

KILROY REALTY CORP  
Form 10-K/A  
November 08, 2005  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

Amendment No. 3

**FORM 10-K/A**

(MARK ONE)

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

For the fiscal year ended December 31, 2004

OR

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

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

Commission file number 1-12675

**KILROY REALTY CORPORATION**

(Exact name of registrant as specified in its charter)

Maryland  
(State or other jurisdiction)

95-4598246  
(I.R.S. Employer)

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of incorporation or organization)

Identification Number)

12200 W. Olympic Boulevard, Suite 200  
Los Angeles, California  
(Address of principal executive offices)

90064  
(Zip Code)

Registrant's telephone number, including area code: (310) 481-8400

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

<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
Common Stock, \$.01 par value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

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

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes  No

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant was approximately \$968,361,059 based on the closing price on the New York Stock Exchange for such shares on June 30, 2004.

As of February 28, 2005, 28,742,839 shares of common stock, par value \$.01 per share, were outstanding.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the Company's Proxy Statement with respect to its 2005 Annual Meeting of Stockholders to be filed not later than 120 days after the end of the registrant's fiscal year are incorporated by reference into Part III hereof.



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**EXPLANATORY NOTE**

This Amendment No. 3 on Form 10-K/A (the Amended Filing ) of Kilroy Realty Corporation (the Company ) of the Form 10-K for the fiscal year ended December 31, 2004 (as amended by Amendments No. 1 and No. 2 on Form 10-K/A, the Original Filing ), is being filed to restate the Company s consolidated financial statements to mark six interest rate swap and two interest rate cap agreements the Company entered into in 2000 and 2002 to market and to recognize the impact of this mark to market adjustment in the income statement for each period, rather than through other comprehensive income. Prior to entering into these agreements, the Company engaged an independent consulting firm specializing in derivatives to advise the Company with respect to derivatives and hedging matters. The Company consulted closely with the independent derivatives specialist during its preparation of the formal designation of the instruments to ensure that each of the instruments qualified for hedge accounting treatment under Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities ( SFAS 133 ) and the related accounting guidance. Although both the Company and the independent derivatives specialist believed the designation documentation met the requirements under SFAS 133 at the time the derivative transactions were entered into, the Company has subsequently determined that the designation documentation does not meet the technical requirements under SFAS 133 to qualify for hedge accounting treatment. As a result, the Company is required to restate prior period financial statements to mark all of these instruments to market and to recognize the impact of this mark to market adjustment in the statement of operations for each period, rather than through other comprehensive income.

In addition, based on a recent review of the Company s accounting treatment for tenant improvements reimbursed by the tenant, the Company is also restating its financial statements to record a capital asset and related depreciation for leasehold improvements constructed by the Company that are reimbursed by tenants, with a corresponding liability for deferred revenue, which will be amortized into rental revenue over the lives of the related leases. In connection with the restatement, certain other immaterial adjustments have been recorded.

The Company previously filed Amendment No. 2 on Form 10-K/A to restate the Company s income from continuing operations per common share included within its consolidated statements of operations for the years ended December 31, 2004 and 2003, and the notes related thereto, to correctly reflect the impact of preferred stock dividends in the calculation of income from continuing operations per common share in accordance with Statement of Financial Accounting Standards No. 128, Earnings per Share, so that income from continuing operations per share is presented net of preferred dividends paid and accrued. Amendment No. 2 was also filed to restate the consolidated statements of cash flows for the years ended December 31, 2004, 2003 and 2002 to correct the classification of two items in the consolidated statements of cash flows.

For a more detailed description of the restatements, see Note 27 to the accompanying consolidated financial statements contained in this Amended Filing. In connection with the restatements, the Company reevaluated the effectiveness of its controls and procedures and, accordingly, includes revised disclosure in this Amended Filing under Part II, Item 9A Controls and Procedures.

The Company is concurrently filing amendments to its Quarterly Reports on Form 10-Q/A for the quarters ended March 31, 2005 and June 30, 2005 also to restate the Company s consolidated financial statements to mark the interest rate swap and interest rate cap agreements the Company entered into in 2000 and 2002 to market and to recognize the impact of this mark to market adjustment in the statement of operations for each period, rather than through other comprehensive income, as well as to record a capital asset and related depreciation for leasehold improvements constructed by the Company that are reimbursed by tenants with a corresponding liability for deferred revenue, which will be amortized into rental revenue over the lives of the related leases. The decision to further restate the Company s consolidated financial statements was previously announced in our Current Reports on Form 8-K filed with the Securities and Exchange Commission on October 25, 2005 and October 31, 2005.

The Company has also updated its historical financial statements and the accompanying selected financial data in this Form 10-K/A for discontinued operations that have resulted from the disposition of five operating

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properties during the nine months ended September 30, 2005. The other concurrently filed amendments referenced above reflect a similar update.

To reflect the restatement of the Company's consolidated financial statements described above and the update for discontinued operations, the Company is also re-issuing Part II, Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations ( MD&A ) and Part II, Item 7A Quantitative and Qualitative Disclosures about Market Risk that accompanied the financial statements in the Original Filing.

This Form 10-K/A does not reflect events occurring after the filing of the Original Filing or modify or update disclosures, including the exhibits to the Original Filing, affected by subsequent events except in connection with the foregoing.

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(in thousands, except per share, square footage and occupancy data)

	Year Ended December 31,				
	2004	2003	2002	2001	2000
	(As Restated, see Note 27 to the Company's consolidated financial statements)				
<b>Statements of Operations Data:</b>					
Rental income	\$ 196,191	\$ 177,346	\$ 173,931	\$ 169,420	\$ 148,156
Tenant reimbursements	21,156	19,665	20,854	20,016	17,365
Other property income	1,202	23,998	2,672	6,268	711
<b>Total revenues</b>	<b>218,549</b>	<b>221,009</b>	<b>197,457</b>	<b>195,704</b>	<b>166,232</b>
Property expenses	34,010	30,910	28,007	27,109	20,220
Real estate taxes	16,344	15,061	14,440	13,776	12,941
Provision for bad debts	886	1,503	6,712	3,609	1,663
Ground leases	1,401	1,296	1,354	1,507	1,643
General and administrative expenses	34,021	20,095	12,902	11,692	10,535
Interest expense	33,994	30,515	30,629	37,854	38,460
Depreciation and amortization	58,620	55,471	57,750	50,381	38,245
<b>Total expenses</b>	<b>179,276</b>	<b>154,851</b>	<b>151,794</b>	<b>145,928</b>	<b>123,707</b>
Net settlement payments on interest rate swaps	(2,893)	(3,218)	(6,819)	(6,454)	
Gain (loss) on derivative	3,099	704	(244)	(5,553)	
Interest and other income	521	196	513	1,030	1,878
Interest income from related party					2,724
Equity in earnings from unconsolidated real estate					191
<b>Total other income (expense)</b>	<b>727</b>	<b>(2,318)</b>	<b>(6,550)</b>	<b>(10,977)</b>	<b>4,793</b>
<b>Income from continuing operations before net gain on dispositions and minority interests</b>	<b>40,000</b>	<b>63,840</b>	<b>39,113</b>	<b>38,799</b>	<b>47,318</b>
Net gain on dispositions of operating properties			896	4,714	11,256
<b>Income from continuing operations before minority interests</b>	<b>40,000</b>	<b>63,840</b>	<b>40,009</b>	<b>43,513</b>	<b>58,574</b>
Minority interests:					
Distributions on Cumulative Redeemable Preferred units	(9,579)	(13,163)	(13,500)	(13,500)	(13,500)
Original issuance costs of redeemed preferred units	(1,200)	(945)			
Minority interest in earnings of Operating Partnership attributable to continuing operations	(3,218)	(6,533)	(3,714)	(2,613)	(5,576)
Recognition of previously reserved Development LLC preferred return			3,908		
Minority interest in earnings of Development LLCs			(1,024)	(3,701)	(421)
<b>Total minority interests</b>	<b>(13,997)</b>	<b>(20,641)</b>	<b>(14,330)</b>	<b>(19,814)</b>	<b>(19,497)</b>

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Income from continuing operations	26,003	43,199	25,679	23,699	39,077
Discontinued operations:					
Revenues from discontinued operations	7,134	10,231	17,706	18,748	18,717
Expenses from discontinued operations	(3,929)	(5,901)	(9,677)	(9,519)	(10,076)
Net gain on dispositions of discontinued operations	6,148	3,642	6,570		
Impairment loss on property held for sale	(726)				
Minority interest in earnings of Operating Partnership attributable to discontinued operations	(1,089)	(1,055)	(1,844)	(968)	(1,078)
<b>Total income from discontinued operations</b>	<b>7,538</b>	<b>6,917</b>	<b>12,755</b>	<b>8,261</b>	<b>7,563</b>
Net income before cumulative effect of change in accounting principle	33,541	50,116	38,434	31,960	46,640
Cumulative effect of change in accounting principle				(1,392)	
<b>Net income</b>	<b>33,541</b>	<b>50,116</b>	<b>38,434</b>	<b>30,568</b>	<b>46,640</b>
Preferred dividends	(3,553)	(349)			
<b>Net income available for common stockholders</b>	<b>\$ 29,988</b>	<b>\$ 49,767</b>	<b>\$ 38,434</b>	<b>\$ 30,568</b>	<b>\$ 46,640</b>
<b>Share Data:</b>					
Weighted average shares outstanding basic	28,244	27,527	27,450	27,167	26,599
Weighted average shares outstanding diluted	28,422	27,738	27,722	27,373	26,755
Income from continuing operations per common share basic	\$ 0.79	\$ 1.56	\$ 0.94	\$ 0.87	\$ 1.47