Company s interest in its properties is held through its operating partnership, Extra Space Storage LP (the Operating Partnership), which was formed on May 5, 2004. The Company s primary assets are general partner and limited partner interests in the Operating Partnership. This structure is commonly referred to as an umbrella partnership REIT, or UPREIT. The Company has elected to be taxed as a REIT under the Internal Revenue Code of 1986, as amended. To the extent the Company continues to qualify as a REIT, it will not be subject to tax, with certain limited exceptions, on the taxable income that is distributed to its stockholders.

The Company invests in self-storage facilities by acquiring or developing wholly-owned facilities or facilities held through joint ventures with third parties. At September 30, 2007, the Company had direct and indirect equity interests in 585 storage facilities located in 33 states and Washington, D.C.

The Company operates in two distinct segments: (1) property management, acquisition and development; and (2) rental operations. The Company s property management, acquisition and development activities include managing, acquiring, developing and selling self-storage facilities. The rental operations activities include rental operations of self-storage facilities. No single tenant accounts for more than 5% of rental income.

2. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements of the Company have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and nine months ended September 30, 2007 are not necessarily indicative of results that may be expected for the year ending December 31, 2007. The Condensed Consolidated Balance Sheet as of December 31, 2006 has been derived from the Company s audited financial statements as of that date, but does not include all of the information and footnotes required by GAAP for complete financial statements. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2006 as filed with the Securities and Exchange Commission (SEC).

Certain amounts in the 2006 financial statements and supporting note disclosures have been reclassified to conform to the current year presentation. Such reclassification did not impact previously reported net income or accumulated deficit.

Recently Issued Accounting Standards

Emerging Issues Task Force (EITF) Topic D-109, *Determining the Nature of a Host Contract Related to a Hybrid Financial Instrument Issued in the Form of a Share under FASB Statement No. 133* (Topic D-109), discussed at the March 15, 2007 EITF meeting, is effective at the beginning of the first fiscal quarter beginning after June 15, 2007 (even if that period is other than the first fiscal quarter of the registrant s fiscal year). Topic D-109 provides the SEC staff s view as to how one must evaluate whether a preferred stock host contract is a debt host or an equity host. It states that the determination of the nature of the host contract for a hybrid financial instrument (that is, whether the nature of the host contract is more akin to debt or to equity) issued in the form of a share should be based on a consideration of economic characteristics and risks. The SEC staff believes that the consideration of the economic characteristics and risks of the host contract should be based on all the stated and implied substantive terms and features of the hybrid financial instrument. This may represent a change from the way these instruments were analyzed in the past.

The Company elected to early adopt Topic D-109 which specifically relates to the AAAAA Rent-A-Space acquisition that was completed during the quarter ended June 30, 2007. See Note 15.

3. NET INCOME PER SHARE

Basic earnings per common share is computed by dividing net income by the weighted average common shares outstanding, less non-vested restricted stock. Diluted earnings per common share measures the performance of the Company over the reporting period while giving effect to all potential common shares that were dilutive and outstanding during the period. The denominator includes the number of additional common shares that would have been outstanding if the potential common shares that were dilutive had been issued and is calculated using either the treasury stock or if converted method. Potential common shares are securities (such as options, warrants, convertible debt, Contingent Conversion Shares (CCS), Contingent Conversion Units (CCU), exchangeable Series A Participating Redeemable Preferred Operating Partnership units (Preferred OP units) and convertible Operating Partnership units) (OP units) that do not have a current right to participate in earnings but could do so in the future by virtue of their option or conversion right. In computing the dilutive effect of convertible securities, net income or loss is adjusted to add back any changes in earnings in the period associated with the convertible security. The numerator also is adjusted for the effects of any other non-discretionary changes in income or loss that would result from the assumed conversion of those potential common shares. In computing diluted earnings per share, only potential common shares that are dilutive, those that reduce earnings per share, are included.

The Company has $250.0 million of exchangeable senior notes issued and outstanding that also can potentially have a dilutive effect on its earnings per share calculations. The exchangeable senior notes are exchangeable by holders into shares of the Company s common stock under certain circumstances per the terms of the indenture governing the exchangeable senior notes. The exchangeable senior notes are not exchangeable unless the price of the Company s common stock is greater than or equal to 130% of the applicable exchange price for a specified period during a quarter, or unless certain other events occur. The exchange price was $23.48 per share at September 30, 2007, and could change over time as described in the indenture. The price of the Company s common stock did not exceed 130% of the exchange price for the specified period of time during the third quarter of 2007, therefore holders of the exchangeable senior notes may not elect to convert them during the fourth quarter of 2007.

The Company has irrevocably agreed to pay only cash for the accreted principal amount of the exchangeable senior notes relative to its exchange obligations, but has retained the right to satisfy the exchange obligations in excess of the accreted principal amount in cash and/or common stock. Though the Company has retained that right, FAS 128, Earnings Per Share, requires an assumption that shares will be used to pay the exchange obligations in excess of the accreted principal amount, and requires that those shares be included in the Company s calculation of weighted average common shares outstanding for the diluted earnings per share computation. No shares were included in the computation at September 30, 2007 because there was no excess over the accreted principal for the period.

For the purposes of computing the diluted impact on earnings per share of the potential conversion of Preferred OP units into common shares, where the Company has the option to redeem in cash or shares as discussed in Note 15 and where the Company has stated the positive intent and ability to settle at least $115 million of the instrument in cash (or net settle a portion of the Preferred OP units against the related outstanding note receivable), only the amount of the instrument in excess of $115 million is considered in the calculation of shares contingently issuable for the purposes of computing diluted earnings per share as allowed by paragraph 29 of FAS 128.

For the three months ended September 30, 2007 and 2006, options to purchase approximately 1,184,978 and 18,511 shares of common stock, and for the nine months ended September 30, 2007 and 2006, options to purchase approximately 256,506 and 66,560 shares of common stock, respectively, were excluded from the computation of earnings per share as their effect would have been anti-dilutive.

The computation of net income per share is as follows:

10

	Three months ended September 30,		Nine months ended September 30,	
	2007	**2006**	**2007**	**2006**
Net income available to common stockholders	$ 9,828	$ 4,307	$ 24,993	$ 8,137
Add:				
Income allocated to minority interest - Preferred and Common Operating Partnership	869	306	1,768	585
Net income for diluted computations	$ 10,697	$ 4,613	$ 26,761	$ 8,722
Weighted average common shares oustanding:				
Average number of common shares outstanding - basic	64,901,249	52,501,864	64,461,353	51,929,336
Operating Partnership units	4,025,332	3,737,579	4,025,332	3,796,384
Preferred Operating Partnership units	961,839		340,561	
Dilutive stock options, restricted stock and CCS/CCU conversions	678,658	833,395	875,591	524,444
Average number of common shares outstanding - diluted	70,567,078	57,072,838	69,702,837	56,250,164
Net income per common share				
Basic	$ 0.15	$ 0.08	$ 0.39	$ 0.16
Diluted	$ 0.15	$ 0.08	$ 0.38	$ 0.16

4. REAL ESTATE ASSETS

The components of real estate assets are summarized as follows:

	September 30, 2007	December 31, 2006
Land	$ 442,882	$ 361,569
Buildings and improvements	1,347,832	1,085,269
Intangible assets - tenant relationships	31,194	25,436
Intangible lease rights	6,150	3,400
	1,828,058	1,475,674
Less: accumulated depreciation and amortization	(120,674)	(93,619)
Net operating real estate assets	1,707,384	1,382,055
Real estate under development	49,943	35,336
Net real estate assets	$ 1,757,327	$ 1,417,391

On August 3, 2007, the Company sold an undeveloped parcel of vacant land in Kendall, Florida for its book value of $1,999. There was no gain or loss recognized on the sale.

5. PROPERTY ACQUISITIONS

The following table shows the Company s acquisition of operating properties for the nine months ended September 30, 2007 and does not include purchases of raw land or improvements made to existing assets:

Property Location(s)	Number of Properties	Date of Acquisition	Total Consideration	Cash Paid	Loan Assumed	Net Liabilities / (Assets) Assumed	Value of OP Units Issued	Number of OP Units Issued	Source of Acquisition	Notes
Alabama (1), Colorado(1), Indiana (1), Missouri (3),New Mexico (1)	7	8/31/07	$ 36,510	$ 13,558	$ 23,340	$ (388)	$		Affiliated joint venture	
Maryland	1	8/31/07	10,471	10,418		53			Affiliated joint venture	
California	1	8/1/2007	14,686	4,915		5	9,766	80,905	Unrelated third party	(1)
California	1	6/26/2007	11,216	196	2,822	1	8,197	61,398	Unrelated third party	(1)
California (6) & Hawaii (2)	8	6/25/2007	126,623	11,154		1,933	113,536	847,677	Unrelated third party	(1)
Georgia	3	6/14/2007	13,693	13,594		99			Unrelated franchisee	
California	1	6/14/2007	18,703	867	14,062	(60)	3,834	218,693	Unrelated third party	(2)
Maryland	1	6/6/2007	14,942	8,128	6,834	(20)			Unrelated third party	
California	1	6/1/2007	4,020	4,036		(16)			Unrelated third party	
Florida	1	5/31/2007	8,975	8,882		93			Unrelated third party	
California	1	5/24/2007	5,585	5,575		10			Unrelated third party	
Maryland	1	4/17/2007	12,670	5,428	7,292	(50)			Unrelated third party	
Florida	1	3/27/2007	6,320	6,257		63			Unrelated franchisee	
Maryland	1	1/11/2007	14,334	14,348		(14)			Unrelated franchisee	
Tennessee	1	1/5/2007	3,684	3,672		12			Unrelated franchisee	
Arizona	1	1/2/2007	4,361	4,527		(166)			Affiliated joint venture	
Total	31		$ 306,793	$ 115,555	$ 54,350	$ 1,555	$ 135,333	1,208,673		

Notes:

(1) - Preferred Operating Partnership Units

(2) - Common Operating Partnership Units

6. INVESTMENTS IN REAL ESTATE VENTURES

Investments in real estate ventures consisted of the following:

	Excess Profit Participation %	Equity Ownership %	Investment balance at September 30, 2007	Investment balance at December 31, 2006
Extra Space West One LLC (ESW)	40%	5%	$ 1,796	$ 1,918
Extra Space Northern Properties Six, LLC (ESNPS)	35%	10%	1,701	1,757
PRISA Self Storage LLC (PRISA)	17%	2%	12,791	13,393
PRISA II Self Storage LLC (PRISA II)	17%	2%	10,781	10,821
PRISA III Self Storage LLC (PRISA III)	20%	5%	4,436	4,534
VRS Self Storage LLC (VRS)	20%	5%	4,542	4,547
WCOT Self Storage LLC (WCOT)	20%	5%	5,236	5,287
Storage Portfolio I, LLC (SP I)	40%	25%	18,708	19,260
Storage Portfolio Bravo II (SPB II)	45%	20%	14,822	15,264
U-Storage de Mexico S.A. and related entities	30-40%	30-40%	4,958	

Other minority owned properties	10-50%	10-50%		10,105		11,334
			$	89,876	$	88,115

In these joint ventures, the Company and the joint venture partner generally receive a preferred return on their invested capital. To the extent that cash/profits in excess of these preferred returns are generated through operations or capital transactions, the Company would receive a higher percentage of the excess cash/profits than its equity interest.

On March 1, 2007, the Company acquired a 39.5% interest in U-Storage de Mexico S.A., an existing Mexican corporation (U-Storage), which currently manages, develops, owns and operates self storage facilities in Mexico. Kenneth T. Woolley, a former Senior Vice President of the Company and son of Kenneth M. Woolley, the CEO of the Company, also acquired a 0.5% interest in U-Storage de Mexico S.A.

The components of equity in earnings of real estate ventures consist of the following:

	Three months ended September 30, 2007	Three months ended September 30, 2006	Nine months ended September 30, 2007	Nine months ended September 30, 2006
Equity in earnings of ESW	$ 411	$ 337	$ 1,106	$ 1,018
Equity in earnings of ESNPS	49	39	136	113
Equity in earnings of PRISA	166	138	521	394
Equity in earnings of PRISA II	153	110	430	334
Equity in earnings of PRISA III	86	35	220	88
Equity in earnings of VRS	67	43	190	119
Equity in earnings of WCOT	77	40	224	114
Equity in earnings of SP I	333	291	785	740
Equity in earnings of SPB II	189	210	560	599
Equity in earnings (losses) of U-Storage and related entities	(141)		(221)	
Equity in earnings (losses) of other minority owned properties	(86)	97	(258)	47
	$ 1,304	$ 1,340	$ 3,693	$ 3,566

Equity in earnings of SP I and SPB II includes the amortization of the Company s excess purchase price of approximately $22 million of these equity investments over its original basis. The excess basis is amortized over 40 years.

7. SHORT-TERM INVESTMENTS

The Company accounts for its investments in debt and equity securities according to the provisions of Statement of Financial Accounting Standards (SFAS) No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, which requires securities classified as available-for-sale to be stated at fair value. Adjustments to fair value of available-for-sale securities are recorded as a component of other comprehensive income. A decline in the market value of investment securities below cost, that is deemed to be other than temporary, results in a reduction in the carrying amount to fair value. The impairment is charged to earnings and a new cost basis for the security is established. At September 30, 2007, the Company had $49,200 in highly-liquid auction rate securities (ARS), government and corporate bonds and variable rate demand notes classified as available-for-sale securities. Although these ARS have long-term stated contractual maturities, they can be presented for redemption at auction when rates are reset which is typically every 7, 28 or 35 days. The Company had no realized or unrealized gains or losses related to these securities during the three and nine months ended September 30, 2007. All income related to these investments was recorded as interest income. In accordance with the Company s investment policy, the Company only invests in ARS with high credit quality issuers and limits the amount of investment exposure to any one issuer.

8. OTHER ASSETS

The components of other assets are summarized as follows:

	September 30, 2007	December 31, 2006
Equipment and fixtures	$ 11,918	$ 11,083
Less: accumulated depreciation	(8,042)	(6,564)
Deferred financing costs, net	15,132	10,511
Prepaid expenses and deposits	5,240	5,139

Accounts receivable, net		7,192		9,373
Investments in Trusts		3,590		3,590
Other		223		224
	$	35,253	$	33,356

9. NOTES PAYABLE

The components of notes payable are summarized as follows:

	September 30, 2007	December 31, 2006
Fixed Rate		
Mortgage and construction loans with banks bearing interest at fixed rates between 4.65% and 8.33%. The loans are collateralized by mortgages on real estate assets and the assignment of rents. Principal and interest payments are made monthly with all outstanding principal and interest due between March 1, 2008 and January 1, 2023.	$ 810,009	$ 743,511
Variable Rate		
Mortgage and construction loans with banks bearing floating interest rates (including loans subject to interest rate swaps) based on LIBOR. Interest rates are between LIBOR plus 0.65% (5.77% and 6.01% at September 30, 2007 and December 31, 2006, respectively) and LIBOR plus 2.00% (7.12% and 7.35% at September 30, 2007 and December 31, 2006, respectively). The loans are collateralized by mortgages on real estate assets and the assignment of rents. Principal and interest payments are made monthly with all outstanding principal and interest due between December 31, 2008 and March 1, 2011.	92,921	85,073
	$ 902,930	$ 828,584

Real estate assets are pledged as collateral for the notes payable. The Company is subject to certain restrictive covenants relating to the outstanding notes payable. The Company was in compliance with all covenants at September 30, 2007.

In October 2004, the Company entered into a reverse interest rate swap agreement (Swap Agreement) to float $61,770 of 4.30% fixed interest rate secured notes due in September 2009. Under this Swap Agreement, the Company will receive interest at a fixed rate of 4.30% and pay interest at a variable rate equal to LIBOR plus 0.65%. The Swap Agreement matures at the same time the notes are due. This Swap Agreement is a fair value hedge, as defined by SFAS No. 133, and the fair value of the Swap Agreement is recorded as an asset or liability, with an offsetting adjustment to the carrying value of the related note payable. Monthly variable interest payments are recognized as an increase or decrease in interest expense.

The estimated fair value of the Swap Agreement at September 30, 2007 and December 31, 2006 was reflected as an other liability of $896 and $1,925, respectively. The Company recorded additional interest expense relating to the Swap Agreement of $273 and $258 for the three months ended September 30, 2007 and 2006, respectively. Interest expense was increased by $798 and $540 for the nine months ended September 30, 2007 and 2006, respectively.

On August 31, 2007, as part of the acquisition of our partner s joint venture interest in seven properties, the Company assumed an interest rate cap agreement related to the assumption of the loan on these properties. The Company has designated the interest rate cap agreement as a cash flow hedge of the interest payments resulting from an increase in the interest rate above the rates designated in the interest rate cap agreement. The interest rate cap agreement will allow increases in interest payments based on an increase in the LIBOR rate above the capped rates (5.19% from 1/1/07 to 12/31/07 and 5.48% from 1/1/08 to 12/31/08) on $23,340 of floating rate debt to be offset by the value of the interest rate cap agreement. The Company is in the process of valuing the hedge as part of the purchase accounting and related allocation for the seven properties.

10. NOTES PAYABLE TO TRUSTS

During July 2005, ESS Statutory Trust III (the Trust III), a newly formed Delaware statutory trust and a wholly-owned, unconsolidated subsidiary of the Operating Partnership, issued an aggregate of $40.0 million of preferred securities which mature on July 31, 2035. In addition, the Trust III issued 1,238 of Trust common securities to the Operating Partnership for a purchase price of $1.2 million. On July 27, 2005, the proceeds from the sale of the preferred and common securities of $41.2 million were loaned in the form of a note to the Operating Partnership (Note 3). Note 3 has a fixed rate of 6.91% through July 31, 2010, and then will be payable at a variable rate equal to the three-month LIBOR plus 2.40% per annum. The interest on Note 3, payable quarterly, will be used by the Trust III to pay dividends on the trust preferred securities. The trust preferred securities may be redeemed by the Trust with no prepayment premium after July 27, 2010.

During May 2005, ESS Statutory Trust II (the Trust II), a newly formed Delaware statutory trust and a wholly-owned, unconsolidated subsidiary of the Operating Partnership, issued an aggregate of $41.0 million of preferred securities which

mature on June 30, 2035. In addition, the Trust II issued 1,269 of Trust common securities to the Operating Partnership for a purchase price of $1.3 million. On May 24, 2005, the proceeds from the sale of the preferred and common securities of $42.3 million were loaned in the form of a note to the Operating Partnership (Note 2). Note 2 has a fixed rate of 6.67% through June 30, 2010, and then will be payable at a variable rate equal to the three-month LIBOR plus 2.40% per annum.

The interest on Note 2, payable quarterly, will be used by the Trust II to pay dividends on the trust preferred securities. The trust preferred securities may be redeemed by the Trust with no prepayment premium after June 30, 2010.

During April 2005, ESS Statutory Trust I (the Trust), a newly formed Delaware statutory trust and a wholly-owned, unconsolidated subsidiary of the Operating Partnership issued an aggregate of $35.0 million of trust preferred securities which mature on June 30, 2035. In addition, the Trust issued 1,083 of trust common securities to the Operating Partnership for a purchase price of $1.1 million. On April 8, 2005, the proceeds from the sale of the trust preferred and common securities of $36.1 million were loaned in the form of a note to the Operating Partnership (the Note). The Note has a variable rate equal to the three-month LIBOR plus 2.25% per annum. The interest on the Note, payable quarterly, will be used by the Trust to pay dividends on the trust preferred securities. The trust preferred securities may be redeemed by the Trust with no prepayment premium after June 30, 2010.

The Company follows Financial Accounting Standards Board (FASB) Intrepretation No. 46R, Consolidation of Variable Interest Entities (FIN 46R), which addresses the consolidation of variable interest entities (VIEs). Under FIN 46R, Trust, Trust II and Trust III are VIEs that are not consolidated because the Company is not the primary beneficiary. A debt obligation has been recorded in the form of notes as discussed above for the proceeds, which are owed to the Trust, Trust II, and Trust III by the Company.

11. EXCHANGEABLE SENIOR NOTES

On March 27, 2007, our Operating Partnership issued $250.0 million of its 3.625% Exchangeable Senior Notes due April 1, 2027 (the Notes). Costs incurred to issue the Notes were approximately $5.7 million. These costs are being amortized as an adjustment to interest expense over five years, which represents the estimated term of the Notes, and are included in other assets, net in the Condensed Consolidated Balance Sheet as of September 30, 2007. The Notes are general unsecured senior obligations of the Operating Partnership and are fully guaranteed by the Company. Interest is payable on April 1 and October 1 of each year beginning October 1, 2007 until the maturity date of April 1, 2027. The Notes bear interest at 3.625% per annum and contain an exchange settlement feature, which provides that the Notes may, under certain circumstances, be exchangeable for cash (up to the principal amount of the Notes) and, with respect to any excess exchange value, for cash, shares of our common stock or a combination of cash and shares of our common stock at an initial exchange rate of approximately 42.5822 shares per $1,000 principal amount of Notes at the option of the Operating Partnership.

The Operating Partnership may redeem the Notes at any time to preserve the Company s status as a REIT. In addition, on or after April 5, 2012, the Operating Partnership may redeem the Notes for cash, in whole or in part, at 100% of the principal amount plus accrued and unpaid interest, upon at least 30 days but not more than 60 days prior written notice to holders of the Notes.

The holders of the Notes have the right to require the Operating Partnership to repurchase the Notes for cash, in whole or in part, on each of April 1, 2012, April 1, 2017 and April 1, 2022, and upon the occurrence of a designated event, in each case for a repurchase price equal to 100% of the principal amount of the Notes plus accrued and unpaid interest. Certain events are considered Events of Default, as defined in the indenture governing the Notes, which may result in the accelerated maturity of the Notes.

The Company has considered whether the exchange settlement feature represents an embedded derivative within the debt instrument under the guidance of FAS 133 *Accounting for Derivative Instruments and Hedging Activities,* EITF 90-19 *Convertible Bonds with Issuer Option to Settle for Cash Upon Conversion*, and EITF 01-6 *The Meaning of Indexed to a Company s Own Stock* that would require bifurcation (i.e., separate accounting). The Company has concluded that the exchange settlement feature has satisfied the exemption in SFAS 133 because it is indexed to the Company s own stock and would otherwise be classified in stockholders equity, among other considerations. Accordingly, the Notes are presented as a single debt instrument (often referred to as Instrument C in EITF 90-19) in accordance with APB 14 *Accounting for Convertible Debt and Debt Issued with Stock Purchase Warrants* due to the inseparability of the debt and the conversion feature.

12. LINE OF CREDIT

The Company, as guarantor, and its Operating Partnership had entered into a $100.0 million revolving line of credit in September 2004, which included a $10.0 million swingline subfacility (the Credit Facility). The Credit Facility had an interest rate of 175 basis points over LIBOR (6.87% and 7.10% at September 30, 2007 and December 31, 2006, respectively), and was collateralized by mortgages on certain real estate assets. No amounts were outstanding on the line of credit at September 30, 2007 or December 31, 2006. The Credit Facility expired on September 30, 2007.

On October 19, 2007, the Company entered into a new $100.0 million revolving line of credit (the Credit Line). The Company intends to use the proceeds of the Credit Line for general corporate purposes. The Credit Line has an interest rate of between 100 and 250 basis points over LIBOR, depending on certain financial ratios of the Company. The Credit Line is collateralized by mortgages on certain real estate assets. As of the closing date, the Credit Line had approximately $97 million of capacity based on the assets collateralizing the Credit Line. The Credit Line matures October 31, 2010.

13. OTHER LIABILITIES

The components of other liabilities are summarized as follows:

	September 30, 2007	December 31, 2006
Deferred rental income	$ 11,622	$ 9,224
Security deposits	401	291
SUSA lease obligation liability	2,655	2,838
Fair value of interest rate swap	896	1,925
Other miscellaneous liabilities	2,842	2,956
	$ 18,416	$ 17,234

14. RELATED PARTY AND AFFILIATED REAL ESTATE JOINT VENTURE TRANSACTIONS

The Company provides management and development services for certain joint ventures, franchise, third party and other related party properties. Management agreements generally provide for management fees of 6% of cash collected from properties for the management of operations at the self-storage facilities. The Company earns development fees of 4%-6% of budgeted costs on developmental projects.

Management fee revenue for related party and affiliated real estate joint ventures is summarized as follows:

Three months ended September 30,	Nine months ended September 30,

Entity	Type	2007	2006	2007	2006
ESW	Affiliated real estate joint ventures	$ 110	$ 103	$ 328	$ 307
ESNPS	Affiliated real estate joint ventures	113	110	329	316
PRISA	Affiliated real estate joint ventures	1,273	1,289	3,868	3,780
PRISA II	Affiliated real estate joint ventures	1,052	1,038	3,142	3,056
PRISA III	Affiliated real estate joint ventures	475	476	1,417	1,384
VRS	Affiliated real estate joint ventures	292	285	860	838
WCOT	Affiliated real estate joint ventures	387	373	1,155	1,096
SP I	Affiliated real estate joint ventures	319	309	945	910
SPB II	Affiliated real estate joint ventures	254	260	770	777
Extra Space Development ("ESD")	Related party	193	129	548	333
Various	Franchisees, third parties and other	701	985	2,158	2,900
		$ 5,169	$ 5,357	15,520	15,697

Development fee revenue for related party and affiliated real estate joint ventures is summarized as follows:

Type	Three months ended September 30, 2007	2006	Nine months ended September 30, 2007	2006
Affiliated real estate joint ventures	$ 97	$ 16	$ 334	$ 163
Related party		31		109
	$ 97	$ 47	$ 334	$ 272

Effective January 1, 2004, the Company entered into a license agreement with Centershift, a related party software provider, to secure a perpetual right for continued use of STORE (the site management software used at all sites operated by the Company) in all aspects of the Company s property acquisition, development, redevelopment and operational activities. The Company paid Centershift $225 and $185 for the three months ended September 30, 2007 and 2006, respectively, and $680 and $549 for the nine months ended September 30, 2007 and 2006, respectively, relating to the purchase of software and to license agreements.

Related party and affiliated real estate joint ventures balances are summarized as follows:

	September 30, 2007	December 31, 2006
Receivables:		
Development fees	$ 2,562	$ 2,633
Other receivables from properties	6,885	13,247
	$ 9,447	$ 15,880

Other receivables from properties consist of amounts due for management fees and expenses paid by the Company on behalf of the managed properties. The Company believes that all of these related party and affiliated joint venture receivables are fully collectible. The Company did not have any payables to related parties at September 30, 2007 or December 31, 2006.

15. MINORITY INTEREST REPRESENTED BY PREFERRED OPERATING PARTNERSHIP UNITS

On June 15, 2007, the Operating Partnership entered into a Contribution Agreement with various limited partnerships affiliated with AAAAA Rent-A-Space to acquire ten self-storage facilities (the Properties) in exchange for the issuance of newly designated Preferred OP Units of the Operating Partnership. The self-storage facilities are located in California and Hawaii.

On June 25 and 26, 2007, nine of the ten properties were contributed to the Operating Partnership in exchange for consideration totaling $137.8 million. Preferred OP units totaling 909,075, with a value of $121.7 million, were issued along with the assumption of approximately $14.2 million of third-party debt, of which $11.4 million was paid off at close. The final property was contributed on August 1, 2007 in exchange for consideration totaling $14.7 million. 80,905 Preferred OP Units with a value of $9.8 million were issued along with $4.9 million of cash.

On June 25, 2007, the Company loaned the holders of the Preferred OP Units $100.0 million. The note receivable bears interest at 4.85%, and is due September 1, 2017. The loan is secured by the borrower s Preferred OP Units. The holders of the Preferred OP Units can convert up to 114,500 Preferred OP Units prior to the maturity date of the loan. If any redemption in excess of 114,500 Preferred OP Units occurs prior to the maturity date, the holder of the Preferred OP Unit is required to repay the loan as of the date of that Preferred OP Unit redemption. Preferred OP Units are shown on the balance sheet net of the $100.0 million loan under the guidance in EITF No. 85-1, *Classifying Notes Receivable for*

Capital because the borrower under the loan receivable is also the holder of the Preferred OP Units.

The Operating Partnership entered into a Second Amended and Restated Agreement of Limited Partnership (the Partnership Agreement) which provides for the designation and issuance of the Preferred OP Units. The Preferred OP Units will have priority over all other partnership interests of the Operating Partnership with respect to distributions and liquidation.

Per the Partnership Agreement, Preferred OP Units in the amount of $115.0 million bear a fixed priority return of 5% and have a fixed liquidation value of $115.0 million. The remaining balance will participate in distributions with and have a

liquidation value equal to that of the common Operating Partnership units. The Preferred OP Units will be redeemable at the option of the holder on or after September 1, 2008, which redemption obligation may be satisfied, at the Company s option, in cash or shares of its common stock.

At issuance, in accordance with SFAS 133: *Accounting for Derivative Instruments and Hedging Activities*, SFAS 150: *Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity,* EITF 00-19: *Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company s Own Stock,* EITF Topic D-109: *Determining the Nature of a Host Contract Related to a Hybrid Financial Instrument Issued in the Form of a Share under FASB Statement No. 133:* and Accounting Series Release (ASR) No. 268: *Presentation in Financial Statements of Redeemable Preferred Stocks,* from inception through September 28, 2007 (the date of the amendment discussed below), the Preferred OP Units were classified as a hybrid instrument such that the value of the units associated with the fixed return were classified in mezzanine after total liabilities on the balance sheet and before stockholders equity. The remaining balance that participates in distributions equal to that of common OP Units had been identified as an embedded derivative and had been classified as a liability on the balance sheet and recorded at fair value on a quarterly basis with any adjustment being recorded to the income statement. For the three and nine months ended September 30, 2007, the fair value adjustment associated with the embedded derivative was $1,054.

On September 28, 2007, the Operating Partnership entered into an amendment to the Contribution Agreement. Pursuant to the amendment, the maximum number of shares that can be issued upon redemption of the Preferred OP Units was set at 116 million, after which the Company will have no further obligations with respect to the redeemed or any other remaining Preferred OP Units. As a result of this amendment, and in accordance with the above referenced guidance, the Preferred OP Units are no longer considered a hybrid instrument and the previously identified embedded derivative no longer requires bifurcation and is considered permanent equity of the Operating Partnership and is included on the balance sheet as the minority interest represented by Preferred Operating Partnership units.

16. MINORITY INTEREST IN OPERATING PARTNERSHIP

The Company s interest in its properties is held through the Operating Partnership. ESS Holding Business Trust I, a wholly owned subsidiary of the Company, is the sole general partner of the Operating Partnership. The Company, through ESS Holding Business Trust II, a wholly owned subsidiary of the Company, is also a limited partner of the Operating Partnership. Between its general partner and limited partner interests, the Company held a 92.86% majority ownership interest therein as of September 30, 2007. The remaining ownership interests in the Operating Partnership (including Preferred OP Units) of 7.14% are held by certain former owners of assets acquired by the Operating Partnership, which includes a director and certain officers of the Company.

The minority interest in the Operating Partnership represents OP Units that are not owned by the Company. In conjunction with the formation of the Company and as a result of subsequent acquisitions, certain persons and entities contributing interests in properties to the Operating Partnership received limited partnership units in the form of either OP Units or Contingent Conversion Units. Limited partners who received OP Units in the formation transactions or in exchange for contributions for interests in properties have the right to require the Operating Partnership to redeem part or all of their OP Units for cash based upon the fair market value of an equivalent number of shares of the Company s common stock at the time of the redemption. Alternatively, the Company may, at its option, elect to acquire those OP Units in exchange for shares of its common stock on a one-for-one basis, subject to anti-dilution adjustments provided in the Operating Partnership agreement.

As of September 30, 2007, the Operating Partnership had 4,032,577 and 154,109 OP Units and CCUs outstanding, respectively.

Unlike the OP Units, CCUs do not carry any voting rights. Upon the achievement of certain performance thresholds relating to 14 early-stage lease-up properties, all or a portion of the CCUs will be automatically converted into OP Units. Initially, each CCU will be convertible on a one-for-one basis into OP Units, subject to customary anti-dilution adjustments. Beginning with the quarter ended March 31, 2006, and ending with the quarter ending December 31, 2008, the Company will calculate the net operating income from the 14 wholly-owned early-stage lease-up properties over the 12-month period ending in such quarter. Within 35 days following the end of each quarter referred to above, some or all of the CCUs will be converted so that the total percentage (not to exceed 100%) of CCUs issued in connection with the formation transactions that have been converted to OP Units will be equal to the percentage determined by dividing the net operating income for such period in excess of $5.1 million by $4.6 million. If

any CCUs remain unconverted through the calculation made in respect of the 12-month period ending December 31, 2008, such outstanding CCUs will be cancelled.

While any CCUs remain outstanding, a majority of the Company s independent directors must review and approve the net operating income calculation for each measurement period and also must approve any sales of any of the 14 wholly-owned early-stage lease-up properties.

As of September 30, 2007, there were 45,937 CCUs converted to OP Units. Based on the performance of the properties as of September 30, 2007, an additional 24,677 CCUs became eligible for conversion. The board of directors approved the conversion of these CCUs on November 1, 2007 as per the Company s charter, and the units were issued on November 5, 2007.

17. STOCKHOLDERS EQUITY

On September 28, 2007, in connection with an amendment to the Contribution Agreement (see Note 15) the Company amended its charter to increase the authorized number of shares of common stock of the Company from 200,000,000 to 300,000,000. The Company s charter now provides that it can issue up to 300,000,000 shares of common stock, $0.01 par value per share, 4,100,000 Contingent Conversion Shares, $.01 par value per share, and 50,000,000 shares of preferred stock, $0.01 par value per share. As of September 30, 2007, 65,276,108 shares of common stock were issued and outstanding, 2,995,845 CCSs were issued and outstanding and no shares of preferred stock were issued and outstanding. All stockholders of the Company s common stock are entitled to receive dividends and to one vote on all matters submitted to a vote of stockholders.

Unlike the Company s shares of common stock, CCSs do not carry any voting rights. Upon the achievement of certain performance thresholds relating to 14 early-stage lease-up properties, all or a portion of the CCSs will be automatically converted into shares of the Company s common stock. Initially, each CCS will be convertible on a one-for-one basis into shares of common stock, subject to customary anti-dilution adjustments. Beginning with the quarter ended March 31, 2006, and ending with the quarter ending December 31, 2008, the Company will calculate the net operating income from the 14 wholly-owned early-stage lease-up properties over the 12-month period ending in such quarter. Within 35 days following the end of each quarter referred to above, some or all of the CCSs will be converted so that the total percentage (not to exceed 100%) of CCSs issued in connection with the formation transactions that have been converted to common stock will be equal to the percentage determined by dividing the net operating income for such period in excess of $5.1 million by $4.6 million. If any CCSs remain unconverted through the calculation made in respect of the 12-month period ending December 31, 2008, such outstanding CCSs will be cancelled and restored to the status of authorized but unissued shares of common stock.

While any CCSs remain outstanding, a majority of the Company s independent directors must review and approve the net operating income calculation for each measurement period and also must approve any sales of any of the 14 wholly-owned early-stage lease-up properties.

As of September 30, 2007, there were 892,998 CCSs converted to common stock. Based on the performance of the properties as of September 30, 2007, an additional 479,730 CCSs became eligible for conversion. The board of directors approved the conversion of these CCSs on November 1, 2007 as per the Company s charter, and the shares were issued on November 5, 2007.

On October 29, 2007, the Company s Board of Directors approved an increase in the Company s annual dividend to $1.00 per common share to be paid quarterly at the rate of $0.25 per common share starting in the fourth quarter of 2007.

18. STOCK-BASED COMPENSATION

Options

The Company has the following two stock option plans under which shares were available for grant at September 30, 2007: 1) the 2004 Long-Term Incentive Compensation Plan, and 2) the 2004 Non-Employee Directors Share Plan. Under the terms of the plans, the exercise price of an option is the fair value of the stock on the date of grant. Each option becomes exercisable after the period or periods specified in the award agreement, which generally do not exceed 10 years from the date of grant. Options are exercisable at such times and subject to such terms as determined by the Compensation, Nominating and Governance Committee; options may not be exercised if such exercise would cause a violation of the ownership limit in the Company s charter. Unless otherwise determined by the Compensation, Nominating and Governance

Committee at the time of grant, stock options vest ratably over a four-year periodbeginning on the date of grant.

The following assumptions were used to estimate the fair value of options granted during the nine months ended September 30, 2007 and 2006 using the Black-Scholes option-pricing model:

	Nine Months Ended September 30,	
	2007	2006
Expected volatility	24%	24%
Dividend yield	5.8%	6.4%
Risk-free interest rate	4.2%	4.6%
Average expected term (years)	5	5

The Black-Scholes model incorporates assumptions to value stock-based awards. The risk-free rate is based on the U.S. Treasury yield curve in effect at the time of grant for the estimated life of the option. The Company uses actual historical data to calculate the expected price volatility and average expected term. The forfeiture rate, which is estimated at a weighted average of 20.65% of unvested options outstanding as of September 30, 2007, is adjusted periodically based on the extent to which actual forfeitures differ, or are expected to differ, from the previous estimate.

The following table summarizes the Company s activities with respect to its stock option plans:

Options	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value as of September 30, 2007
Outstanding at December 31, 2006	2,564,563	$ 13.92		
Granted	418,000	18.51		
Exercised	(99,290)	13.55		
Forfeited	(161,609)	14.56		
Outstanding at September 30, 2007	2,721,664	$ 14.55	7.54	$ 3,757,019
Vested and Expected to Vest	2,085,677	$ 14.28	7.41	$ 3,192,279
Ending Exercisable	1,345,343	$ 13.59	7.04	$ 2,522,751