WASHINGTON REAL ESTATE INVESTMENT TRUST
Form 10-Q
May 08, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For quarterly period ended March 31, 2014

OR

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

COMMISSION FILE NO. 1-6622

WASHINGTON REAL ESTATE
INVESTMENT TRUST
(Exact name of registrant as specified in its charter)

MARYLAND	53-0261100
(State of incorporation)	(IRS Employer Identification Number)

6110 EXECUTIVE BOULEVARD, SUITE 800, ROCKVILLE, MARYLAND 20852
(Address of principal executive office) (Zip code)
Registrant’s telephone number, including area code: (301) 984-9400

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

Title of Each Class	Name of exchange on which registered
Shares of Beneficial Interest	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 such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past ninety (90) days. YES x NO o

Indicate by checkmark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES x NO o

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES o NO x

As of May 5, 2014, 66,630,035 common shares were outstanding.

WASHINGTON REAL ESTATE INVESTMENT TRUST
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PART I
FINANCIAL INFORMATION

ITEM 1: FINANCIAL STATEMENTS
The information furnished in the accompanying unaudited Consolidated Balance Sheets, Condensed Consolidated Statements of Income, Consolidated Statement of Shareholders' Equity and Consolidated Statements of Cash Flows reflects all adjustments, consisting of normal recurring items, which are, in the opinion of management, necessary for a fair presentation of the financial position, results of operations and cash flows for the interim periods. The accompanying financial statements and notes thereto should be read in conjunction with the financial statements and notes for the three years ended December 31, 2013 included in Washington Real Estate Investment Trust’s 2013 Annual Report on Form 10-K.

WASHINGTON REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS, EXCEPT PER SHARE DATA)

	March 31, 2014 (Unaudited)	December 31, 2013
Assets		
Land	$472,056	$426,575
Income producing property	1,784,850	1,675,652
	2,256,906	2,102,227
Accumulated depreciation and amortization	(581,644)	(565,342)
Net income producing property	1,675,262	1,536,885
Properties under development or held for future development	68,963	61,315
Total real estate held for investment, net	1,744,225	1,598,200
Investment in real estate sold or held for sale, net	—	79,901
Cash and cash equivalents	62,080	130,343
Restricted cash	107,039	9,189
Rents and other receivables, net of allowance for doubtful accounts of $5,719 and $6,783, respectively	52,736	48,756
Prepaid expenses and other assets	109,092	105,004
Other assets related to properties sold or held for sale	—	4,100
Total assets	$2,075,172	$1,975,493
Liabilities		
Notes payable	$746,830	$846,703
Mortgage notes payable	404,359	294,671
Lines of credit	—	—
Accounts payable and other liabilities	56,804	51,742
Advance rents	14,688	13,529
Tenant security deposits	8,402	7,869
Liabilities related to properties sold or held for sale	—	1,533
Total liabilities	1,231,083	1,216,047
Equity		
Shareholders' equity		
Preferred shares; $0.01 par value; 10,000 shares authorized; no shares issued or outstanding	—	—
Shares of beneficial interest; $0.01 par value; 100,000 shares authorized: 66,630 and 66,531 shares issued and outstanding at March 31, 2014 and December 31, 2013, respectively	666	665
Additional paid in capital	1,151,353	1,151,174
Distributions in excess of net income	(312,417)	(396,880)
Total shareholders' equity	839,602	754,959
Noncontrolling interests in subsidiaries	4,487	4,487
Total equity	844,089	759,446
Total liabilities and equity	$2,075,172	$1,975,493

See accompanying notes to the consolidated financial statements.

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WASHINGTON REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

	Three Months Ended March 31, 2014	2013
Revenue		
Real estate rental revenue	$68,611	$64,560
Expenses		
Real estate expenses	26,342	22,554
Depreciation and amortization	22,753	21,123
Acquisition costs	3,045	213
General and administrative	4,429	3,862
	56,569	47,752
Real estate operating income	12,042	16,808
Other income (expense)		
Interest expense	(14,530)	(16,190)
Other income	223	239
	(14,307)	(15,951)
(Loss) income from continuing operations	(2,265)	857
Discontinued operations:		
Income from operations of properties sold or held for sale	546	3,283
Gain on sale of real estate	106,273	3,195
Net income	104,554	7,335
Less: Net income attributable to noncontrolling interests in subsidiaries	—	—
Net income attributable to the controlling interests	$104,554	$7,335
Basic net income per share:		
Continuing operations	$(0.04)	$0.01
Discontinued operations	1.60	0.10
Net income per share	$1.56	$0.11
Diluted net income per share:		
Continuing operations	$(0.04)	$0.01
Discontinued operations	1.60	0.10
Net income per share	$1.56	$0.11
Weighted average shares outstanding – basic	66,701	66,393
Weighted average shares outstanding – diluted	66,701	66,519
Dividends declared per share	$0.3000	$0.3000

See accompanying notes to the consolidated financial statements.

WASHINGTON REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY
(IN THOUSANDS)
(UNAUDITED)

	Shares Outstanding	Shares of Beneficial Interest at Par Value	Additional Paid in Capital	Distributions in Excess of Net Income Attributable to the Controlling Interests	Total Shareholders' Equity	Noncontrolling Interests in Subsidiaries	Total Equity
Balance, December 31, 2013	66,531	$ 665	$1,151,174	$ (396,880)	$ 754,959	$ 4,487	$759,446
Net income attributable to the controlling interests	—	—	—	104,554	104,554	—	104,554
Dividends	—	—	—	(20,091)	(20,091)	—	(20,091)
Share grants, net of share grant amortization and forfeitures	99	1	179	—	180	—	180
Balance, March 31, 2014	66,630	$ 666	$1,151,353	$ (312,417)	$ 839,602	$ 4,487	$844,089

See accompanying notes to the consolidated financial statements.

WASHINGTON REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)
(UNAUDITED)

	Three Months Ended March 31,	
	2014	2013
Cash flows from operating activities		
Net income	$104,554	$7,335
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization, including amounts in discontinued operations	22,753	25,524
Provision for losses on accounts receivable	568	1,566
Gain on sale of real estate	(106,273)	(3,195)
Amortization of share grants, net	1,058	1,026
Amortization of debt premiums, discounts and related financing costs	937	1,016
Changes in operating other assets	(3,152)	(628)
Changes in operating other liabilities	2,040	4,260
Net cash provided by operating activities	22,485	36,904
Cash flows from investing activities		
Real estate acquisitions, net	(48,051)	—
Net cash received for sale of real estate	189,386	15,161
Net proceeds from the sale of real estate placed in exchange escrow	(96,610)	—
Capital improvements to real estate	(10,369)	(10,202)
Development in progress	(4,203)	(3,788)
Real estate deposits, net	(2,500)	—
Non-real estate capital improvements	(17)	(7)
Net cash provided by investing activities	27,636	1,164
Cash flows from financing activities		
Line of credit borrowings, net	—	70,000
Dividends paid	(20,091)	(20,034)
Net contributions from noncontrolling interests	—	213
Payment of financing costs	(660)	—
Principal payments – mortgage notes payable	(830)	(30,828)
Borrowings under construction loan	3,197	—
Notes payable repayments	(100,000)	(60,000)
Net cash used in financing activities	(118,384)	(40,649)
Net decrease in cash and cash equivalents	(68,263)	(2,581)
Cash and cash equivalents at beginning of period	130,343	19,324
Cash and cash equivalents at end of period	$62,080	$16,743
Supplemental disclosure of cash flow information:		
Cash paid for interest, net of amounts capitalized	$8,970	$10,684
Cash paid for income taxes, net of refund	$71	$4
Decrease (increase) in accrued capital improvements and development costs	$2,616	$(554)
Mortgage notes payable assumed in connection with the acquisition of real estate	$100,861	$—

See accompanying notes to the consolidated financial statements.

WASHINGTON REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
MARCH 31, 2014
(UNAUDITED)

NOTE 1: NATURE OF BUSINESS

Washington Real Estate Investment Trust ("Washington REIT"), a Maryland real estate investment trust, is a self-administered, self-managed equity real estate investment trust, successor to a trust organized in 1960. Our business consists of the ownership and operation of income-producing real estate properties in the greater Washington metro region. We own a diversified portfolio of office buildings, multifamily buildings and retail centers.

Federal Income Taxes

We believe that we qualify as a real estate investment trust ("REIT") under Sections 856-860 of the Internal Revenue Code and intend to continue to qualify as such. To maintain our status as a REIT, we are required to distribute 90% of our ordinary taxable income to our shareholders. When selling properties, we have the option of (a) reinvesting the sales proceeds of properties sold, allowing for a deferral of income taxes on the sale, (b) paying out capital gains to the shareholders with no tax to Washington REIT or (c) treating the capital gains as having been distributed to the shareholders, paying the tax on the gain deemed distributed and allocating the tax paid as a credit to the shareholders.

During the first quarter of 2014, we closed on Transactions III (for the sale of Woodburn Medical Park I and II) and IV (for the sale of Prosperity Medical Center I, II and III) of the Medical Office Portfolio sale for an aggregate contract sales price of $193.6 million. We have identified a portion of the sold Medical Office Portfolio properties for tax deferred exchange under Section 1031 of the Internal Revenue Code. The remaining sales proceeds designated for Section 1031 exchanges as of March 31, 2014 are reported as restricted cash on our consolidated balance sheets.

Generally, and subject to our ongoing qualification as a REIT, no provisions for income taxes are necessary except for taxes on undistributed REIT taxable income and taxes on the income generated by our taxable REIT subsidiaries ("TRSs"). Our TRSs are subject to corporate federal and state income tax on their taxable income at regular statutory rates or as calculated under the alternative minimum tax, as appropriate. There were no material income tax provisions or material net deferred income tax items for our TRSs for the three months ended March 31, 2014 and 2013.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND BASIS OF PRESENTATION

Significant Accounting Policies

We have prepared our consolidated financial statements using the accounting policies described in our Annual Report on Form 10-K for the year ended December 31, 2013.

New Accounting Pronouncements

In April 2014, the Financial Accounting Standards Board ("FASB") issued ASU No. 2014-08, Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity, which changes the requirements for reporting discontinued operations. Specifically, under this ASU only those disposals of components of an entity that represent a strategic shift that has (or will have) a major effect on an entity's operations and financial results will be reported as discontinued operations in the financial statements. The primary impact of this ASU is that we are no longer required to report the disposal of every operating property in discontinued operations. Adoption of this ASU is required for all disposals (or classifications as held for sale) of components of an entity that occur within annual periods beginning on or after after December 15, 2014, and interim periods within those years. Early adoption is permitted, but only for disposals (or classifications as held for sale) that have not been reported in financial statements previously issued or available for issuance. We early adopted this ASU effective for the first quarter of 2014.

Principles of Consolidation and Basis of Presentation

The accompanying unaudited consolidated financial statements include the consolidated accounts of Washington REIT, our majority-owned subsidiaries and entities in which Washington REIT has a controlling interest, including where Washington REIT has been determined to be a primary beneficiary of a variable interest entity ("VIE"). See note 3 for additional information on the properties for which there is a noncontrolling interest. All intercompany balances and transactions have been eliminated in consolidation.

We have prepared the accompanying unaudited financial statements pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and note disclosures normally included in annual financial statements prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) have been condensed or omitted pursuant to those rules and regulations, although we believe that the disclosures made are adequate to make the information presented not misleading.

In addition, in the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of the results for the periods presented have been included. These unaudited financial statements should be read in conjunction with the financial statements and notes included in our Annual Report on Form 10-K for the year ended December 31, 2013.

Within these notes to the financial statements, we refer to the three months ended March 31, 2014 and March 31, 2013 as the "2014 Quarter" and the "2013 Quarter," respectively.

Use of Estimates in the Financial Statements

The preparation of financial statements in conformity with GAAP requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications

Certain prior period amounts have been reclassified to conform to the current period presentation due to the reclassification of certain properties as discontinued operations (see note 3).

NOTE 3: REAL ESTATE

Acquisitions

Washington REIT acquired the following properties during the 2014 Quarter:

Acquisition Date	Property Name	Type	Rentable Square Feet	Contract Purchase Price (in thousands)
February 21, 2014	Yale West (216 units)	Multifamily	N/A	$73,000
March 26, 2014	The Army Navy Club Building	Office	108,000	79,000
			108,000	$152,000

The results of operations from the acquired operating properties are included in the consolidated statements of income as of their acquisition dates.

The revenue and earnings of our 2014 acquisitions are as follows (amounts in thousands):

	Three Months Ended March 31, 2014
Real estate revenues	$757
Net loss	(815)

We record the acquired physical assets (land, building and tenant improvements), and in-place leases (absorption, tenant origination costs, leasing commissions, and net lease intangible assets/liabilities), and any other liabilities at their fair values.

We have recorded the total purchase price of the above acquisitions as follows (in thousands):

Land	$45,481
Buildings	96,816
Tenant origination costs	3,856
Leasing commissions/absorption costs	7,335
Net lease intangible assets	3,499
Net lease intangible liabilities	(54)
Fair value of assumed mortgages	(107,125)
Furniture fixtures and equipment	932
Total	$50,740

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The weighted remaining average life for the 2014 acquisition components above, other than land and building, are 85 months for tenant origination costs, 54 months for leasing commissions/absorption costs, 89 months for net lease intangible assets and 211 months for net lease intangible liabilities.
The difference in the total contract purchase price of $152.0 million for the 2014 acquisitions and the acquisition cost per the consolidated statement of cash flows of $48.1 million is primarily due to the assumption of two mortgage notes secured by Yale West and The Army Navy Club Building for an aggregate $100.9 million and the payment of a $3.6 million deposit for Yale West in 2013.

The following unaudited pro-forma combined condensed statements of operations are for the 2014 and 2013 Quarters as if the above described acquisitions had occurred at the beginning of the period of acquisition and the same period in the year prior to acquisition. The unaudited pro-forma information does not purport to be indicative of the results that actually would have occurred if the acquisitions had been in effect for the 2014 and 2013 Quarters. The unaudited data presented is in thousands, except per share data.

	Three Months Ended March 31,	
	2014	2013
Real estate revenues	$70,921	$67,627
Loss from continuing operations	(3,329)	(934)
Net income	103,490	5,543
Diluted earnings per share	1.55	0.08

Redevelopment
In the office segment, we have an active redevelopment project to renovate 7900 Westpark Drive. Our total investment in the renovation at 7900 Westpark Drive is expected to be $35.0 million. As of March 31, 2014 and December 31, 2013, we had invested $6.9 million and $3.6 million, respectively, in the renovation.

Variable Interest Entities
In June 2011, we executed a joint venture operating agreement with a real estate development company to develop a mid-rise multifamily property at 650 North Glebe Road in Arlington, Virginia. We estimate the total cost of the project to be $49.9 million. During the first quarter of 2013, we secured third-party debt financing for approximately 70% of the project's cost. Washington REIT is the 90% owner of the joint venture and will have management and leasing responsibilities when the project is completed and stabilized (defined as 90% of the residential units leased). The real estate development company owns 10% of the joint venture and is responsible for the development and construction of the property. The joint venture currently expects to complete this development project during the fourth quarter of 2014.

In November 2011, we executed a joint venture operating agreement with a real estate development company to develop a high-rise multifamily property at 1225 First Street (formerly 1219 First Street) in Alexandria, Virginia. We estimate the total cost of the project to be $95.3 million, with approximately 70% of the project financed with debt. Washington REIT is the 95% owner of the joint venture and will have management and leasing responsibilities if the project is completed and stabilized. The real estate development company owns 5% of the joint venture and is responsible for the development and construction of the property. In the first quarter of 2013, we decided to delay commencement of construction due to market conditions and concerns of oversupply. We continue to reassess this project on a periodic basis going forward.

We have determined that the 650 North Glebe Road and 1225 First Street joint ventures are variable interest entities (“VIE's”) primarily based on the fact that the equity investment at risk is not sufficient to permit either entity to finance its activities without additional financial support. We expect that 70% of the total development costs for each project would be financed through debt. We have also determined that Washington REIT is the primary beneficiary of each VIE due to the fact that Washington REIT is providing 90% to 95% of the equity contributions and will manage each property after stabilization.

We include the joint venture land acquisitions on our consolidated balance sheets in properties under development or held for future development. As of March 31, 2014 and December 31, 2013, the land and capitalized development costs are as follows (in thousands):

	March 31, 2014	December 31, 2013
650 North Glebe	$31,747	$27,343
1225 First Street	20,793	20,788

As of March 31, 2014 and December 31, 2013, the accounts payable and accrued liabilities related to the joint ventures are as follows (in thousands):

	March 31, 2014	December 31, 2013
650 North Glebe	$2,494	$1,785
1225 First Street	94	39

On February 21, 2013, Washington REIT, through its consolidated joint venture to develop a mid-rise multifamily property at 650 North Glebe Road, entered into a construction loan agreement with Citizens Bank for $33.0 million. The loan bears interest at LIBOR plus 2.15%, which decreases to LIBOR plus 2.0% upon completion of construction and the joint venture not being in default. The loan matures on February 21, 2016, with two one year extension options exercisable by the joint venture, subject to fees and compliance with certain provisions in the loan agreement. As of March 31, 2014, the consolidated joint venture had $10.5 million outstanding on this construction loan agreement.

Discontinued Operations

We dispose of assets that no longer meet our long-term strategy or return objectives and where market conditions for sale are favorable. The proceeds from the sales may be reinvested into other properties, used to fund development operations or to support other corporate needs, or distributed to our shareholders. Properties are considered held for sale when they meet the criteria specified (see "Discontinued Operations" in note 2 of the consolidated financial statements included in Washington REIT's Annual Report on Form 10-K for the year ended December 31, 2013). Depreciation on these properties is discontinued at that time, but operating revenues, other operating expenses and interest continue to be recognized until the date of sale.

In September 2013, we entered into four separate purchase and sale agreements to effectuate the sale of our entire medical office segment (including land held for development at 4661 Kenmore Avenue) and two office buildings (Woodholme Center and 6565 Arlington Boulevard) for an aggregate purchase price of $500.8 million. The sale was structured as four transactions. Transactions I and II closed in November 2013 and Transactions III and IV closed in January 2014.

The results of our medical office segment are summarized as follows (amounts in thousands, except per share data):

	Three Months Ended March 31,	
	2014	2013
Real estate revenues	$892	$11,028
Net income	546	2,821
Basic net income per share	0.01	0.04
Diluted net income per share	0.01	0.04

We sold the following properties in 2014 and 2013:

Property Name	Segment	Rentable Square Feet	Contract Purchase Price (In thousands)	Gain on Sale (In thousands)

Medical Office Portfolio Transactions III & IV (1)	Medical Office	427,000	$193,561	$106,273
	Total 2014	427,000	$193,561	$106,273
Atrium Building	Office	79,000	$15,750	$3,195
Medical Office Portfolio Transactions I & II (2)	Medical Office / Office	1,093,000	307,189	18,949
	Total 2013	1,172,000	$322,939	$22,144

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(1) Woodburn Medical Park I and II and Prosperity Medical Center I, II and III.

(2) 2440 M Street, 15001 Shady Grove Road, 15505 Shady Grove Road, 19500 at Riverside Park (formerly Lansdowne Medical Office Building), 9707 Medical Center Drive, CentreMed I and II, 8301 Arlington Boulevard, Sterling Medical Office Building, Shady Grove Medical Village II, Alexandria Professional Center, Ashburn Farm Office Park I, Ashburn Farm Office Park II, Ashburn Farm Office Park III, Woodholme Medical Office Building, two office properties (6565 Arlington Boulevard and Woodholme Center) and undeveloped land at 4661 Kenmore Avenue.

As of March 31, 2014 and December 31, 2013, investment in real estate for properties sold or held for sale, all of which were in the medical office segment, was as follows (in thousands):

	March 31, 2014	December 31, 2013
Investment in real estate sold or held for sale	$—	$125,967
Less accumulated depreciation	—	(46,066)
Investment in real estate sold or held for sale, net	$—	$79,901

Income from operations of properties sold or held for sale for the three months ended March 31, 2014 and 2013 was as follows (in thousands):

	Three Months Ended March 31,	
	2014	2013
Revenues	$892	$12,711
Property expenses	(346)	(4,699)
Depreciation and amortization	—	(4,401)
Interest expense	—	(328)
Income from operations of properties sold or held for sale	$546	$3,283

Income from operations of properties sold or held for sale by property for the three months ended March 31, 2014 and 2013 was as follows (in thousands):

		Three Months Ended March 31,	
Property	Segment	2014	2013
Atrium Building	Office	$—	$185
Medical Office Portfolio	Medical Office / Office	546	3,098
		$546	$3,283

NOTE 4: MORTGAGE NOTES PAYABLE

In February 2014, we assumed a $48.2 million mortgage note as partial consideration for the acquisition of Yale West. This mortgage note bears interest at 5.55% per annum. The fair value interest rate on this mortgage note is 3.75% based on quotes obtained for similar loans. We recorded the mortgage note at its estimated fair value of $54.0 million. Principal and interest are payable monthly until January 1, 2052, at which time all unpaid principal and interest are payable in full. The loan may be prepaid, without penalty, on January 31, 2022 or thereafter on the last business day of the month until maturity, with thirty days prior written notice to the lender.

In March 2014, we assumed a $52.7 million mortgage note as partial consideration for acquisition of The Army Navy Club Building. This mortgage note bears interest at 3.45% per annum. The fair value interest rate on this mortgage note is 3.18% based on quotes obtained for similar loans. We recorded the mortgage at its estimated fair value of $53.2 million. Principal and interest are payable monthly until May 1, 2017, at which time all unpaid principal and interest are payable in full.

NOTE 5: UNSECURED LINES OF CREDIT PAYABLE

As of March 31, 2014, we maintained a $100.0 million unsecured line of credit maturing in June 2015 ("Credit Facility No. 1") and a $400.0 million unsecured line of credit maturing in July 2016 ("Credit Facility No. 2"). Credit

Facilities No. 1 and No. 2 have accordion features that allow us to increase the facilities to $200.0 million and $600.0 million, respectively, subject to additional lender commitments.

The amounts of these lines of credit unused and available at March 31, 2014 are as follows (in thousands):

	Credit Facility No. 1	Credit Facility No. 2
Committed capacity	$100,000	$400,000
Borrowings outstanding	—	—
Unused and available	$100,000	$400,000

We had no borrowings and no repayments on the unsecured lines of credit during the 2014 Quarter.

NOTE 6: NOTES PAYABLE

We repaid without penalty the $100.0 million of our 5.25% unsecured notes on their due date of January 15, 2014, using proceeds from the sale of the Medical Office Portfolio.

NOTE 7: STOCK BASED COMPENSATION

Washington REIT maintains short-term ("STIP") and long-term ("LTIP") incentive plans that allow for stock-based awards to officers and non-officer employees. Stock based awards are provided to officers and non-officer employees, as well as trustees, under the Washington Real Estate Investment Trust 2007 Omnibus Long-Term Incentive Plan which allows for awards in the form of restricted shares, restricted share units, options and other awards up to an aggregate of 2,000,000 shares over the ten year period in which the plan will be in effect. Restricted share units are converted into shares of our stock upon full vesting through the issuance of new shares.

Total Compensation Expense

Total compensation expense recognized in the consolidated financial statements for all outstanding share based awards was $1.1 million and $1.0 million for the 2014 and 2013 Quarters, respectively.

Restricted Share Awards

The total fair values of restricted share awards vested was $0.2 million and $0.5 million for the 2014 and 2013 Quarters, respectively.

The total unvested restricted share awards at March 31, 2014 was 242,218 shares, which had a weighted average grant date fair value of $25.48 per share. As of March 31, 2014, the total compensation cost related to unvested restricted share awards was $3.1 million, which we expect to recognize over a weighted average period of 18 months.

NOTE 8: FAIR VALUE DISCLOSURES

Assets and Liabilities Measured at Fair Value

For assets and liabilities measured at fair value on a recurring basis, quantitative disclosures about the fair value measurements are required to be disclosed separately for each major category of assets and liabilities, as follows:

Level 1: Quoted prices in active markets for identical assets

Level 2: Significant other observable inputs

Level 3: Significant unobservable inputs

The only assets or liabilities we had at March 31, 2014 and December 31, 2013 that are recorded at fair value on a recurring basis are the assets held in the Supplemental Executive Retirement Program (“SERP”). We base the valuations related to this asset on assumptions derived from significant other observable inputs and accordingly these valuations fall into Level 2 in the fair value hierarchy.

The fair values of these assets at March 31, 2014 and December 31, 2013 were as follows (in thousands):

	March 31, 2014				December 31, 2013			
	Fair Value	Level 1	Level 2	Level 3	Fair Value	Level 1	Level 2	Level 3
Assets:								
SERP	$3,382	$—	$3,382	$—	$3,290	$—	$3,290	$—

Financial Assets and Liabilities Not Measured at Fair Value

The following disclosures of estimated fair value were determined by management using available market information and established valuation methodologies, including discounted cash flow. Many of these estimates involve significant judgment. The estimated fair value disclosed may not necessarily be indicative of the amounts we could realize on disposition of the financial instruments. The use of different market assumptions or estimation methodologies could have an effect on the estimated fair value amounts. In addition, fair value estimates are made at a point in time and thus, estimates of fair value subsequent to March 31, 2014 may differ significantly from the amounts presented. Following is a summary of significant methodologies used in estimating fair values and a schedule of fair values at March 31, 2014.

Cash and Cash Equivalents and Restricted Cash

Cash and cash equivalents and restricted cash include cash and commercial paper with original maturities of less than 90 days, which are valued at the carrying value, which approximates fair value due to the short maturity of these instruments (Level 1 inputs).

Notes Receivable

We acquired a note receivable ("2445 M Street note") in 2008 with the purchase of 2445 M Street. We estimate the fair value of the 2445 M Street note based on a discounted cash flow methodology using market discount rates (Level 3 inputs).

Debt

Mortgage notes payable consist of instruments in which certain of our real estate assets are used for collateral. We estimate the fair value of the mortgage notes payable by discounting the contractual cash flows at a rate equal to the relevant treasury rates (with respect to the timing of each cash flow) plus credit spreads estimated through independent comparisons to real estate assets or loans with similar characteristics. Lines of credit payable consist of bank facilities which we use for various purposes including working capital, acquisition funding or capital improvements. The lines of credit advances are priced at a specified rate plus a spread. We estimate the market value based on a comparison of the spreads of the advances to market given the adjustable base rate. We estimate the fair value of the notes payable by discounting the contractual cash flows at a rate equal to the relevant treasury rates (with respect to the timing of each cash flow) plus credit spreads derived using the relevant securities' market prices. We classify these fair value measurements as Level 3 as we use significant unobservable inputs and management judgment due to the absence of quoted market prices.

As of March 31, 2014 and December 31, 2013, the carrying values and estimated fair values of our financial instruments were as follows (in thousands):

	March 31, 2014		December 31, 2013	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Cash and cash equivalents	$62,080	$62,080	$130,343	$130,343
Restricted cash	107,039	107,039	9,189	9,189
2445 M Street note	6,280	7,184	6,070	6,803
Mortgage notes payable	404,359	423,454	294,671	313,476
Notes payable	746,830	772,063	846,703	856,171

NOTE 9: EARNINGS PER COMMON SHARE

We determine “Basic earnings per share” using the two-class method as our unvested restricted share awards and units have non-forfeitable rights to dividends and are therefore considered participating securities. We compute basic earnings per share by dividing

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net income attributable to the controlling interest less the allocation of undistributed earnings to unvested restricted share awards and units by the weighted-average number of common shares outstanding for the period.
We also determine "Diluted earnings per share" under the two-class method with respect to the unvested restricted share awards. We further evaluate any other potentially dilutive securities at the end of the period and adjust the basic earnings per share calculation for the impact of those securities that are dilutive. Our dilutive earnings per share calculation includes the dilutive impact of employee stock options based on the treasury stock method and our incentive share awards with performance or market conditions under the contingently issuable method. The diluted earnings per share calculation also considers our operating partnership units under the if-converted method. We have a loss from continuing operations for the 2014 Quarter, and therefore diluted earnings per share is calculated in the same manner as basic earnings per share for this quarter.

The computations of basic and diluted earnings per share for the three months ended March 31, 2014 and 2013 were as follows (in thousands, except per share data):

	Three Months Ended March 31,	
	2014	2013
Numerator:		
(Loss) income from continuing operations	$(2,265)	$857
Allocation of earnings to unvested restricted share awards	(10)	(14)
Adjusted (loss) income from continuing operations attributable to the controlling interests	(2,275)	843
Income from discontinued operations, including gain on sale of real estate, net of taxes	106,819	6,478
Allocation of earnings to unvested restricted share awards	(285)	(106)
Adjusted income from discontinuing operations attributable to the controlling interests	106,534	6,372
Adjusted net income attributable to the controlling interests	$104,259	$7,215
Denominator:		
Weighted average shares outstanding – basic	66,701	66,393
Effect of dilutive securities:		
Operating partnership units	—	117
Employee stock options and restricted share awards	—	9
Weighted average shares outstanding – diluted	66,701	66,519
Earnings (loss) per common share, basic:		
Continuing operations	$(0.04)	$0.01
Discontinued operations	1.60	0.10
	$1.56	$0.11
Earnings (loss) per common share, diluted:		
Continuing operations	$(0.04)	$0.01
Discontinued operations	1.60	0.10
	$1.56	$0.11

NOTE 10: SEGMENT INFORMATION

We have three reportable segments: office, retail and multifamily. Office buildings provide office space for various types of businesses and professions. Retail shopping centers are typically grocery store anchored neighborhood centers that include other small shop tenants or regional power centers with several junior box tenants. Multifamily properties provide rental housing for individuals and families throughout the Washington metropolitan area. During the 2014 Quarter, we completed the sale of our medical office segment (see note 3).
We evaluate performance based upon operating income from the combined properties in each segment. Our reportable operating segments are consolidations of similar properties. GAAP requires that segment disclosures present the measure(s) used by the chief operating decision maker for purposes of assessing segments' performance. Net operating income is a key measurement of our segment profit and loss. Net operating income is defined as segment real estate rental revenue less segment real estate expenses.

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The following tables present revenues, net operating income, capital expenditures and total assets for the 2014 and 2013 Quarters from these segments, and reconciles net operating income of reportable segments to net income attributable to the controlling interests as reported (in thousands):

	Three Months Ended March 31, 2014					
	Office	Retail	Multifamily	Corporate and Other	Consolidated	
Real estate rental revenue	$39,064	$14,625	$14,922	$—	$68,611	
Real estate expenses	15,696	4,231	6,415	—	26,342	
Net operating income	$23,368	$10,394	$8,507	$—	$42,269	
Depreciation and amortization					(22,753	)
General and administrative					(4,429	)
Acquisition costs					(3,045	)
Interest expense					(14,530	)
Other income					223	
Discontinued operations:						
Income from operations of properties sold or held for sale					546	
Gain on sale of real estate					106,273	
Net income					104,554	
Less: Net income attributable to noncontrolling interests in subsidiaries					—	
Net income attributable to the controlling interests					$104,554	
Capital expenditures	$8,703	$110	$1,556	$17	$10,386	
Total assets	$1,151,585	$341,134	$392,531	$189,922	$2,075,172	