CORPORATE OFFICE PROPERTIES TRUST
Form 10-Q
August 08, 2008
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 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 June 30, 2008

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 1-14023

Corporate Office Properties Trust

(Exact name of registrant as specified in its charter)

Maryland	**23-2947217**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
6711 Columbia Gateway Drive, Suite 300, Columbia, MD	**21046**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code: **(443) 285-5400**

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.

x Yes o No

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) o Yes x No

As of July 29, 2008, 47,705,998 of the Company s Common Shares of Beneficial Interest, $0.01 par value, were issued and outstanding.

Table of Contents

TABLE OF CONTENTS

FORM 10-Q

		PAGE
PART I:	**FINANCIAL INFORMATION**	
Item 1:	Financial Statements:	
	Consolidated Balance Sheets as of June 30, 2008 and December 31, 2007 (unaudited)	3

Consolidated Statements of Operations for the three and six months ended June 30, 2008 and 2007 (unaudited) 4

Consolidated Statements of Cash Flows for the six months ended June 30, 2008 and 2007 (unaudited)	5

Notes to Consolidated Financial Statements 6

Item 2:	Management s Discussion and Analysis of Financial Condition and Results of Operations	27

Item 3:	Quantitative and Qualitative Disclosures About Market Risk	43
Item 4:	Controls and Procedures	43

PART II:	OTHER INFORMATION	
Item 1:	Legal Proceedings	44

Item 1A:	Risk Factors	44

Item 2:	Unregistered Sales of Equity Securities and Use of Proceeds	44

Item 3:	Defaults Upon Senior Securities	44

Item 4:	Submission of Matters to a Vote of Security Holders	45

Item 5:	Other Information	45

Item 6:	Exhibits	46

SIGNATURES 47

2

Table of Contents

PART I: FINANCIAL INFORMATION

ITEM 1. Financial Statements

Corporate Office Properties Trust and Subsidiaries

Consolidated Balance Sheets

(Dollars in thousands)

(unaudited)

	June 30, 2008	December 31, 2007
Assets		
Investment in real estate:		
Operating properties, net	$ 2,245,003	$ 2,192,939
Property held for sale, net		14,988
Projects under construction or development	456,164	396,012
Total commercial real estate properties, net	2,701,167	2,603,939
Cash and cash equivalents	12,857	24,638
Restricted cash	23,066	15,121
Accounts receivable, net	23,452	24,831
Deferred rent receivable	59,238	53,631
Intangible assets on real estate acquisitions, net	104,136	108,661
Deferred charges, net	48,620	49,051
Prepaid expenses and other assets	37,934	51,981
Total assets	$ 3,010,470	$ 2,931,853
Liabilities and shareholders equity		
Liabilities:		
Mortgage and other loans payable	$ 1,704,351	$ 1,625,842
3.5% Exchangeable Senior Notes	200,000	200,000
Accounts payable and accrued expenses	82,526	75,535
Rents received in advance and security deposits	32,569	31,234
Dividends and distributions payable	22,548	22,441
Deferred revenue associated with acquired operating leases	12,762	11,530
Distributions in excess of investment in unconsolidated real estate joint venture	4,506	4,246
Other liabilities	8,820	8,288
Total liabilities	2,068,082	1,979,116
Minority interests:		
Common units in the Operating Partnership	111,033	114,127
Preferred units in the Operating Partnership	8,800	8,800
Other consolidated real estate joint ventures	10,259	7,168
Total minority interests	130,092	130,095
Commitments and contingencies (Note 20)		
Shareholders equity:		
Preferred Shares of beneficial interest ($0.01 par value; shares authorized of 15,000,000, issued and outstanding of 8,121,667 at June 30, 2008 and December 31, 2007 (Note 13))	81	81
Common Shares of beneficial interest ($0.01 par value; 75,000,000 shares authorized, shares issued and outstanding of 47,701,812 at June 30, 2008 and 47,366,475 at December 31,	477	474

2007)				
Additional paid-in capital		956,683		950,615
Cumulative distributions in excess of net income		(142,330)		(126,156)
Accumulated other comprehensive loss		(2,615)		(2,372)
Total shareholders equity		812,296		822,642
Total liabilities and shareholders equity	$	3,010,470	$	2,931,853

See accompanying notes to consolidated financial statements.

Table of Contents

Corporate Office Properties Trust and Subsidiaries

Consolidated Statements of Operations

(Dollars in thousands, except per share data)

(unaudited)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
Revenues				
Rental revenue	$ 83,154	$ 78,337	$ 164,864	$ 153,612
Tenant recoveries and other real estate operations revenue	14,957	12,037	30,398	25,630
Construction contract revenues	14,619	10,620	23,133	19,311
Other service operations revenues	525	1,073	1,003	2,459
Total revenues	113,255	102,067	219,398	201,012
Expenses				
Property operating expenses	33,957	29,032	68,499	60,591
Depreciation and other amortization associated with real estate operations	24,955	26,834	49,847	52,786
Construction contract expenses	14,192	10,136	22,475	18,619
Other service operations expenses	454	1,126	1,056	2,531
General and administrative expenses	6,036	5,326	11,969	10,203
Total operating expenses	79,594	72,454	153,846	144,730
Operating income	33,661	29,613	65,552	56,282
Interest expense	(19,437)	(20,437)	(39,746)	(40,213)
Amortization of deferred financing costs	(910)	(921)	(1,713)	(1,805)
Gain on sale of non-real estate investment	5	1,033	51	1,033
Income from continuing operations before equity in loss of unconsolidated entities, income taxes and minority interests	13,319	9,288	24,144	15,297
Equity in loss of unconsolidated entities	(56)	(57)	(110)	(151)
Income tax benefit (expense)	107	(178)	(5)	(283)
Income from continuing operations before minority interests	13,370	9,053	24,029	14,863
Minority interests in income from continuing operations				
Common units in the Operating Partnership	(1,378)	(807)	(2,365)	(1,088)
Preferred units in the Operating Partnership	(165)	(165)	(330)	(330)
Other consolidated entities	(120)	31	(106)	78
Income from continuing operations	11,707	8,112	21,228	13,523
Income (loss) from discontinued operations, net of minority interests	1,115	(396)	2,187	(260)
Income before gain on sales of real estate	12,822	7,716	23,415	13,263
Gain on sales of real estate, net	31	161	833	161
Net income	12,853	7,877	24,248	13,424
Preferred share dividends	(4,026)	(4,025)	(8,051)	(8,018)
Net income available to common shareholders	$ 8,827	$ 3,852	$ 16,197	$ 5,406
Basic earnings per common share				
Income from continuing operations	$ 0.16	$ 0.09	$ 0.30	$ 0.12
Discontinued operations	0.03	(0.01)	0.04	
Net income available to common shareholders	$ 0.19	$ 0.08	$ 0.34	$ 0.12
Diluted earnings per common share				
Income from continuing operations	$ 0.16	$ 0.09	$ 0.29	$ 0.12

Discontinued operations		0.02		(0.01)		0.05		(0.01)
Net income available to common shareholders	$	0.18	$	0.08	$	0.34	$	0.11
Dividends declared per common share	$	0.34	$	0.31	$	0.68	$	0.62

See accompanying notes to consolidated financial statements.

Table of Contents

Corporate Office Properties Trust and Subsidiaries

Consolidated Statements of Cash Flows

(Dollars in thousands)

(unaudited)

	For the Six Months Ended June 30, 2008	2007
Cash flows from operating activities		
Net income	$ 24,248	$ 13,424
Adjustments to reconcile net income to net cash provided by operating activities:		
Minority interests	3,461	1,325
Depreciation and other amortization	50,676	54,055
Amortization of deferred financing costs	1,713	1,805
Amortization of deferred market rental revenue	(903)	(985)
Equity in loss of unconsolidated entities	110	151
Gain on sales of real estate	(4,204)	(183)
Gain on sale of non-real estate investment	(51)	(1,033)
Share-based compensation	4,556	3,141
Excess income tax benefits from share-based compensation	(1,053)	
Changes in operating assets and liabilities:		
Increase in deferred rent receivable	(5,701)	(5,936)
Decrease in accounts receivable	1,379	7,541
Decrease (increase) in restricted cash and prepaid and other assets	3,380	(10,274)
Increase (decrease) in accounts payable, accrued expenses and other liabilities	4,406	(4,037)
Increase in rents received in advance and security deposits	1,335	6,310
Other	268	(370)
Net cash provided by operating activities	83,620	64,934
Cash flows from investing activities		
Purchases of and additions to commercial real estate properties	(149,358)	(243,936)
Proceeds from sales of properties	28,304	
Leasing costs paid	(2,383)	(8,164)
(Increase) decrease in restricted cash associated with investing activities	(425)	14,838
Other	(2,079)	1,091
Net cash used in investing activities	(125,941)	(236,171)
Cash flows from financing activities		
Proceeds from mortgage and other loans payable	227,932	431,495
Repayments of mortgage and other loans payable	(149,374)	(216,352)
Deferred financing costs paid	(2,250)	(1,556)
Net proceeds from issuance of common shares	1,350	6,140
Dividends paid	(40,309)	(35,523)
Distributions paid	(5,878)	(5,505)
Excess income tax benefits from share-based compensation	1,053	
Restricted share redemptions	(1,304)	
Other	(680)	(262)
Net cash provided by financing activities	30,540	178,437
Net (decrease) increase in cash and cash equivalents	(11,781)	7,200

Cash and cash equivalents				
Beginning of period		24,638		7,923
End of period	$	12,857	$	15,123

See accompanying notes to consolidated financial statements.

Table of Contents

Corporate Office Properties Trust and Subsidiaries

Notes to Consolidated Financial Statements

(Dollars in thousands, except per share data)

(unaudited)

1. Organization

Corporate Office Properties Trust (COPT) and subsidiaries (collectively, the Company , we or us) is a specialty office real estate investment trus (REIT) that focuses on strategic customer relationships and specialized tenant requirements in the United States Government, defense information technology and data sectors. We acquire, develop, manage and lease properties that are typically concentrated in large office parks primarily located adjacent to government demand drivers and/or in demographically strong markets possessing growth opportunities. As of June 30, 2008, our investments in real estate included the following:

- 234 wholly owned operating properties totaling 18.2 million square feet;
- 18 wholly owned properties under construction or development that we estimate will total approximately 1.8 million square feet upon completion;
- wholly owned land parcels totaling 1,457 acres that we believe are potentially developable into approximately 12.1 million square feet; and
- partial ownership interests in a number of other real estate projects in operation or under development or redevelopment.

We conduct almost all of our operations through our operating partnership, Corporate Office Properties, L.P. (the Operating Partnership), for which we are the managing general partner. The Operating Partnership owns real estate both directly and through subsidiary partnerships and limited liability companies (LLCs). A summary of our Operating Partnership s forms of ownership and the percentage of those securities owned by COPT as of June 30, 2008 follows:

Common Units	85%
Series G Preferred Units	100%
Series H Preferred Units	100%
Series I Preferred Units	0%
Series J Preferred Units	100%
Series K Preferred Units	100%

Three of our trustees also controlled at that date, either directly or through ownership by other entities or family members, 13% of the Operating Partnership s common units.

In addition to owning interests in real estate, the Operating Partnership also owns 100% of Corporate Office Management, Inc. (COMI) and owns, either directly or through COMI, 100% of the consolidated subsidiaries that are set forth below (collectively defined as the Service Companies):

Entity Name	Type of Service Business
COPT Property Management Services, LLC (CPM)	Real Estate Management
COPT Development & Construction Services, LLC (CDC)	Construction and Development
Corporate Development Services, LLC (CDS)	Construction and Development
COPT Environmental Systems, LLC (CES)	Heating and Air Conditioning

Most of the services that CPM provides are for us. CDC, CDS and CES provide services to us and to third parties.

Table of Contents

2. Basis of Presentation

The accompanying unaudited interim Consolidated Financial Statements have been prepared in accordance with the rules and regulations for reporting on Form 10-Q. Accordingly, certain information and disclosures required by accounting principles generally accepted in the United States for complete Consolidated Financial Statements are not included herein. These interim financial statements should be read together with the financial statements and notes thereto included in our 2007 Annual Report on Form 10-K. The interim financial statements reflect all adjustments that we believe are necessary for the fair statement of our financial position and results of operations for the interim periods presented. These adjustments are of a normal recurring nature. The results of operations for such interim periods are not necessarily indicative of the results for a full year.

We reclassified certain amounts from the prior period to conform to the current period presentation of our Consolidated Financial Statements. These reclassifications did not affect previously reported consolidated net income or shareholders equity.

3. Earnings Per Share (EPS)

We present both basic and diluted EPS. We compute basic EPS by dividing net income available to common shareholders by the weighted average number of common shares of beneficial interest (common shares) outstanding during the period. Our computation of diluted EPS is similar except that:

- the denominator is increased to include: (1) the weighted average number of potential additional common shares that would have been outstanding if securities that are convertible into our common shares were converted; and (2) the effect of dilutive potential common shares outstanding during the period attributable to share-based compensation using the treasury stock method; and
- the numerator is adjusted to add back any changes in income or loss that would result from the assumed conversion into common shares that we added to the denominator.

Our computation of diluted EPS does not assume conversion of securities into our common shares if conversion of those securities would increase our diluted EPS in a given period. A summary of the numerator and denominator for purposes of basic and diluted EPS calculations is set forth below (dollars and shares in thousands, except per share data):

Table of Contents

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
Numerator:				
Income from continuing operations	$ 11,707	$ 8,112	$ 21,228	$ 13,523
Add: Gain on sales of real estate, net	31	161	833	161
Less: Preferred share dividends	(4,026)	(4,025)	(8,051)	(8,018)
Numerator for basic and diluted EPS from continuing operations	7,712	4,248	14,010	5,666
Income (loss) from discontinued operations, net	1,115	(396)	2,187	(260)
Numerator for basic and diluted EPS on net income available to common shareholders	$ 8,827	$ 3,852	$ 16,197	$ 5,406
Denominator (all weighted averages):				
Denominator for basic EPS (common shares)	47,110	46,686	47,055	46,185
Dilutive effect of share-based compensation awards	888	1,105	797	1,305
Denominator for diluted EPS	47,998	47,791	47,852	47,490
Basic EPS:				
Income from continuing operations	$ 0.16	$ 0.09	$ 0.30	$ 0.12
Income (loss) from discontinued operations	0.03	(0.01)	0.04	
Net income available to common shareholders	$ 0.19	$ 0.08	$ 0.34	$ 0.12
Diluted EPS:				
Income from continuing operations	$ 0.16	$ 0.09	$ 0.29	$ 0.12
Income (loss) from discontinued operations	0.02	(0.01)	0.05	(0.01)
Net income available to common shareholders	$ 0.18	$ 0.08	$ 0.34	$ 0.11

Our diluted EPS computations do not include the effects of the following securities since the conversions of such securities would increase diluted EPS for the respective periods:

	Weighted Average Shares in Denominator			
	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
Conversion of weighted average common units	8,151	8,313	8,153	8,361
Conversion of weighted average convertible preferred shares	434	434	434	415
Conversion of weighted average convertible preferred units	176	176	176	176

The 3.5% Exchangeable Senior Notes did not affect our diluted EPS reported above since the weighted average closing price of our common shares during each of the periods was less than the exchange price per common share applicable for such periods.

4. Recent Accounting Pronouncements

SFAS 157

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. The Statement does not require or permit any new fair value measurements but does apply under other accounting pronouncements that require or permit fair value measurements. The changes to current practice resulting from the Statement relate to the definition of fair value, the methods used to measure fair value and the expanded disclosures about fair value measurements. With respect to SFAS 157, the FASB also issued FASB Staff Position SFAS 157-1, Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13 (FSP FAS 157-1) and FASB Staff Position SFAS 157-2, Effective Date of FASB Statement No. 157 (FSP FAS 157-2). FSP FAS 157-1 amends SFAS 157 to exclude from the scope of SFAS 157 certain leasing transactions accounted for under Statement of Financial

Table of Contents

Accounting Standards No. 13, Accounting for Leases. FSP FAS 157-2 amends SFAS 157 to defer the effective date of SFAS 157 for all non-financial assets and non-financial liabilities except those that are recognized or disclosed at fair value in the financial statements on a recurring basis to fiscal years beginning after November 15, 2008. Effective January 1, 2008, we adopted, on a prospective basis, the portions of SFAS 157 not deferred by FSP FAS 157-2; this adoption did not have a material effect on our financial position, results of operations or cash flows. We are evaluating the impact that SFAS 157 will have on our non-financial assets and non-financial liabilities since the application of SFAS 157 for such items for us was deferred to January 1, 2009.

Under SFAS 157, fair value is defined as the exit price, or the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants as of the measurement date. SFAS 157 also establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are inputs market participants would use in valuing the asset or liability developed based on market data obtained from sources independent of us. Unobservable inputs are inputs that reflect our assumptions about the factors market participants would use in valuing the asset or liability developed based upon the best information available in the circumstances. The hierarchy of these inputs is broken down into three levels: Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities; Level 2 inputs include (1) quoted prices for similar assets or liabilities in active markets, (2) quoted prices for identical or similar assets or liabilities in markets that are not active and (3) inputs (other than quoted prices) that are observable for the asset or liability, either directly or indirectly; and Level 3 inputs are unobservable inputs for the asset or liability. Categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

The assets held in connection with our non-qualified elective deferred compensation plan and the corresponding liability to the participants are measured at fair value on a recurring basis on our consolidated balance sheet using quoted market prices. The assets are treated as trading securities for accounting purposes and included in restricted cash on our consolidated balance sheet. The offsetting liability is adjusted to fair value at the end of each accounting period based on the fair value of the plan assets and reported in other liabilities in our consolidated balance sheet. The assets and corresponding liability of our non-qualified elective deferred compensation plan are classified in Level 1 of the fair value hierarchy.

The valuation of our derivatives is determined using widely accepted valuation techniques, including discounted cash flow analysis on the expected cash flows of each derivative. This analysis reflects the contractual terms of the derivatives, including the period to maturity, and uses observable market-based inputs, including interest rate market data and implied volatilities in such interest rates. While we determined that the majority of the inputs used to value our derivatives fall within Level 2 of the fair value hierarchy under SFAS 157, the credit valuation adjustments associated with our derivatives also utilize Level 3 inputs, such as estimates of current credit spreads to evaluate the likelihood of default. However, as of June 30, 2008, we assessed the significance of the impact of the credit valuation adjustments on the overall valuation of our derivatives and determined that these adjustments are not significant to the overall valuation of our derivatives. As a result, we determined that our derivative valuations in their entirety are classified in Level 2 of the fair value hierarchy.

The table below sets forth our financial assets and liabilities that are accounted for at fair value on a recurring basis as of June 30, 2008:

Description	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Total**
Assets:				
Deferred compensation plan assets (1)	$ 6,331	$	$	$ 6,331
Liabilities:				

Deferred compensation plan liability (2)	$	6,331	$		$		$	6,331
Interest rate swap contracts (2)				2,648				2,648
Liabilities	$	6,331	$	2,648	$		$	8,979

---

(1) Included in the line entitled restricted cash on our Consolidated Balance Sheet.

(2) Included in the line entitled other liabilities on our Consolidated Balance Sheet.

Table of Contents

Other Recent Accounting Pronouncements

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (SFAS 159). SFAS 159 permits entities to choose to measure many financial assets and financial liabilities at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. We adopted SFAS 159 on a prospective basis effective January 1, 2008. Our adoption of SFAS 159 did not have a material effect on our financial position, results of operations or cash flows since we did not elect to apply the fair value option for any of our eligible financial instruments or other items on the January 1, 2008 effective date.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141(R), Business Combinations (SFAS 141(R)). SFAS 141(R) requires the acquiring entity in a business combination to recognize all (and only) the assets acquired and liabilities assumed in the transactions; establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed; and requires the acquirer to disclose to investors and other users all of the information they need to evaluate and understand the nature and financial effect of the business combination. SFAS 141(R) is effective for fiscal years beginning after December 15, 2008. While we are currently assessing the impact of SFAS 141(R) on our consolidated financial position and results of operations, SFAS 141(R) will require us to expense transaction costs associated with property acquisitions occurring subsequent to the pronouncment s effective date, which is a significant change since our current practice is to capitalize such costs into the cost of the acquisitions.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 160, Noncontrolling Interests in Consolidated Financial Statements (SFAS 160). SFAS 160 requires all entities to report noncontrolling (minority) interests in subsidiaries as equity in the consolidated financial statements. SFAS 160 is effective for fiscal years beginning after December 15, 2008. We are currently assessing the impact of SFAS 160 on our consolidated financial position and results of operations.

In March 2008, the FASB issued Statement of Financial Accounting Standards No. 161 Disclosures about Derivative Instruments and Hedging Activities (SFAS 161). This new standard expands the disclosure requirements for derivative instruments and for hedging activities in order to provide users of financial statements with an enhanced understanding of: (1) how and why an entity uses derivative instruments; (2) how derivative instruments and related hedged items are accounted for under Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities and its related interpretations; and (3) how derivative instruments and related hedged items affect an entity s financial position, financial performance, and cash flows. SFAS 161 is to be applied prospectively for the first annual reporting period beginning on or after November 15, 2008. We are evaluating the impact that SFAS 161 will have on our reporting for derivatives.

In May 2008, the FASB issued FASB Staff Position No. APB 14-1, Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement) (FSP APB-14-1). FSP APB-14-1 requires that the initial proceeds from convertible debt instruments that may be settled in cash, including partial cash settlements, be allocated between a liability component and an equity component associated with the embedded conversion option. This pronouncement s objective is to require the liability and equity components of convertible debt to be separately accounted for in order to enable interest expense to be recorded at a rate that would reflect the issuer s conventional debt borrowing rate (previously, interest expense on such debt was recorded based on the contractual rate of interest under the debt). Under this pronouncement, the liability component is recorded at its fair value, as calculated based on the present value of its cash flows discounted using the issuer s conventional debt borrowing rate. The equity component is recorded based on the difference between the debt proceeds and the fair value of the liability. The difference between the liability s principal amount and fair value is reported as a debt discount and amortized as interest expense over the debt s expected life using the effective interest method. The provisions of FSP APB 14-1 will be effective beginning January 1, 2009 and are to be applied retrospectively to all periods presented. While we are in the process of evaluating FSP APB 14-1, we currently believe that this pronouncement will affect the accounting for our 3.5% Exchangeable Senior Notes by resulting in our recognition of additional annual interest expense of approximately $3,000 to $4,000 over the five-year expected life of the debt, beginning on the debt s

September 18, 2006 origination date.

Table of Contents

5. Commercial Real Estate Properties

Operating properties consisted of the following:

	June 30, 2008	December 31, 2007
Land	$ 420,182	$ 413,779
Buildings and improvements	2,145,700	2,064,960
	2,565,882	2,478,739
Less: accumulated depreciation	(320,879)	(285,800)
	$ 2,245,003	$ 2,192,939

As of December 31, 2007, 429 Ridge Road, an office property located in Dayton, New Jersey that we were under contract to sell for $17,000, was classified as held for sale (Dayton, New Jersey is located in the Northern/Central New Jersey Region). We completed the sale of this property on January 31, 2008. The components associated with 429 Ridge Road as of December 31, 2007 included the following:

	December 31, 2007
Land	$ 2,932
Buildings and improvements	15,003
	17,935
Less: accumulated depreciation	(2,947)
	$ 14,988

Projects we had under construction or development consisted of the following:

	June 30, 2008	December 31, 2007
Land	$ 208,742	$ 214,696
Construction in progress	247,422	181,316
	$ 456,164	$ 396,012

2008 Acquisitions

We acquired the following office properties during the six months ended June 30, 2008:

Project Name	Location	Date of Acquisition	Number of Buildings	Total Rentable Square Feet		Acquisition Cost
3535 Northrop Grumman Point	Colorado Springs, CO	6/10/2008	1	124,305	$	23,240
1560 Cable Ranch Road (Buildings A and B)	San Antonio, TX	6/19/2008	2	122,975		17,317
			3	247,280	$	40,557

The table below sets forth the allocation of the acquisition costs of the three properties:

	3535 Northrop Grumman Point	1560 Cable Ranch Road	Total
Land, operating properties	$	$ 3,396	$ 3,396
Building and improvements	22,163	10,315	32,478
Intangible assets on real estate acquisitions	3,423	4,208	7,631
Total assets	25,586	17,919	43,505
Deferred revenue associated with acquired operating leases	(2,346)	(602)	(2,948)
Total acquisition cost	$ 23,240	$ 17,317	$ 40,557

Table of Contents

Intangible assets recorded in connection with the above acquisitions included the following:

			Weighted Average Amortization Period (in Years)
Lease-up value	$	4,558	10
Tenant relationship value		1,537	12
Lease cost portion of deemed cost avoidance		1,536	11
	$	7,631	11

2008 Construction, Development and Redevelopment Activities

During the six months ended June 30, 2008, we had five properties totaling 437,064 square feet become fully operational (89,497 of these square feet were placed into service in 2007). Three of these properties are located in Colorado Springs, Colorado (Colorado Springs) and two in the Baltimore/Washington Corridor.

As of June 30, 2008, we had construction underway on four new properties in the Baltimore/Washington Corridor (including one through a joint venture), four in Colorado Springs, two in San Antonio, Texas (San Antonio) and one in the Suburban Maryland region through a joint venture. We also had development activities underway on three new properties in Suburban Baltimore, two each in the Baltimore/Washington Corridor, San Antonio and Suburban Maryland (including one through a joint venture) and one in King George County, Virginia. In addition, we had redevelopment underway on two properties owned by a joint venture (one located in the Baltimore/Washington Corridor and the other in Northern Virginia).

2008 Dispositions

We sold the following operating properties during the six months ended June 30, 2008:

Project Name	Location	Date of Sale	Number of Buildings	Total Rentable Square Feet	Sale Price	Gain on Sale
429 Ridge Road	Dayton, New Jersey	1/31/2008	1	142,385	$ 17,000	$ 1,365
7253 Ambassador Road	Woodlawn, Maryland	6/2/2008	1	38,930	5,100	1,278
47 Commerce Road	Cranbury, New Jersey	4/1/2008	1	41,398	3,150	
			3	222,713	$ 25,250	$ 2,643

During the six months ended June 30, 2008, we also completed the sale of six recently constructed office condominiums located in Herndon Virginia (located in the Northern Virginia region) for sale prices totaling $8,388 in the aggregate. We recognized an aggregate gain before minority interests and taxes of $1,368 on these sales.

The table below sets forth the components of the line on our Consolidated Statements of Operations entitled gain on sales of real estate for the three and six months ended June 30, 2008:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
Gain on sales of real estate	$ 46	$ 194	$ 1,678	$ 194
Income taxes	(5)	(3)	(578)	(3)
Minority interests				
Common units in the Operating Partnership	(8)	(30)	(151)	(30)
Other consolidated entities	(2)		(116)	
Gain on sale of real estate, net	$ 31	$ 161	$ 833	$ 161

Table of Contents

6. Real Estate Joint Ventures

During the six months ended June 30, 2008, we had an investment in one unconsolidated real estate joint venture accounted for using the equity method of accounting. Information pertaining to this joint venture investment is set forth below.

	Investment Balance at						
	June 30, 2008	December 31, 2007	Date Acquired	Ownership	Nature of Activity	Total Assets at 6/30/2008	Maximum Exposure to Loss (1)
Harrisburg Corporate Gateway Partners, L.P.	$ (4,506)(2)	$ (4,246)(2)	9/29/2005	20%	Operates 16 buildings (3)	$ 71,261	$

(1) Derived from the sum of our investment balance and maximum additional unilateral capital contributions or loans required from us. Not reported above are additional amounts that we and our partner are required to fund when needed by this joint venture; these funding requirements are proportional to our respective ownership percentages. Also not reported above are additional unilateral contributions or loans from us, the amounts of which are uncertain, which we would be required to make if certain contingent events occur.

(2) The carrying amount of our investment in this joint venture was lower than our share of the equity in the joint venture by $5,196 at June 30, 2008 and December 31, 2007 due to our deferral of gain on the contribution by us of real estate into the joint venture upon its formation. A difference will continue to exist to the extent the nature of our continuing involvement in the joint venture remains the same.

(3) This joint venture s properties are located in Greater Harrisburg, Pennsylvania.

The following table sets forth condensed balance sheets for Harrisburg Corporate Gateway Partners, L.P.:

	June 30, 2008	December 31, 2007
Commercial real estate property	$ 62,961	$ 63,773
Other assets	8,300	9,051
Total assets	$ 71,261	$ 72,824
Liabilities	$ 67,799	$ 67,991
Owners equity	3,462	4,833
Total liabilities and owners equity	$ 71,261	$ 72,824

The following table sets forth condensed statements of operations for Harrisburg Corporate Gateway Partners, L.P.:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
Revenues	$ 2,413	$ 2,426	$ 4,796	$ 4,870
Property operating expenses	(876)	(876)	(1,701)	(1,836)
Interest expense	(980)	(980)	(1,960)	(2,118)
Depreciation and amortization expense	(830)	(855)	(1,660)	(1,722)
Net loss	$ (273)	$ (285)	$ (525)	$ (806)

On January 29, 2008, we completed the formation of M Square Associates, LLC (M Square), a consolidated joint venture in which we hold a 50% equity interest through Enterprise Campus Developer, LLC, another consolidated joint venture in which we own a 90% interest. M Square was formed to develop and own office properties, approved for up to approximately 750,000 square feet, located in M Square Research Park in College Park, Maryland (located in the Suburban Maryland region).

The table below sets forth information pertaining to our investments in consolidated joint ventures at June 30, 2008:

Table of Contents

	Date Acquired	Ownership % at 6/30/2008	Nature of Activity		Total Assets at 6/30/2008	Collateralized Assets at 6/30/2008
COPT Opportunity Invest I, LLC	12/20/2005	92.5%	Redeveloping two properties(1)	$	43,252	$
Arundel Preserve #5, LLC	7/2/2007	50.0%	Developing land parcel(2)		26,113	
Enterprise Campus Developer, LLC	6/26/2007	90.0%	Developing land parcels(3)		24,317	
COPT-FD Indian Head, LLC	10/23/2006	75.0%	Developing land parcel(4)		4,772	
MOR Forbes 2 LLC	12/24/2002	50.0%	Operates one building(5)		4,409	
13849 Park Center Road, LLC	10/2/2007	92.5%	Redeveloping one property(6)		542	
				$	103,405	$

(1) This joint venture owns one property in the Northern Virginia region and one in the Baltimore/Washington Corridor region.

(2) This joint venture is developing a land parcel located in Hanover, Maryland (located in the Baltimore/Washington Corridor).

(3) This joint venture is developing land parcels located in College Park, Maryland through the M Square joint venture.

(4) This joint venture s property is located in Charles County, Maryland (located in our other business segment).

(5) This joint venture s property is located in Lanham, Maryland (located in the Suburban Maryland region).

(6) This joint venture is redeveloping a property in the Northern Virginia region.

Our commitments and contingencies pertaining to our real estate joint ventures are disclosed in Note 20.

7. Intangible Assets on Real Estate Acquisitions

Intangible assets on real estate acquisitions consisted of the following:

	June 30, 2008						December 31, 2007					
	Gross Carrying Amount		Accumulated Amortization		Net Carrying Amount		Gross Carrying Amount		Accumulated Amortization		Net Carrying Amount	
Lease-up value	$	129,613	$	65,322	$	64,291	$	125,338	$	58,435	$	66,903
Tenant relationship value		36,514		10,623		25,891		35,189		7,892		27,297
Lease cost portion of deemed cost avoidance		18,587		9,828		8,759		17,133		8,697		8,436
Lease to market value		14,428		10,369		4,059		14,428		9,555		4,873
Market concentration premium		1,333		197		1,136		1,333		181		1,152
	$	200,475	$	96,339	$	104,136	$	193,421	$	84,760	$	108,661

Amortization of the intangible asset categories set forth above totaled $11,724 in the six months ended June 30, 2008 and $16,678 in the six months ended June 30, 2007. The approximate weighted average amortization periods of the categories set forth above follow: lease-up value: nine years; tenant relationship value: seven years; lease cost portion of deemed cost avoidance: six years; lease to market value: four years; and market concentration premium: 34 years. The approximate weighted average amortization period for all of the categories combined is nine years. Estimated amortization expense associated with the intangible asset categories set forth above is $10,500 for the six months ending December 31, 2008, $19,100 for 2009, $14,900 for 2010, $12,100 for 2011, $9,800 for 2012 and $7,300 for 2013.

8. Deferred Charges

Deferred charges consisted of the following:

	June 30, 2008	December 31, 2007
Deferred leasing costs	$ 64,946	$ 63,052
Deferred financing costs	34,874	32,617
Goodwill	1,853	1,853
Deferred other	155	155
	101,828	97,677
Accumulated amortization	(53,208)	(48,626)
Deferred charges, net	$ 48,620	$ 49,051

Table of Contents

9. Accounts Receivable

Our accounts receivable are reported net of an allowance for bad debts of $1,249 at June 30, 2008 and $798 at December 31, 2007.

10. Prepaid Expenses and Other Assets

Prepaid and other assets consisted of the following:

	June 30, 2008	December 31, 2007
Furniture, fixtures and equipment	$ 11,807	$ 11,410
Prepaid expenses	8,834	13,907
Construction contract costs incurred in excess of billings	8,031	19,425
Other assets	9,262	7,239
Prepaid expenses and other assets	$ 37,934	$ 51,981

11. Debt

Our debt consisted of the following:

	Maximum Principal Amount Under Debt at June 30, 2008	Carrying Value at June 30, 2008	Carrying Value at December 31, 2007	Stated Interest Rates at June 30, 2008	Scheduled Maturity Dates at June 30, 2008
Mortgage and other loans payable:					
Revolving Credit Facility	$ 600,000	$ 465,000	$ 361,000	LIBOR + 0.75% to 1.25%	September 30, 2011 (1)
Mortgage and Other Secured Loans					
Fixed rate mortgage loans (2)	N/A	1,063,596	1,124,551	5.20% - 8.63 (3)%	2008 - 2034 (4)
Revolving Construction Facility (5)	225,000	35,432		LIBOR + 1.60% to 2.00%	May 2, 2011 (1)
Other construction loan facilities	111,500	104,089	104,089	LIBOR + 1.40% to 1.50%	2008-2009
Other variable-rate secured loans	N/A	34,500	34,500	LIBOR + 1.20% to 1.50%	2008
Total mortgage and other secured loans		1,237,617	1,263,140		
Note payable					
Unsecured seller notes	N/A	1,734	1,702	0% - 5.95%	2008-2016
Total mortgage and other loans payable		1,704,351	1,625,842		
3.5% Exchangeable Senior Notes	N/A	200,000	200,000	3.50%	September 2026 (6)

Total debt	$ 1,904,351	$ 1,825,842

---

(1) These facilities may be extended for a one-year period at our option, subject to certain conditions.

(2) Several of the fixed rate mortgages carry interest rates that were above or below market rates upon assumption and therefore are recorded at their fair value based on applicable effective interest rates. The carrying values of these loans reflect net premiums totaling $556 at June 30, 2008 and $605 at December 31, 2007.

(3) The weighted average interest rate on these loans was 5.82% at June 30, 2008.

(4) A loan with a balance of $4,781 at June 30, 2008 that matures in 2034 may be repaid in March 2014, subject to certain conditions.

(5) This loan is described in further detail below.

(6) Refer to our 2007 Annual Report on Form 10-K for descriptions of provisions for early redemption and repurchase of these notes.

On May 2, 2008, we entered into a construction loan agreement with a group of lenders for which KeyBanc Capital Markets, Inc. acted as arranger, KeyBank National Association acted as administrative agent, Bank of America, N.A. acted as syndication agent and Manufacturers and Traders Trust Company acted as documentation agent; this loan is referred to in the table above as the Revolving Construction Facility. The construction loan agreement provides for an aggregate commitment by the lenders of $225,000, with a right for us to further increase the lenders aggregate commitment during the term to a maximum of $325,000, subject to certain conditions. Ownership interests in the properties for which construction costs are being financed through loans under the

Table of Contents

agreement are pledged as collateral. Borrowings are generally available for properties included in this construction loan agreement based on 85% of the total budgeted costs of construction of the applicable improvements for such properties as set forth in the properties construction budgets, subject to certain other loan-to-value and debt coverage requirements. As loans for properties under the construction loan agreement are repaid in full and the ownership interests in such properties are no longer pledged as collateral, capacity under the construction loan agreement s aggregate commitment will be restored, giving us the ability to obtain new loans for other construction properties in which we pledge the ownership interests as collateral. The construction loan agreement matures on May 2, 2011, and may be extended by one year at our option, subject to certain conditions. The variable interest rate on each loan is based on one of the following, to be selected by us: (1) subject to certain conditions, the LIBOR rate for the interest period designated by us (customarily the 30-day rate) plus 1.6% to 2.0%, as determined by our leverage levels at different points in time; or (2) the greater of (a) the prime rate of the lender then acting as agent or (b) the Federal Funds Rate, as defined in the construction loan agreement, plus 0.50%. Interest is payable at the end of each interest period (as defined in the agreement), and principal outstanding under each loan under the agreement is payable on the maturity date. The construction loan agreement also carries a quarterly fee that is based on the unused amount of the commitment multiplied by a per annum rate of 0.125% to 0.20%.

We capitalized interest costs of $8,957 in the six months ended June 30, 2008 and $8,906 in the six months ended June 30, 2007.

12. Derivatives

The following table sets forth our interest rate swap contracts in place during the six months ended June 30, 2008 and their respective fair values:

Notional Amount	One-Month LIBOR Base	Effective Date	Expiration Date	Fair Value at June 30, 2008	Fair Value at December 31, 2007
$ 50,000	4.3300%	10/23/2007	10/23/2009	$ (836)	$ (596)
50,000	5.0360%	3/28/2006	3/30/2009	(826)	(765)
25,000	5.2320%	5/1/2006	5/1/2009	(493)	(486)
25,000	5.2320%	5/1/2006	5/1/2009	(493)	(486)
				$ (2,648)	$ (2,333)

These amounts are included on our Consolidated Balance Sheets as other liabilities.

We designated these derivatives as cash flow hedges. These contracts hedge the risk of changes in interest rates on certain of our one-month LIBOR-based variable rate borrowings until their respective maturities.

The table below sets forth our accounting application of changes in derivative fair values:

	For the Three Months Ended June 30,	For the Six Months Ended June 30,

	2008	2007	2008	2007
Beginning balance	$ (4,701)	$ (556)	$ (2,333)	$ (308)
Increase (decrease) in fair value applied to accumulated other comprehensive loss and minority interests	2,053	669	(315)	421
Ending balance	$ (2,648)	$ 113	$ (2,648)	$ 113

Table of Contents

13. Shareholders Equity

Preferred Shares

Preferred shares of beneficial interest (preferred shares) consisted of the following:

	June 30, 2008	December 31, 2007
2,200,000 designated as Series G Cumulative Redeemable Preferred Shares of beneficial interest (2,200,000 shares issued with an aggregate liquidation preference of $55,000)	$ 22	$ 22
2,000,000 designated as Series H Cumulative Redeemable Preferred Shares of beneficial interest (2,000,000 shares issued with an aggregate liquidation preference of $50,000)	20	20
3,390,000 designated as Series J Cumulative Redeemable Preferred Shares of beneficial interest (3,390,000 shares issued with an aggregate liquidation preference of $84,750)	34	34
531,667 designated as Series K Cumulative Redeemable Convertible Preferred Shares of beneficial interest (531,667 shares issued with an aggregate liquidation preference of $26,583)	5	5
Total preferred shares	$ 81	$ 81

Common Shares

During the six months ended June 30, 2008, we converted 15,242 common units in our Operating Partnership into common shares on the basis of one common share for each common unit.

See Note 17 for disclosure of common share activity pertaining to our share-based compensation plans.

Accumulated Other Comprehensive Loss

The table below sets forth activity in the accumulated other comprehensive loss component of shareholders equity:

	For the Six Months Ended June 30, 2008	2007
Beginning balance	$ (2,372)	$ (693)
Unrealized (loss) gain on derivatives, net of minority interests	(269)	342
Realized loss on derivatives, net of minority interests	26	26

Ending balance	$	(2,615)	$	(325)

The table below sets forth our comprehensive income:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	**2007**	**2008**	**2007**
Net income	$ 12,853	$ 7,877	$ 24,248	$ 13,424
Unrealized gain (loss) on derivatives, net of minority interests	1,740	565	(269)	342
Realized loss on derivatives, net of minority interests	13	13	26	26
Total comprehensive income	$ 14,606	$ 8,455	$ 24,005	$ 13,792

Table of Contents

14. Dividends and Distributions

The following table summarizes our dividends and distributions when either the payable dates or record dates occurred during the six months ended June 30, 2008:

	Record Date	Payable Date	Dividend/ Distribution Per Share/unit	Total Dividend/ Distribution
Series G Preferred Shares:				
Fourth Quarter 2007	December 31, 2007	January 15, 2008	$ 0.5000	$ 1,100
First Quarter 2008	March 31, 2008	April 15, 2008	$ 0.5000	$ 1,100
Second Quarter 2008	June 30, 2008	July 15, 2008	$ 0.5000	$ 1,100
Series H Preferred Shares:				
Fourth Quarter 2007	December 31, 2007	January 15, 2008	$ 0.4688	$ 938
First Quarter 2008	March 31, 2008	April 15, 2008	$ 0.4688	$ 938
Second Quarter 2008	June 30, 2008	July 15, 2008	$ 0.4688	$ 938
Series J Preferred Shares:				
Fourth Quarter 2007	December 31, 2007	January 15, 2008	$ 0.4766	$ 1,616
First Quarter 2008	March 31, 2008	April 15, 2008	$ 0.4766	$ 1,616
Second Quarter 2008	June 30, 2008	July 15, 2008	$ 0.4766	$ 1,616
Series K Preferred Shares:				
Fourth Quarter 2007	December 31, 2007	January 15, 2008	$ 0.7000	$ 372
First Quarter 2008	March 31, 2008	April 15, 2008	$ 0.7000	$ 372
Second Quarter 2008	June 30, 2008	July 15, 2008	$ 0.7000	$ 372
Common Shares:				
Fourth Quarter 2007	December 31, 2007	January 15, 2008	$ 0.3400	$ 16,097
First Quarter 2008	March 31, 2008	April 15, 2008	$ 0.3400	$ 16,173
Second Quarter 2008	June 30, 2008	July 15, 2008	$ 0.3400	$ 16,197
Series I Preferred Units:				
Fourth Quarter 2007	December 31, 2007	January 15, 2008	$ 0.4688	$ 165
First Quarter 2008	March 31, 2008	April 15, 2008	$ 0.4688	$ 165
Second Quarter 2008	June 30, 2008	July 15, 2008	$ 0.4688	$ 165
Common Units:				
Fourth Quarter 2007	December 31, 2007	January 15, 2008	$ 0.3400	$ 2,777
First Quarter 2008	March 31, 2008	April 15, 2008	$ 0.3400	$ 2,771
Second Quarter 2008	June 30, 2008	July 15, 2008	$ 0.3400	$ 2,772

Table of Contents

15. Supplemental Information to Statements of Cash Flows

	For the Six Months Ended June 30,			
	2008		2007	
Supplemental schedule of non-cash investing and financing activities:				
Debt assumed in connection with acquisition of properties	$		$	38,848
Issuance of common shares in connection with acquisition of properties	$		$	156,691
Issuance of preferred shares in connection with acquisition of properties	$		$	26,583
Restricted cash used in connection with acquisitions of properties	$		$	20,122
Issuance of common units in the Operating Partnership in connection with acquisition of interest in properties	$		$	12,125
Increase (decrease) in accrued capital improvements, leasing, and acquisition costs	$	2,176	$	(3,057)
Consolidation of real estate joint venture:				
Real estate assets	$	14,208	$	39
Prepaid and other assets		(10,859)		1,021
Minority interest		(3,349)		(1,060)
Net adjustment	$		$	
Proceeds from sale of property invested in restricted cash	$	5,103	$	
Reclassification of operating assets to investment in consolidated real estate joint venture	$		$	10,341
Amortization of discounts and premiums on mortgage loans to commercial real estate properties	$	26	$	275
(Decrease) increase in fair value of derivatives applied to AOCL and minority interests	$	(315)	$	421
Adjustments to minority interests resulting from changes in ownership of the Operating Partnership by COPT	$		$	25,167
Dividends/distribution payable	$	22,548	$	20,754
Decrease in minority interests and increase in shareholders equity in connection with the conversion of common units into common shares	$	420	$	18,958

Table of Contents

16. Information by Business Segment

As of June 30, 2008, we had nine primary office property segments: Baltimore/Washington Corridor; Northern Virginia; Suburban Baltimore; Colorado Springs; Suburban Maryland; Greater Philadelphia; St. Mary s and King George Counties; San Antonio; and Northern/Central New Jersey.

The table below reports segment financial information. Our segment entitled Other includes assets and operations not specifically associated with the other defined segments, including corporate assets and investments in unconsolidated entities. We measure the performance of our segments based on total revenues less property operating expenses, a measure we define as net operating income (NOI). We believe that NOI is an important supplemental measure of operating performance for a REIT s operating real estate because it provides a measure of the core operations that is unaffected by depreciation, amortization, financing and general and administrative expenses; this measure is particularly useful in our opinion in evaluating the performance of geographic segments, same-office property groupings and individual properties.

	Baltimore/ Washington Corridor	Northern Virginia	Suburban Baltimore	Colorado Springs	Suburban Maryland	Greater Philadelphia	St. Mary s & King George Counties	San Antonio	Northern/ Central New Jersey	Other	Intersegment Elimination	Total
Three Months Ended June 30, 2008												
Revenues	$ 46,426	$ 18,927	$ 13,502	$ 4,691	$ 4,516	$ 2,506	$ 3,134	$ 1,999	$ 586	$ 2,812	$ (903)	$ 98,196
Property operating expenses	15,686	7,255	5,691	1,738	1,553	40	747	443	38	1,196	(419)	33,968
NOI	$ 30,740	$ 11,672	$ 7,811	$ 2,953	$ 2,963	$ 2,466	$ 2,387	$ 1,556	$ 548	$ 1,616	$ (484)	$ 64,228
Additions to commercial real estate properties	$ 39,987	$ 803	$ 4,309	$ 41,468	$ 1,238	$ 384	$ 674	$ 18,738	$ 22	$ 943	$ (15)	$ 108,551
Three Months Ended June 30, 2007												
Revenues	$ 42,722	$ 18,254	$ 13,448	$ 3,604	$ 3,943	$ 2,507	$ 3,029	$ 1,863	$ 1,006	$ 1,610	$ (816)	$ 91,170
Property operating expenses	13,376	6,483	4,976	1,193	1,655	29	743	385	385	1,249	(1,079)	29,395
NOI	$ 29,346	$ 11,771	$ 8,472	$ 2,411	$ 2,288	$ 2,478	$ 2,286	$ 1,478	$ 621	$ 361	$ 263	$ 61,775
Additions to commercial real estate properties	$ 20,602	$ 6,019	$ 2,495	$ 20,564	$ 1,412	$ 300	$ 214	$ 40	$ 11	$ 17,883	$ (513)	$ 69,027
Six Months Ended June 30,												

2008												
Revenues	$ 92,003	$ 37,931	$ 27,412	$ 8,863	$ 9,100	$ 5,012	$ 6,294	$ 3,907	$ 1,338	$ 5,538	$ (1,781)	$ 195,617
Property operating expenses	31,901	14,239	12,014	3,320	3,217	104	1,489	876	247	2,513	(1,223)	68,697
NOI	$ 60,102	$ 23,692	$ 15,398	$ 5,543	$ 5,883	$ 4,908	$ 4,805	$ 3,031	$ 1,091	$ 3,025	$ (558)	$ 126,920
Additions to commercial real estate properties	$ 54,074	$ 1,729	$ 7,737	$ 53,446	$ 22,096	$ 612	$ 1,236	$ 18,248	$ 43	$ 2,225	$ (15)	$ 161,431
Segment assets at June 30, 2008	$ 1,248,057	$ 469,146	$ 438,424	$ 235,458	$ 160,509	$ 95,123	$ 94,798	$ 84,359	$ 22,155	$ 163,421	$ (980)	$ 3,010,470
Six Months Ended June 30, 2007												
Revenues	$ 86,559	$ 35,426	$ 26,529	$ 7,199	$ 7,910	$ 5,013	$ 6,127	$ 3,644	$ 2,792	$ 2,109	$ (1,743)	$ 181,565
Property operating expenses	27,911	12,811	10,747	2,482	3,323	66	1,519	747	1,085	2,551	(1,760)	61,482
NOI	$ 58,648	$ 22,615	$ 15,782	$ 4,717	$ 4,587	$ 4,947	$ 4,608	$ 2,897	$ 1,707	$ (442)	$ 17	$ 120,083
Additions to commercial real estate properties	$ 99,128	$ 16,916	$ 262,875	$ 24,367	$ 1,908	$ 532	$ 283	$ 6	$ 265	$ 43,735	$ (945)	$ 449,070
Segment assets at June 30, 2007	$ 1,168,553	$ 482,966	$ 452,324	$ 157,397	$ 129,064	$ 96,888	$ 96,061	$ 53,032	$ 44,425	$ 174,026	$ (7)	$ 2,854,729

Table of Contents

The following table reconciles our segment revenues to total revenues as reported on our Consolidated Statements of Operations:

	For the Three Months Ended June 30, 2008	For the Three Months Ended June 30, 2007	For the Six Months Ended June 30, 2008	For the Six Months Ended June 30, 2007
Segment revenues	$ 98,196	$ 91,170	$ 195,617	$ 181,565
Construction contract revenues	14,619	10,620	23,133	19,311
Other service operations revenues	525	1,073	1,003	2,459
Less: Revenues from discontinued real estate operations (Note 19)	(85)	(796)	(355)	(2,323)
Total revenues	$ 113,255	$ 102,067	$ 219,398	$ 201,012

The following table reconciles our segment property operating expenses to property operating expenses as reported on our Consolidated Statements of Operations:

	For the Three Months Ended June 30, 2008	For the Three Months Ended June 30, 2007	For the Six Months Ended June 30, 2008	For the Six Months Ended June 30, 2007
Segment property operating expenses	$ 33,968	$ 29,395	$ 68,697	$ 61,482
Less: Property operating expenses from discontinued real estate operations (Note 19)	(11)	(363)	(198)	(891)
Total property operating expenses	$ 33,957	$ 29,032	$ 68,499	$ 60,591

The following table reconciles our NOI for reportable segments to income from continuing operations as reported on our Consolidated Statements of Operations:

	For the Three Months Ended June 30, 2008	For the Three Months Ended June 30, 2007	For the Six Months Ended June 30, 2008	For the Six Months Ended June 30, 2007
NOI for reportable segments	$ 64,228	$ 61,775	$ 126,920	$ 120,083
Construction contract revenues	14,619	10,620	23,133	19,311
Other service operations revenues	525	1,073	1,003	2,459
Equity in loss of unconsolidated entities	(56)	(57)	(110)	(151)
Income tax benefit (expense)	107	(178)	(5)	(283)
Other adjustments:				
Depreciation and other amortization associated with real estate operations	(24,955)	(26,834)	(49,847)	(52,786)
Construction contract expenses	(14,192)	(10,136)	(22,475)	(18,619)
Other service operations expenses	(454)	(1,126)	(1,056)	(2,531)
General and administrative expenses	(6,036)	(5,326)	(11,969)	(10,203)
Interest expense on continuing operations	(19,437)	(20,437)	(39,746)	(40,213)
Amortization of deferred financing costs	(910)	(921)	(1,713)	(1,805)
Gain on sale of non-real estate investment	5	1,033	51	1,033
Minority interests in continuing operations	(1,663)	(941)	(2,801)	(1,340)
NOI from discontinued operations	(74)	(433)	(157)	(1,432)
Income from continuing operations	$ 11,707	$ 8,112	$ 21,228	$ 13,523

The accounting policies of the segments are the same as those previously disclosed for Corporate Office Properties Trust and subsidiaries, where applicable. We did not allocate interest expense,

Table of Contents

amortization of deferred financing costs and depreciation and other amortization to segments since they are not included in the measure of segment profit reviewed by management. We also did not allocate construction contract revenues, other service operations revenues, construction contract expenses, other service operations expenses, equity in loss of unconsolidated entities, general and administrative expense, gain on sale of non-real estate investment, income taxes and minority interests because these items represent general corporate items not attributable to segments.

17. Share-Based Compensation

During the six months ended June 30, 2008, we granted 40,000 options to purchase common shares (options) to members of our Board of Trustees. The exercise price of these option grants was $37.81 per share. These options vest on the first anniversary of the grant date provided that the Trustees remain in their positions. These option grants expire ten years after the grant date. We computed share-based compensation expense for these options under the fair value method using the Black-Scholes option-pricing model; the assumptions we used in that model are set forth below:

Fair value of grants on grant date	$	8.00
Risk-free interest rate		3.62%
Expected life (in years)		6.52
Expected volatility		24.22%
Expected annual dividend yield		3.07%

During the six months ended June 30, 2008, 90,209 options were exercised. The weighted average exercise price of these options was $15.12 per share, and the total intrinsic value of options exercised was $1,986.

During the six months ended June 30, 2008, certain employees were granted a total of 286,094 restricted shares with a weighted average grant date fair value of $32.19 per share. These shares are subject to forfeiture restrictions that lapse in equal increments annually over a three-year period (for most of the grants) or a five-year period, in each case beginning on the first anniversary of the grant date provided that the employees remain employed by us. During the six months ended June 30, 2008, forfeiture restrictions lapsed on 134,145 common shares previously issued to employees. These shares had a weighted average grant date fair value of $34.82 per share, and the total fair value of the shares on the vesting dates was $4,259.

We realized a windfall tax benefit of $1,053 in the six months ended June 30, 2008 on options exercised and vesting restricted shares in connection with employees of our subsidiaries that are subject to income tax. We did not realize a windfall tax benefit in the six months ended June 30, 2007 because COMI had a net operating loss carryforward for tax purposes; had COMI not had a net operating loss carryforward during the six months ended June 30, 2007, we would have recognized a windfall tax benefit of $1,687 in that period.

Expenses from share-based compensation are reflected in our Consolidated Statements of Operations as follows:

	For the Three Months	For the Six Months

	Ended June 30,		Ended June 30,	
	2008	2007	2008	2007
Increase in general and administrative expenses	$ 1,572	$ 1,196	$ 3,103	$ 2,075
Increase in construction contract and other service operations expenses	583	509	1,098	863
Share-based compensation expense	2,155	1,705	4,201	2,938
Income tax benefit (expense)	10	(66)	(29)	(101)
Minority interests	(329)	(256)	(635)	(449)
Net share-based compensation expense	$ 1,836	$ 1,383	$ 3,537	$ 2,388

Table of Contents

18. Income Taxes

The table below sets forth COMI s provision for income tax benefit (expense) and its presentation on our Consolidated Statements of Operations:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
Deferred				
Federal	$ 53	$ (148)	$ (303)	$ (234)
State	8	(33)	(71)	(52)
	61	(181)	(374)	(286)
Current				
Federal	34		(171)	
State	7		(38)	
	41		(209)	
Total income tax benefit (expense)	$ 102	$ (181)	$ (583)	$ (286)
Reported on line entitled income tax benefit (expense)	$ 107	$ (178)	$ (5)	$ (283)
Reported on line entitled gain on sales of real estate, net	(5)	(3)	(578)	(3)
Total income tax benefit (expense)	$ 102	$ (181)	$ (583)	$ (286)

Items contributing to temporary differences that lead to deferred taxes include net operating losses that are not deductible until future periods, depreciation and amortization, certain accrued compensation and compensation paid in the form of contributions to a nonqualified deferred compensation plan.

COMI s combined Federal and state effective tax rate was 39% for the three and six months ended June 30, 2008 and 2007.

19. Discontinued Operations

Income from discontinued operations primarily includes revenues and expenses associated with the following:

- 2 and 8 Centre Drive properties that were sold on September 7, 2007;
- 7321 Parkway property that was sold on September 7, 2007;
- 429 Ridge Road property that was sold on January 31, 2008;

- 47 Commerce Drive property that was sold on April 1, 2008; and
- 7253 Ambassador Road property that was sold on June 2, 2008.

Table of Contents

The table below sets forth the components of income from discontinued operations:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
Revenue from real estate operations	$ 85	$ 796	$ 355	$ 2,323
Expenses from real estate operations:				
Property operating expenses	11	363	198	891
Depreciation and amortization		253	52	601
Interest expense	10	637	51	1,125
Expenses from real estate operations	21	1,253	301	2,617
Income (loss) from discontinued operations before gain on sales of real estate and minority interests	64	(457)	54	(294)
Gain (loss) on sales of real estate	1,250	(11)	2,526	(11)
Minority interests in discontinued operations	(199)	72	(393)	45
Income (loss) from discontinued operations, net of minority interests	$ 1,115	$ (396)	$ 2,187	$ (260)

20. Commitments and Contingencies

In the normal course of business, we are involved in legal actions arising from our ownership and administration of properties. Management does not anticipate that any liabilities that may result will have a materially adverse effect on our financial position, operations or liquidity. We are subject to various Federal, state and local environmental regulations related to our property ownership and operation. We have performed environmental assessments of our properties, the results of which have not revealed any environmental liability that we believe would have a materially adverse effect on our financial position, operations or liquidity.

Acquisitions

As of June 30, 2008, we were under contract to acquire a parcel of land in San Antonio for a purchase price of $8,102, on which we had paid a deposit of $1,000; we completed this acquisition on July 16, 2008. We were also under contract to acquire a parcel of land in Frederick, Maryland for a purchase price of $8,000, on which we had paid a deposit of $355.

Joint Ventures

As part of our obligations under the partnership agreement of Harrisburg Corporate Gateway Partners, LP, we agreed to indemnify the partnership s lender for 80% of losses under standard nonrecourse loan guarantees (environmental indemnifications and guarantees against fraud and misrepresentation) during the period of time in which we manage the partnership s properties; we do not expect to incur any losses under these loan guarantees.

We are party to a contribution agreement that formed a joint venture relationship with a limited partnership to develop up to 1.8 million square feet of office space on 63 acres of land located in Hanover, Maryland. Under the contribution agreement, we agreed to fund up to $2,200 in pre-construction costs associated with the property. As we and the joint venture partner agree to proceed with the construction of buildings in the future, our joint venture partner would contribute land into newly-formed entities and we would make additional cash capital contributions into such entities to fund development and construction activities for which financing is not obtained. We owned a 50% interest in one such joint venture as of June 30, 2008.

Table of Contents

We may be required to make our pro rata share of additional investments in our real estate joint ventures (generally based on our percentage ownership) in the event that additional funds are needed. In the event that the other members of these joint ventures do not pay their share of investments when additional funds are needed, we may then deem it appropriate to make even larger investments in these joint ventures.

In one of the consolidated joint ventures that we owned as of June 30, 2008, we would be obligated to acquire the other member s 50% interest in the joint venture if defined events were to occur. The amount we would need to pay for that membership interest is computed based on the amount that the owner of the interest would receive under the joint venture agreement in the event that the office property owned by the joint venture was sold for a capitalized fair value (as defined in the agreement) on a defined date. We estimate the aggregate amount we would need to pay for the other member s membership interest in this joint venture to be $718; however, since the determination of this amount is dependent on the operations of the office property, which is not both completed and sufficiently occupied, this estimate is preliminary and could be materially different from the actual obligation.

Office Space Operating Leases

We are obligated as lessee under five operating leases for office space. Future minimum rental payments due under the terms of these leases as of June 30, 2008 follow:

Six months ended December 31, 2008	$	127
2009		178
2010		135
2011		57
	$	497

Other Operating Leases

We are obligated under various leases for vehicles and office equipment. Future minimum rental payments due under the terms of these leases as of June 30, 2008 follow:

Six months ended December 31, 2008	$	244
2009		367
2010		179
2011		43
	$	833

Environmental Indemnity Agreement

We agreed to provide certain environmental indemnifications in connection with a lease of three properties in our New Jersey region. The prior owner of the properties, a Fortune 100 company which is responsible for groundwater contamination at such properties, previously agreed to indemnify us for (1) direct losses incurred in connection with the contamination and (2) its failure to perform remediation activities required by the State of New Jersey, up to the point that the state declares the remediation to be complete. Under the lease agreement, we agreed to the following:

- to indemnify the tenant against losses covered under the prior owner s indemnity agreement if the prior owner fails to indemnify the tenant for such losses. This indemnification is capped at $5,000 in perpetuity after the State of New Jersey declares the remediation to be complete;

- to indemnify the tenant for consequential damages (e.g., business interruption) at one of the buildings in perpetuity and another of the buildings for 15 years after the tenant s acquisition of the property from us. This indemnification is capped at $12,500; and

- to pay 50% of additional costs related to construction and environmental regulatory activities incurred by the tenant as a result of the indemnified environmental condition of the properties. This indemnification is capped at $300 annually and $1,500 in the aggregate.

Table of Contents

21. Subsequent Event

On July 18, 2008, we borrowed $221,400 under a mortgage loan requiring interest only payments for the term at a variable rate of LIBOR plus 225 basis points. This loan facility has a four-year term with an option to extend by an additional year.

Table of Contents

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

Overview

Corporate Office Properties Trust (COPT) and subsidiaries (collectively, the Company , we or us) is a specialty office real estate investment trust (REIT) that focuses on strategic customer relationships and specialized tenant requirements in the United States Government, defense information technology and data sectors. We acquire, develop, manage and lease properties that are typically concentrated in large office parks primarily located adjacent to government demand drivers and/or in demographically strong markets possessing growth opportunities. As of June 30, 2008, our investments in real estate included the following:

- 234 wholly owned operating properties totaling 18.2 million square feet;
- 18 wholly owned properties under construction or development that we estimate will total approximately 1.8 million square feet upon completion;
- wholly owned land parcels totaling 1,457 acres that we believe are potentially developable into approximately 12.1 million square feet; and
- partial ownership interests in a number of other real estate projects in operation or under development or redevelopment.

During the six months ended June 30, 2008, we:

- experienced significant growth in revenues from real estate operations and property operating expenses due primarily to the addition of properties through construction activities and acquisitions;
- finished the period with occupancy of our wholly owned portfolio of properties at 93.4%;
- acquired three office properties totaling 247,280 square feet (one located in Colorado Springs and two in San Antonio) for $40.6 million;
- had five newly-constructed properties totaling 437,064 square feet (three located in Colorado Springs and two in the Baltimore/Washington Corridor) become fully operational. We also had 41,500 square feet placed into service in one partially operational property;
- sold three operating properties for a total of $25.3 million, resulting in recognized gains before minority interests of $2.6 million;

• sold six recently constructed office condominiums located in Northern Virginia for sale prices totaling $8.4 million in the aggregate, resulting in a recognized gain before minority interests and taxes of $1.4 million; and

• entered into a construction loan agreement with a group of lenders that provides for an aggregate commitment by the lenders of $225.0 million, with a right for us to further increase the aggregate commitment during the term to a maximum of $325.0 million, subject to certain conditions. The construction loan agreement matures on May 2, 2011, and may be extended by one year at our option, subject to certain conditions.

On July 18, 2008, we borrowed $221.4 million under a mortgage loan requiring interest only payments for the term at a variable rate of LIBOR plus 225 basis points. This loan facility has a four-year term with an option to extend by an additional year.

In this section, we discuss our financial condition and results of operations as of and for the three and six months ended June 30, 2008. This section includes discussions on, among other things:

• our results of operations and why various components of our Consolidated Statements of Operations changed for the three and six months ended June 30, 2008 compared to the same periods in 2007;

• how we raised cash for acquisitions and other capital expenditures during the six months ended June 30, 2008;

• changes in our cash flows for the six months ended June 30, 2008 and 2007;

• how we expect to generate cash for short and long-term capital needs;

• our commitments and contingencies at June 30, 2008; and

Table of Contents

- the computation of our Funds from Operations for the three and six months ended June 30, 2008 and 2007.

You should refer to our Consolidated Financial Statements as you read this section.

This section contains forward-looking statements, as defined in the Private Securities Litigation Reform Act of 1995, that are based on our current expectations, estimates and projections about future events and financial trends affecting the financial condition and operations of our business. Forward-looking statements can be identified by the use of words such as may, will, should, expect, estimate or other comparable terminology. Forward-looking statements are inherently subject to risks and uncertainties, many of which we cannot predict with accuracy and some of which we might not even anticipate. Although we believe that the expectations, estimates and projections reflected in such forward-looking statements are based on reasonable assumptions at the time made, we can give no assurance that these expectations, estimates and projections will be achieved. Future events and actual results may differ materially from those discussed in the forward-looking statements. Important factors that may affect these expectations, estimates and projections include, but are not limited to:

- our ability to borrow on favorable terms;
- general economic and business conditions, which will, among other things, affect office property demand and rents, tenant creditworthiness, interest rates and financing availability;
- adverse changes in the real estate markets, including, among other things, increased competition with other companies;
- risks of real estate acquisition and development activities, including, among other things, risks that development projects may not be completed on schedule, that tenants may not take occupancy or pay rent or that development and operating costs may be greater than anticipated;
- risks of investing through joint venture structures, including risks that our joint venture partners may not fulfill their financial obligations as investors or may take actions that are inconsistent with our objectives;
- our ability to satisfy and operate effectively under Federal income tax rules relating to real estate investment trusts and partnerships;
- governmental actions and initiatives; and
- environmental requirements.

We undertake no obligation to update or supplement forward-looking statements.

Table of Contents

Corporate Office Properties Trust and Subsidiaries

Operating Data Variance Analysis

(Dollars for this table are in thousands, except per share data)

	For the Three Months Ended June 30,				For the Six Months Ended June 30,			
	2008	2007	Variance	% Change	2008	2007	Variance	% Change
Revenues								
Rental revenue	$ 83,154	$ 78,337	$ 4,817	6.1%	$ 164,864	$ 153,612	$ 11,252	7.3%
Tenant recoveries and other real estate operations revenue	14,957	12,037	2,920	24.3%	30,398	25,630	4,768	18.6%
Construction contract revenues	14,619	10,620	3,999	37.7%	23,133	19,311	3,822	19.8%
Other service operations revenues	525	1,073	(548)	(51.1)%	1,003	2,459	(1,456)	(59.2)%
Total revenues	113,255	102,067	11,188	11.0%	219,398	201,012	18,386	9.1%
Expenses								
Property operating expenses	33,957	29,032	4,925	17.0%	68,499	60,591	7,908	13.1%
Depreciation and other amortization associated with real estate operations	24,955	26,834	(1,879)	(7.0)%	49,847	52,786	(2,939)	(5.6)%
Construction contract expenses	14,192	10,136	4,056	40.0%	22,475	18,619	3,856	20.7%
Other service operations expenses	454	1,126	(672)	(59.7)%	1,056	2,531	(1,475)	(58.3)%
General and administrative expenses	6,036	5,326	710	13.3%	11,969	10,203	1,766	17.3%
Total operating expenses	79,594	72,454	7,140	9.9%	153,846	144,730	9,116	6.3%
Operating income	33,661	29,613	4,048	13.7%	65,552	56,282	9,270	16.5%
Interest expense and amortization of deferred financing costs	(20,347)	(21,358)	1,011	(4.7)%	(41,459)	(42,018)	559	(1.3)%
Gain on sale of non-real estate investment	5	1,033	(1,028)	(99.5)%	51	1,033	(982)	(95.1)%
Equity in loss of unconsolidated entities	(56)	(57)	1	(1.8)%	(110)	(151)	41	(27.2)%
Income tax benefit (expense)	107	(178)	285	N/A	(5)	(283)	278	(98.2)%
Income from continuing operations before minority interests	13,370	9,053	4,317	47.7%	24,029	14,863	9,166	61.7%
Minority interests in income from continuing operations	(1,663)	(941)	(722)	76.7%	(2,801)	(1,340)	(1,461)	109.0%
Income from continuing operations	11,707	8,112	3,595	44.3%	21,228	13,523	7,705	57.0%
Income (loss) from discontinued operations, net	1,115	(396)	1,511	N/A	2,187	(260)	2,447	N/A
Gain on sales of real estate, net	31	161	(130)	(80.7)%	833	161	672	417.4%
Net income	12,853	7,877	4,976	63.2%	24,248	13,424	10,824	80.6%
Preferred share dividends	(4,026)	(4,025)	(1)	0.0%	(8,051)	(8,018)	(33)	0.4%
	$ 8,827	$ 3,852	$ 4,975	129.2%	$ 16,197	$ 5,406	$ 10,791	199.6%

Net income available to common shareholders								
Basic earnings per common share								
Income from continuing operations	$ 0.16	$ 0.09	$ 0.07	77.8%	$ 0.30	$ 0.12	$ 0.18	150.0%
Net income available to common shareholders	$ 0.19	$ 0.08	$ 0.11	137.5%	$ 0.34	$		