
UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

- Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the quarterly period ended **June 30, 2008**

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 **1-10709**

PS BUSINESS PARKS, INC.

(Exact name of registrant as specified in its charter)

California
(State or Other Jurisdiction
of Incorporation)

95-4300881
(I.R.S. Employer
Identification Number)

701 Western Avenue, Glendale, California 91201-2397
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: **(818) 244-8080**

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 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 Accelerated filer Non-accelerated filer Smaller reporting company
(Do not check if a smaller reporting company)

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

Yes No

As of July 31, 2008, the number of shares of the registrant's common stock, \$0.01 par value per share, outstanding was 20,441,499.

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PS BUSINESS PARKS, INC.

CONSOLIDATED BALANCE SHEETS
(In thousands, except share data)

	June 30, 2008 (Unaudited)	December 31, 2007
ASSETS		
Cash and cash equivalents	\$ 38,309	\$ 35,041
Real estate facilities, at cost:		
Land	494,849	494,849
Buildings and equipment	<u>1,503,218</u>	<u>1,484,049</u>
	1,998,067	1,978,898
Accumulated depreciation	<u>(589,657)</u>	<u>(539,857)</u>
	1,408,410	1,439,041
Land held for development	<u>7,869</u>	<u>7,869</u>
	1,416,279	1,446,910
Rent receivable	1,720	2,240
Deferred rent receivable	21,844	21,927
Other assets	<u>7,149</u>	<u>10,465</u>
Total assets	<u>\$ 1,485,301</u>	<u>\$ 1,516,583</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
Accrued and other liabilities	\$ 49,829	\$ 51,058
Mortgage notes payable	<u>60,037</u>	<u>60,725</u>
Total liabilities	109,866	111,783
Minority interests:		
Preferred units	94,750	94,750
Common units	148,620	154,470
Commitments and contingencies Shareholders' equity:		
Preferred stock, \$0.01 par value, 50,000,000 shares authorized, 28,650 shares issued and outstanding at June 30, 2008 and December 31, 2007	716,250	716,250
Common stock, \$0.01 par value, 100,000,000 shares authorized, 20,439,118 and 20,777,219 shares issued and outstanding at June 30, 2008 and December 31, 2007, respectively	204	207
Paid-in capital	357,305	371,267
Cumulative net income	586,007	552,069
Cumulative distributions	<u>(527,701)</u>	<u>(484,213)</u>
Total shareholders' equity	<u>1,132,065</u>	<u>1,155,580</u>
Total liabilities and shareholders' equity	<u>\$ 1,485,301</u>	<u>\$ 1,516,583</u>

See accompanying notes.

PS BUSINESS PARKS, INC.

CONSOLIDATED STATEMENTS OF INCOME
(Unaudited, in thousands, except per share data)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
Revenues:				
Rental income	\$ 70,446	\$ 67,275	\$ 140,557	\$ 132,399
Facility management fees	177	182	372	365
Total operating revenues	<u>70,623</u>	<u>67,457</u>	<u>140,929</u>	<u>132,764</u>
Expenses:				
Cost of operations	21,939	21,022	44,429	41,461
Depreciation and amortization	25,120	24,916	50,567	46,556
General and administrative	2,085	2,112	4,131	3,814
Total operating expenses	<u>49,144</u>	<u>48,050</u>	<u>99,127</u>	<u>91,831</u>
Other income and expenses:				
Interest and other income	282	1,189	610	2,990
Interest expense	(990)	(1,012)	(1,983)	(2,119)
Total other income and expenses	<u>(708)</u>	<u>177</u>	<u>(1,373)</u>	<u>871</u>
Income before minority interests	<u>20,771</u>	<u>19,584</u>	<u>40,429</u>	<u>41,804</u>
Minority interests:				
Minority interest in income — preferred units	(1,752)	(1,752)	(3,504)	(3,351)
Minority interest in income — common units	(1,639)	(1,294)	(2,987)	(3,324)
Total minority interests	<u>(3,391)</u>	<u>(3,046)</u>	<u>(6,491)</u>	<u>(6,675)</u>
Net income	<u>17,380</u>	<u>16,538</u>	<u>33,938</u>	<u>35,129</u>
Net income allocable to preferred shareholders:				
Preferred stock distributions	12,757	12,757	25,513	25,425
Net income allocable to common shareholders	<u>\$ 4,623</u>	<u>\$ 3,781</u>	<u>\$ 8,425</u>	<u>\$ 9,704</u>
Net income per common share:				
Basic	\$ 0.23	\$ 0.18	\$ 0.41	\$ 0.46
Diluted	\$ 0.22	\$ 0.17	\$ 0.41	\$ 0.45
Weighted average common shares outstanding:				
Basic	<u>20,430</u>	<u>21,334</u>	<u>20,432</u>	<u>21,325</u>
Diluted	<u>20,686</u>	<u>21,681</u>	<u>20,665</u>	<u>21,692</u>

See accompanying notes.

PS BUSINESS PARKS, INC.

CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY
FOR THE SIX MONTHS ENDED JUNE 30, 2008
(Unaudited, in thousands, except share data)

	Preferred Stock		Common Stock		Paid-in Capital	Cumulative Net Income	Cumulative Distributions	Total Shareholders' Equity
	Shares	Amount	Shares	Amount				
Balances at December 31, 2007	28,650	\$ 716,250	20,777,219	\$ 207	\$ 371,267	\$ 552,069	\$ (484,213)	\$ 1,155,580
Repurchase of common stock	—	—	(370,042)	(3)	(18,321)	—	—	(18,324)
Exercise of stock options	—	—	17,500	—	447	—	—	447
Stock compensation	—	—	14,441	—	1,502	—	—	1,502
Net income	—	—	—	—	—	33,938	—	33,938
Distributions:								
Preferred stock	—	—	—	—	—	—	(25,513)	(25,513)
Common stock	—	—	—	—	—	—	(17,975)	(17,975)
Adjustment to minority interests underlying ownership	—	—	—	—	2,410	—	—	2,410
Balances at June 30, 2008	<u>28,650</u>	<u>\$ 716,250</u>	<u>20,439,118</u>	<u>\$ 204</u>	<u>\$ 357,305</u>	<u>\$ 586,007</u>	<u>\$ (527,701)</u>	<u>\$ 1,132,065</u>

See accompanying notes.

PS BUSINESS PARKS, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited, in thousands)

	For the Six Months Ended June 30,	
	2008	2007
Cash flows from operating activities:		
Net income	\$ 33,938	\$ 35,129
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization expense	50,567	46,556
In-place lease adjustment	(96)	(9)
Lease incentives net of tenant improvement reimbursements	(69)	110
Amortization of mortgage premium	(128)	(122)
Minority interest in income	6,491	6,675
Stock compensation expense	1,502	1,703
Decrease in receivables and other assets	3,514	2,096
Increase (decrease) in accrued and other liabilities	2,644	(507)
Total adjustments	<u>64,425</u>	<u>56,502</u>
Net cash provided by operating activities	<u>98,363</u>	<u>91,631</u>
Cash flows from investing activities:		
Capital improvements to real estate facilities	(19,936)	(17,272)
Acquisition of real estate facilities	—	(113,812)
Net cash used in investing activities	<u>(19,936)</u>	<u>(131,084)</u>
Cash flows from financing activities:		
Principal payments on mortgage notes payable	(560)	(584)
Repayment of mortgage note payable	—	(4,950)
Net proceeds from the issuance of preferred units	—	11,665
Net proceeds from the issuance of preferred stock	—	139,567
Proceeds from the exercise of stock options	447	365
Shelf registration costs	—	(88)
Repurchase of common stock	(21,626)	—
Redemption of preferred stock	—	(50,000)
Distributions paid to preferred shareholders	(25,513)	(25,425)
Distributions paid to minority interests — preferred units	(3,504)	(3,351)
Distributions paid to common shareholders	(17,975)	(15,571)
Distributions paid to minority interests — common units	(6,428)	(5,333)
Net cash (used in) provided by financing activities	<u>(75,159)</u>	<u>46,295</u>
Net increase in cash and cash equivalents	3,268	6,842
Cash and cash equivalents at the beginning of the period	35,041	67,017
Cash and cash equivalents at the end of the period	<u>\$ 38,309</u>	<u>\$ 73,859</u>
Supplemental schedule of non cash investing and financing activities:		
Adjustment to minority interest to underlying ownership:		
Minority interest — common units	\$ (2,410)	\$ (941)
Paid-in capital	\$ 2,410	\$ 941

See accompanying notes.

PS BUSINESS PARKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008

1. Organization and description of business

PS Business Parks, Inc. ("PSB") was incorporated in the state of California in 1990. As of June 30, 2008, PSB owned approximately 73.7% of the common partnership units of PS Business Parks, L.P. (the "Operating Partnership" or "OP"). The remaining common partnership units were owned by Public Storage ("PS"). PSB, as the sole general partner of the Operating Partnership, has full, exclusive and complete responsibility and discretion in managing and controlling the Operating Partnership. PSB and the Operating Partnership are collectively referred to as the "Company."

The Company is a fully-integrated, self-advised and self-managed real estate investment trust ("REIT") that acquires, develops, owns and operates commercial properties, primarily multi-tenant flex, office and industrial space. As of June 30, 2008, the Company owned and operated approximately 19.6 million rentable square feet of commercial space located in eight states. The Company also manages approximately 1.4 million rentable square feet on behalf of PS and its affiliated entities.

Any reference to the number of properties or square footage are unaudited and outside the scope of the Company's independent registered public accounting firm's review of the Company's financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States).

2. Summary of significant accounting policies

Basis of presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information and with instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) necessary for a fair presentation have been included. Operating results for the three and six months ended June 30, 2008 are not necessarily indicative of the results that may be expected for the year ended December 31, 2008. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2007.

The accompanying consolidated financial statements include the accounts of PSB and the Operating Partnership. All significant inter-company balances and transactions have been eliminated in the consolidated financial statements.

Use of estimates

The preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from these estimates.

Allowance for doubtful accounts

The Company monitors the collectibility of its receivable balances including the deferred rent receivable on an ongoing basis. Based on these reviews, the Company maintains an allowance for doubtful accounts for estimated losses resulting from the possible inability of tenants to make contractual rent payments to the Company. A provision for doubtful accounts is recorded during each period. The allowance for doubtful accounts, which represents the cumulative allowances less write-offs of uncollectible rent, is netted against tenant and other receivables on the consolidated balance sheets. Tenant receivables are net of an allowance for uncollectible accounts totaling \$300,000 at June 30, 2008 and December 31, 2007.

Financial instruments

The methods and assumptions used to estimate the fair value of financial instruments are described below. The Company has estimated the fair value of financial instruments using available market information and appropriate valuation methodologies. Considerable judgment is required in interpreting market data to develop estimates of market value. Accordingly, estimated fair values are not necessarily indicative of the amounts that could be realized in current market exchanges.

The Company considers all highly liquid investments with a remaining maturity of three months or less at the date of purchase to be cash equivalents. Due to the short period to maturity of the Company's cash and cash equivalents, accounts receivable, other assets and accrued and other liabilities, the carrying values as presented on the consolidated balance sheets are reasonable estimates of fair value. Based on borrowing rates currently available to the Company, the carrying amount of debt approximates fair value.

Financial assets that are exposed to credit risk consist primarily of cash and cash equivalents and receivables. Cash and cash equivalents, which consist primarily of short-term investments, including commercial paper, are only invested in entities with an investment grade rating. Receivables are comprised of balances due from a large number of customers. Balances that the Company expects to become uncollectible are reserved for or written off.

Real estate facilities

Real estate facilities are recorded at cost. Costs related to the renovation or improvement of the properties are capitalized. Expenditures for repairs and maintenance are expensed as incurred. Expenditures that are expected to benefit a period greater than two years and exceed \$2,000 are capitalized and depreciated over the estimated useful life. Buildings and equipment are depreciated on the straight-line method over the estimated useful lives, which are generally 30 and five years, respectively. Leasing costs in excess of \$1,000 for leases with terms greater than two years are capitalized and depreciated over their estimated useful lives. Leasing costs for leases of less than two years or less than \$1,000 are expensed as incurred. Interest cost and property taxes incurred during the period of construction of real estate facilities are capitalized.

Intangible assets/liabilities

Intangible assets and liabilities include above-market and below-market in-place lease values of acquired properties based on the present value (using an interest rate which reflects the risks associated with the leases acquired) of the difference between (i) the contractual amounts to be paid pursuant to the in-place leases and (ii) management's estimate of fair market lease rates for the corresponding in-place leases, measured over a period equal to the remaining non-cancelable term of the lease. The capitalized above-market and below-market lease values (included in other assets and accrued liabilities in the accompanying consolidated balance sheets) are amortized, net, to rental income over the remaining non-cancelable terms of the respective leases. The Company recorded net amortization of \$48,000 and \$36,000 of intangible assets and liabilities resulting from the above-market and below-market lease values during the three months ended June 30, 2008 and 2007, respectively. Amortization was \$96,000 and \$9,000 for each of the six months ended June 30, 2008 and 2007, respectively. As of June 30, 2008, the value of in-place leases resulted in a net intangible asset of \$300,000, net of \$892,000 of accumulated amortization, and a net intangible liability of \$801,000, net of \$556,000 of accumulated amortization. As of December 31, 2007, the value of in-place leases resulted in a net intangible asset of \$419,000, net of \$773,000 of accumulated amortization, and a net intangible liability of \$1.0 million, net of \$340,000 of accumulated amortization.

Evaluation for asset impairments

The Company evaluates its assets used in operations by identifying indicators of impairment and by comparing the sum of the estimated undiscounted future cash flows for each asset to the asset's carrying value. When indicators of impairment are present and the sum of the undiscounted future cash flows is less than the carrying value of such asset, an impairment loss is recorded equal to the difference between the asset's current carrying value and its value based on discounting its estimated future cash flows. In addition, the Company evaluates its assets held for disposition for impairment. Assets held for disposition are reported at the lower of their carrying value or fair value, less cost of disposition. At June 30, 2008, the Company did not consider any assets to be impaired.

Stock-based compensation

Stock-based compensation is accounted for in accordance with Statement of Financial Accounting Standards ("SFAS") No. 123(R) "Share-Based Payment," which requires all share-based payments to employees, including grants of employee stock options, to be recognized in the income statement based on their fair values. See Note 11.

Revenue and expense recognition

Revenue is recognized in accordance with Staff Accounting Bulletin No. 104 of the Securities and Exchange Commission, Revenue Recognition in Financial Statements ("SAB 104"). SAB 104 requires that four basic criteria must be met before revenue can be recognized: persuasive evidence of an arrangement exists; the delivery has occurred or services rendered; the fee is fixed or determinable; and collectibility is reasonably assured. All leases are classified as operating leases. Rental income is recognized on a straight-line basis over the terms of the leases. Straight-line rent is recognized for all tenants with contractual increases in rent that are not included on the Company's credit watch list. Deferred rent receivables represent rental revenue recognized on a straight-line basis in excess of billed rents. Reimbursements from tenants for real estate taxes and other recoverable operating expenses are recognized as revenues in the period the applicable costs are incurred. Property management fees are recognized in the period earned.

Costs incurred in connection with leasing (primarily tenant improvements and lease commissions) are capitalized and amortized over the lease period.

Gains from sales of real estate

The Company recognizes gains from the sale of real estate at the time of the sale using the full accrual method, provided that various criteria related to the terms of the transactions and any subsequent involvement by the Company with the properties sold are met. If the criteria are not met, the Company defers the gains and recognizes them when the criteria are met or using the installment or cost recovery methods as appropriate under the circumstances.

General and administrative expense

General and administrative expense includes executive and other compensation, office expense, professional fees, state income taxes and other such administrative items.

Income taxes

The Company qualified and intends to continue to qualify as a REIT, as defined in Section 856 of the Internal Revenue Code. As a REIT, the Company is not subject to federal income tax to the extent that it distributes its taxable income to its shareholders. A REIT must distribute at least 90% of its taxable income each year. In addition, REITs are subject to a number of organizational and operating requirements. If the Company fails to qualify as a REIT in any taxable year, the Company will be subject to federal income tax (including any applicable alternative minimum tax) based on its taxable income using corporate income tax rates. Even if the Company qualifies for taxation as a REIT, the Company may be subject to certain state and local taxes on its income and property and to federal income and excise taxes on its undistributed taxable income. The Company believes it met all organizational and operating requirements to maintain its REIT status during 2007 and intends to continue to meet such requirements for 2008. Accordingly, no provision for income taxes has been made in the accompanying consolidated financial statements.

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In July 2006, the Financial Accounting Standards Board (“FASB”) issued FASB Interpretation No. 48, “Accounting for Uncertainty in Income Taxes” (“FIN 48”). FIN 48 is an interpretation of FASB Statement No. 109, “Accounting for Income Taxes,” and it seeks to reduce the diversity in practice associated with certain aspects of measurement and recognition in accounting for income taxes. In addition, FIN 48 provides guidance on derecognition, classification, interest and penalties, and accounting in interim periods and requires expanded disclosure with respect to the uncertainty in income taxes. The Company adopted FIN 48 as of January 1, 2007 and did not record any adjustment as a result of such adoption.

Accounting for preferred equity issuance costs

In accordance with Emerging Issues Task Force (“EITF”) Topic D-42, the Company records its issuance costs as a reduction to paid-in capital on its balance sheet at the time the preferred securities are issued and reflects the carrying value of the preferred stock at the stated value. The Company records issuance costs as non-cash preferred equity distributions at the time it notifies the holders of preferred stock or units of its intent to redeem such shares or units.

Net income per common share

Per share amounts are computed using the number of weighted average common shares outstanding. “Diluted” weighted average common shares outstanding includes the dilutive effect of stock options and restricted stock units under the treasury stock method. “Basic” weighted average common shares outstanding excludes such effect. Earnings per share has been calculated as follows (in thousands, except per share amounts):

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
Net income allocable to common shareholders	\$ 4,623	\$ 3,781	\$ 8,425	\$ 9,704
Weighted average common shares outstanding:				
Basic weighted average common shares outstanding	20,430	21,334	20,432	21,325
Net effect of dilutive stock compensation — based on treasury stock method using average market price	256	347	233	367
Diluted weighted average common shares outstanding	20,686	21,681	20,665	21,692
Net income per common share — Basic	\$ 0.23	\$ 0.18	\$ 0.41	\$ 0.46
Net income per common share — Diluted	\$ 0.22	\$ 0.17	\$ 0.41	\$ 0.45

Options to purchase approximately 66,000 shares for the three and six months ended June 30, 2008 were not included in the computation of diluted net income per share because such options were considered anti-dilutive. Options to purchase approximately 32,000 shares for the three months ended June 30, 2007 were not included in the computation of diluted net income per share because such options were considered anti-dilutive. No options to purchase shares were considered anti-dilutive for the six months ended June 30, 2007.

Segment reporting

The Company views its operations as one segment.

Reclassifications

Certain reclassifications have been made to the consolidated financial statements for 2007 in order to conform to the 2008 presentation.

3. Real estate facilities

The activity in real estate facilities for the six months ended June 30, 2008 is as follows (in thousands):

	<u>Land</u>	<u>Buildings and Equipment</u>	<u>Accumulated Depreciation</u>	<u>Total</u>
Balances at December 31, 2007	\$ 494,849	\$ 1,484,049	\$ (539,857)	\$ 1,439,041
Capital improvements, net	—	19,936	—	19,936
Disposals	—	(767)	767	—
Depreciation expense	—	—	(50,567)	(50,567)
Balances at June 30, 2008	<u>\$ 494,849</u>	<u>\$ 1,503,218</u>	<u>\$ (589,657)</u>	<u>\$ 1,408,410</u>

In accordance with SFAS No. 141, “Business Combinations,” the purchase price of acquired properties is allocated to land, buildings and equipment and identified tangible and intangible assets and liabilities associated with in-place leases (including tenant improvements, unamortized lease commissions, value of above-market and below-market leases, acquired in-place lease values, and tenant relationships, if any) based on their respective estimated fair values.

In determining the fair value of the tangible assets of the acquired properties, management considers the value of the properties as if vacant as of the acquisition date. Management must make significant assumptions in determining the value of assets and liabilities acquired. Using different assumptions in the allocation of the purchase cost of the acquired properties would affect the timing of recognition of the related revenue and expenses. Amounts allocated to land are derived from comparable sales of land within the same region. Amounts allocated to buildings and improvements, tenant improvements and unamortized lease commissions are based on current market replacement costs and other market information. The amount allocated to acquired in-place leases is determined based on management’s assessment of current market conditions and the estimated lease-up periods for the respective spaces.

The following table summarizes assets acquired and liabilities assumed during the six months ended June 30, 2007 (in thousands):

Land	\$ 44,979
Buildings	71,264
In-place leases	<u>(1,075)</u>
Total purchase price	115,168
Net operating assets and liabilities acquired	<u>(1,356)</u>
Total cash paid	<u>\$ 113,812</u>

The Company did not acquire any assets or assume any liabilities during the six months ended June 30, 2008.

4. Leasing activity

The Company leases space in its real estate facilities to tenants primarily under non-cancelable leases generally ranging from one to 10 years. Future minimum rental revenues excluding recovery of operating expenses as of June 30, 2008 under these leases are as follows (in thousands):

2008	\$	109,574
2009		187,529
2010		141,291
2011		98,430
2012		66,358
Thereafter		96,839
Total	\$	700,021

In addition to minimum rental payments, certain tenants reimburse the Company for their pro-rata share of specified operating expenses. Such reimbursements amounted to \$13.5 million and \$11.3 million for the three months ended June 30, 2008 and 2007, respectively and \$26.5 million and \$21.8 million for the six months ended June 30, 2008 and 2007, respectively. These amounts are included as rental income in the accompanying consolidated statements of income.

Leases accounting for approximately 6.7% of the leased square footage are subject to termination options which include leases for approximately 2.4% of the total leased square footage having termination options exercisable through December 31, 2008. In general, these leases provide for termination payments should the termination options be exercised. The above table is prepared assuming such options are not exercised.

5. Bank loans

Subsequent to June 30, 2008, the Company extended the term of its line of credit (the "Credit Facility") with Wells Fargo Bank to August 1, 2010. The Credit Facility has a borrowing limit of \$100.0 million. Interest on outstanding borrowings is payable monthly. At the option of the Company, the rate of interest charged is equal to (i) the prime rate or (ii) a rate ranging from the London Interbank Offered Rate ("LIBOR") plus 0.70% to LIBOR plus 1.50% depending on the Company's credit ratings and coverage ratios, as defined (currently LIBOR plus 0.85%). In addition, the Company is required to pay an annual commitment fee ranging from 0.15% to 0.30% of the borrowing limit (currently 0.20%). In connection with the modification of the Credit Facility, the Company paid a fee of \$300,000, which will be amortized over the life of the Credit Facility. The Company had no balance outstanding as of June 30, 2008 or December 31, 2007. The Credit Facility requires the Company to meet certain covenants, and the Company was in compliance with all such covenants at June 30, 2008.

6. Mortgage notes payable

Mortgage notes consist of the following (in thousands):

	June 30, 2008	December 31, 2007
7.29% mortgage note, secured by one commercial property with a net book value of \$6.3 million, principal and interest payable monthly, due February, 2009	\$ 5,235	\$ 5,323
5.73% mortgage note, secured by one commercial property with a net book value of \$30.0 million, principal and interest payable monthly, due March, 2013	14,390	14,510
6.15% mortgage note, secured by one commercial property with a net book value of \$30.5 million, principal and interest payable monthly, due November, 2031 (1)	17,133	17,348
5.52% mortgage note, secured by one commercial property with a net book value of \$16.4 million, principal and interest payable monthly, due May, 2013	10,165	10,274
5.68% mortgage note, secured by one commercial property with a net book value of \$18.4 million, principal and interest payable monthly, due May, 2013	10,175	10,281
5.61% mortgage note, secured by one commercial property with a net book value of \$6.0 million, principal and interest payable monthly, due January, 2011 (2)	2,939	2,989
Total	\$ 60,037	\$ 60,725

- (1) The mortgage note has a stated principal balance of \$16.4 million and a stated interest rate of 7.20%. Based on the fair market value at the time of assumption, a mortgage premium was computed based on an effective interest rate of 6.15%. The unamortized premiums were \$736,000 and \$834,000 as of June 30, 2008 and December 31, 2007, respectively. This mortgage is repayable without penalty beginning November, 2011.
- (2) The mortgage note has a stated principal balance of \$2.8 million and a stated interest rate of 7.61%. Based on the fair market value at the time of assumption, a mortgage premium was computed based on an effective interest rate of 5.61%. The unamortized premiums were \$167,000 and \$198,000 as of June 30, 2008 and December 31, 2007, respectively.

At June 30, 2008, mortgage notes payable have a weighted average interest rate of 5.9% and a weighted average maturity of 4.0 years with principal payments as follows (in thousands):

2008	\$ 707
2009	6,442
2010	1,376
2011	19,428
2012	856
Thereafter	31,228
Total	\$ 60,037

7. Minority interests

Common partnership units

The Company presents the accounts of PSB and the Operating Partnership on a consolidated basis. Ownership interests in the Operating Partnership that can be redeemed for common stock, other than PSB's interest, are classified as minority interest — common units in the consolidated financial statements. Minority interest in income consists of the minority interests' share of the consolidated operating results after allocation to preferred units and shares. Beginning one year from the date of admission as a limited partner (common units) and subject to certain limitations described below, each limited partner other than PSB has the right to require the redemption of its partnership interest.

A limited partner (common units) that exercises its redemption right will receive cash from the Operating Partnership in an amount equal to the market value (as defined in the Operating Partnership Agreement) of the partnership interests redeemed. In lieu of the Operating Partnership redeeming the partner for cash, PSB, as general partner, has the right to elect to acquire the partnership interest directly from a limited partner exercising its redemption right, in exchange for cash in the amount specified above or by issuance of one share of PSB common stock for each unit of limited partnership interest redeemed.

A limited partner (common units) cannot exercise its redemption right if delivery of shares of PSB common stock would be prohibited under the applicable articles of incorporation, if the general partner believes that there is a risk that delivery of shares of common stock would cause the general partner to no longer qualify as a REIT, would cause a violation of the applicable securities laws, or would result in the Operating Partnership no longer being treated as a partnership for federal income tax purposes.

At June 30, 2008, there were 7,305,355 common units owned by PS, which are accounted for as minority interests. On a fully converted basis, assuming all 7,305,355 minority interest common units were converted into shares of common stock of PSB at June 30, 2008, the minority interest units would convert into approximately 26.3% of the common shares outstanding. Combined with PS's common stock ownership, on a fully converted basis, PS has a combined ownership of approximately 45.9% of the Company's common equity. At the end of each reporting period, the Company determines the amount of equity (book value of net assets) which is allocable to the minority interest based upon the ownership interest, and an adjustment is made to the minority interest, with a corresponding adjustment to paid-in capital, to reflect the minority interests' equity in the Company.

Preferred partnership units

Through the Operating Partnership, the Company has the following preferred units outstanding as of June 30, 2008 and December 31, 2007 (in thousands):

Series	Issuance Date	Earliest Potential Redemption Date	Dividend Rate	June 30, 2008		December 31, 2007	
				Units Outstanding	Amount	Units Outstanding	Amount
Series G	October, 2002	October, 2007	7.950%	800	\$ 20,000	800	\$ 20,000
Series J	May & June, 2004	May, 2009	7.500%	1,710	42,750	1,710	42,750
Series N	December, 2005	December, 2010	7.125%	800	20,000	800	20,000
Series Q	March, 2007	March, 2012	6.550%	480	12,000	480	12,000
Total				3,790	\$ 94,750	3,790	\$ 94,750

During the first quarter of 2007, the Company completed a private placement of \$12.0 million of preferred units through its Operating Partnership. The 6.550% Series Q Cumulative Redeemable Preferred Units are non-callable for five years and have no mandatory redemption.

The Operating Partnership has the right to redeem preferred units on or after the fifth anniversary of the applicable issuance date at the original capital contribution plus the cumulative priority return, as defined, to the redemption date to the extent not previously distributed. The preferred units are exchangeable for Cumulative Redeemable Preferred Stock of the respective series of PSB on or after the tenth anniversary of the date of issuance at the option of the Operating Partnership or a majority of the holders of the respective preferred units. The Cumulative Redeemable Preferred Stock will have the same distribution rate and par value as the corresponding preferred units and will otherwise have equivalent terms to the other series of preferred stock described in Note 9. As of June 30, 2008, the Company had \$2.7 million of deferred costs in connection with the issuance of preferred units, which the Company will report as additional distributions upon notice of redemption.

8. Related party transactions

Pursuant to a cost sharing and administrative services agreement, the Company shares costs with PS and affiliated entities for certain administrative services, which are allocated among PS and its affiliates in accordance with a methodology intended to fairly allocate those costs. These costs totaled \$97,000 and \$76,000 for the three months ended June 30, 2008 and 2007, respectively and \$195,000 and \$152,000 for the six months ended June 30, 2008 and 2007, respectively.

The Operating Partnership manages industrial, office and retail facilities for PS and its affiliated entities. These facilities, all located in the United States, operate under the “Public Storage” or “PS Business Parks” names.

Under the property management contracts, the Operating Partnership is compensated based on a percentage of the gross revenues of the facilities managed. Under the supervision of the property owners, the Operating Partnership coordinates rental policies, rent collections, marketing activities, the purchase of equipment and supplies, maintenance activities, and the selection and engagement of vendors, suppliers and independent contractors. In addition, the Operating Partnership assists and advises the property owners in establishing policies for the hire, discharge and supervision of employees for the operation of these facilities, including property managers and leasing, billing and maintenance personnel.

The property management contract with PS is for a seven-year term with the agreement automatically extending for an additional one-year period upon each one-year anniversary of its commencement (unless cancelled by either party). Either party can give notice of its intent to cancel the agreement upon expiration of its current term. Management fee revenues under these contracts were \$177,000 and \$182,000 for the three months ended June 30, 2008 and 2007, respectively and \$372,000 and \$365,000 for the six months ended June 30, 2008 and 2007, respectively.

In December, 2006, PS began providing property management services for the mini storage component of two assets owned by the Company. These mini storage facilities, located in Palm Beach County, Florida, operate under the “Public Storage” name.

Under the property management contracts, PS is compensated based on a percentage of the gross revenues of the facilities managed. Under the supervision of the Company, PS coordinates rental policies, rent collections, marketing activities, the purchase of equipment and supplies, maintenance activities, and the selection and engagement of vendors, suppliers and independent contractors. In addition, PS assists and advises the Company in establishing policies for the hire, discharge and supervision of employees for the operation of these facilities, including on-site managers, assistant managers and associate managers.

Both the Company and PS can cancel the property management contract upon 60 days notice. Management fee expense under the contract was approximately \$13,000 and \$12,000 for the three months ended June 30, 2008 and 2007, respectively and \$24,000 for the six months ended June 30, 2008 and 2007.

The Company had amounts due from PS of \$199,000 and \$717,000 at June 30, 2008 and December 31, 2007, respectively, for these contracts, as well as for certain operating expenses paid by the Company on behalf of PS.

9. Shareholders' equity

Preferred stock

As of June 30, 2008 and December 31, 2007, the Company had the following preferred stock outstanding (in thousands, except share data):

Series	Issuance Date	Earliest Potential Redemption Date	Dividend Rate	June 30, 2008		December 31, 2007	
				Shares Outstanding	Amount	Shares Outstanding	Amount
Series H	January & October, 2004	January, 2009	7.000%	8,200	\$ 205,000	8,200	\$ 205,000
Series I	April, 2004	April, 2009	6.875%	3,000	75,000	3,000	75,000
Series K	June, 2004	June, 2009	7.950%	2,300	57,500	2,300	57,500
Series L	August, 2004	August, 2009	7.600%	2,300	57,500	2,300	57,500
Series M	May, 2005	May, 2010	7.200%	3,300	82,500	3,300	82,500
Series O	June & August, 2006	June, 2011	7.375%	3,800	95,000	3,800	95,000
Series P	January, 2007	January, 2012	6.700%	5,750	143,750	5,750	143,750
Total				<u>28,650</u>	<u>\$ 716,250</u>	<u>28,650</u>	<u>\$ 716,250</u>

On January 17, 2007, the Company issued 5.8 million depository shares, each representing 1/1,000 of a share of the 6.700% Cumulative Preferred Stock, Series P, at \$25.00 per depository share for gross proceeds of \$143.8 million.

The Company recorded \$12.8 million in distributions to its preferred shareholders for the three months ended June 30, 2008 and 2007. The Company recorded \$25.5 million and \$25.4 million in distributions to its preferred shareholders for the six months ended June 30, 2008 and 2007, respectively.

Holders of the Company's preferred stock will not be entitled to vote on most matters, except under certain conditions. In the event of a cumulative arrearage equal to six quarterly dividends, the holders of the preferred stock will have the right to elect two additional members to serve on the Company's Board of Directors until all events of default have been cured.

Except under certain conditions relating to the Company's qualification as a REIT, the preferred stock is not redeemable prior to the previously noted redemption dates. On or after the respective redemption dates, the respective series of preferred stock will be redeemable, at the option of the Company, in whole or in part, at \$25.00 per depository share, plus any accrued and unpaid dividends. As of June 30, 2008, the Company had \$23.7 million of deferred costs in connection with the issuance of preferred stock, which the Company will report as additional non-cash distributions upon notice of its intent to redeem such shares.

Common stock

The Company's Board of Directors previously authorized the repurchase, from time to time, of up to 6.5 million shares of the Company's common stock on the open market or in privately negotiated transactions. During the six months ended June 30, 2008, the Company repurchased 370,042 shares of common stock at an aggregate cost of \$18.3 million or an average cost per share of \$49.52. Since inception of the program, the Company has repurchased an aggregate of 4.3 million shares of common stock at an aggregate cost of \$152.8 million or an average cost per share of \$35.84. Under existing board authorizations, the Company can repurchase an additional 2.2 million shares. No shares were repurchased during the six months ended June 30, 2007.

The Company paid \$9.0 million (\$0.44 per common share) and \$9.4 million (\$0.44 per common share) in distributions to its common shareholders for the three months ended June 30, 2008 and 2007, respectively and \$18.0 million (\$0.88 per common share) and \$15.6 million (\$0.73 per common share) for the six months ended June 30, 2008 and 2007, respectively.

Equity Stock

In addition to common and preferred stock, the Company is authorized to issue 100.0 million shares of Equity Stock. The Articles of Incorporation provide that the Equity Stock may be issued from time to time in one or more series and give the Board of Directors broad authority to fix the dividend and distribution rights, conversion and voting rights, redemption provisions and liquidation rights of each series of Equity Stock.

10. Commitments and contingencies

The Company currently is neither subject to any material litigation nor, to management’s knowledge, is any material litigation currently threatened against the Company other than routine litigation and administrative proceedings arising in the ordinary course of business.

11. Stock-based compensation

PSB has a 1997 Stock Option and Incentive Plan (the “1997 Plan”) and a 2003 Stock Option and Incentive Plan (the “2003 Plan”), each covering 1.5 million shares of PSB’s common stock. Under the 1997 Plan and 2003 Plan, PSB has granted non-qualified options to certain directors, officers and key employees to purchase shares of PSB’s common stock at a price no less than the fair market value of the common stock at the date of grant. Additionally, under the 1997 Plan and 2003 Plan, PSB has granted restricted stock units to officers and key employees.

The weighted average grant date fair value of the options granted during the six months ended June 30, 2008 and 2007 were \$8.50 per share and \$12.11 per share, respectively. The Company has calculated the fair value of each option grant on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions used for grants during the six months ended June 30, 2008 and 2007, respectively; a dividend yield of 3.1% and 2.6%; expected volatility of 19.1% and 18.2%; expected life of five years; and risk-free interest rates of 3.1% and 4.5%.

The weighted average grant date fair value of restricted stock units granted during the six months ended June 30, 2008 and 2007 were \$52.35 and \$71.23, respectively. The Company calculated the fair value of each restricted stock unit grant using the market value on the date of grant.

At June 30, 2008, there were a combined total of 1.2 million options and restricted stock units authorized to grant. Information with respect to outstanding options and nonvested restricted stock units granted under the 1997 Plan and 2003 Plan is as follows:

Options:	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contract Life	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2007	572,587	\$ 37.86		
Granted	14,000	\$ 57.79		
Exercised	(17,500)	\$ 25.54		
Forfeited	—	—		
Outstanding at June 30, 2008	569,087	\$ 38.73	5.12 Years	\$ 8,132
Exercisable at June 30, 2008	427,887	\$ 34.52	4.33 Years	\$ 7,452

Restricted Stock Units:	Number of Units	Weighted Average Grant Date Fair Value
Nonvested at December 31, 2007	228,227	\$ 53.91
Granted	38,650	\$ 52.35
Vested	(22,469)	\$ 48.35
Forfeited	(2,000)	\$ 53.65
Nonvested at June 30, 2008	<u>242,408</u>	<u>\$ 54.18</u>

Included in the Company’s consolidated statements of income for the three months ended June 30, 2008 and 2007, was \$111,000 and \$262,000, respectively, in net stock option compensation expense related to stock options. Net stock option compensation expense for the six months ended June 30, 2008 and 2007 was \$217,000 and \$332,000, respectively. Net compensation expense of \$882,000 and \$777,000 related to restricted stock units was recognized during the three months ended June 30, 2008 and 2007, respectively. Net compensation expense of \$1.8 million and \$1.3 million related to restricted stock units was recognized during the six months ended June 30, 2008 and 2007, respectively.

As of June 30, 2008, there was \$992,000 of unamortized compensation expense related to stock options expected to be recognized over a weighted average period of 3.0 years. As of June 30, 2008, there was \$7.7 million of unamortized compensation expense related to restricted stock units expected to be recognized over a weighted average period of 3.3 years.

Cash received from 17,500 stock options exercised during the six months ended June 30, 2008 was \$447,000. Cash received from 9,600 stock options exercised during the six months ended June 30, 2007 was \$365,000. The aggregate intrinsic value of the stock options exercised during the six months ended June 30, 2008 and 2007 was \$509,000 and \$326,000, respectively.

During the six months ended June 30, 2008, 22,469 restricted stock units vested; in settlement of these units, 14,441 shares were issued, net of shares applied to payroll taxes. The aggregate fair value of the shares vested for the six months ended June 30, 2008 was \$1.2 million. During the six months ended June 30, 2007, 18,373 restricted stock units vested; in settlement of these units, 11,749 shares were issued, net of shares applied to payroll taxes. The aggregate fair value of the shares vested for the six months ended June 30, 2007 was \$1.3 million.

In May of 2004, the shareholders of the Company approved the issuance of up to 70,000 shares of common stock under the Retirement Plan for Non-Employee Directors (the “Director Plan”). Under the Director Plan, the Company grants 1,000 shares of common stock for each year served as a director up to a maximum of 5,000 shares issued upon retirement. The Company recognizes compensation expense with regards to grants to be issued in the future under the Director Plan. As a result, included in the Company’s consolidated statements of income was \$25,000 in compensation expense for the three months ended June 30, 2008 and 2007 and \$51,000 for the six months ended June 30, 2008 and 2007. As of June 30, 2008 and 2007, there was \$261,000 and \$363,000, respectively, of unamortized compensation expense related to these shares. In April of 2007, the Company issued 5,000 shares to a director upon retirement with an aggregate fair value of \$345,000.

12. Recent accounting pronouncements

In December 2007, the FASB issued SFAS No. 141 (R), “Business Combinations” (“SFAS 141R”), to create greater consistency in the accounting and financial reporting of business combinations. SFAS 141R requires a company to recognize the assets acquired, the liabilities assumed, and any noncontrolling interest in the acquired entity to be measured at their fair values as of the acquisition date. SFAS 141R also requires companies to recognize the fair value of assets acquired, the liabilities assumed and any noncontrolling interest in acquisitions of less than a 100% interest when the acquisition constitutes a change in control of the acquired entity. In addition, SFAS 141R requires that acquisition-related costs and restructuring costs be recognized separately from the business combination and expensed as incurred. SFAS 141R is effective for business combinations for which the acquisition date is on or after January 1, 2009. Early adoption is prohibited. The Company is currently evaluating the impact of SFAS 141R on our consolidated financial statements.

Effective January 1, 2008, the Company adopted, on a prospective basis, SFAS No. 157, "Fair Value Measurements" ("SFAS 157") as amended by 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"). SFAS 157 defines fair value, establishes a framework for measuring fair value in GAAP and provides for expanded disclosure about fair value measurements. SFAS 157 applies prospectively to all other accounting pronouncements that require or permit fair value measurements. FSP FAS 157-1 amends SFAS 157 to exclude from the scope of SFAS 157 certain leasing transactions accounted for under SFAS 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.

The adoption of SFAS 157 did not have a material impact on the Company's consolidated financial statements. Management is evaluating the impact that SFAS 157 will have on its non-financial assets and non-financial liabilities since the application of SFAS 157 for such items was deferred to January 1, 2009. The Company believes that the impact of these items will not be material to its consolidated financial statements.

Effective January 1, 2008, the Company adopted, on a prospective basis, SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" ("SFAS 159"). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The objective of the guidance is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. The adoption of SFAS 159 did not have a material impact on the Company's consolidated financial statements since the Company did not elect to apply the fair value option for any of its eligible financial instruments or other items on the January 1, 2008 effective date.

In December 2007, the FASB issued SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements — an amendment of ARB No. 51" ("SFAS 160"). SFAS 160 amends Accounting Research Bulletin No. 51, "Consolidated Financial Statements", and requires all entities to report noncontrolling interests in subsidiaries within equity in the consolidated financial statements, but separate from the parent shareholders' equity. SFAS 160 also requires any acquisitions or dispositions of noncontrolling interests that do not result in a change of control to be accounted for as equity transactions. In addition, SFAS 160 requires that a parent company recognize a gain or loss in net income when a subsidiary is deconsolidated upon a change in control. SFAS 160 applies to our fiscal year beginning on January 1, 2009 and will be adopted prospectively. The presentation and disclosure requirements shall be applied retrospectively for all periods presented. Early adoption is prohibited. The adoption of SFAS 160 will result in a reclassification of minority interest to a separate component of total equity and net income allocable to noncontrolling interest will no longer be treated as a reduction to net income but will be shown as a reduction from net income in calculating net income available to common shareholders. The adoption of SFAS 160 is not expected to have an impact on net income allocable to common shareholders or net income per common share.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements: Forward-looking statements are made throughout this Quarterly Report on Form 10-Q. For this purpose, any statements contained herein that are not statements of historical fact may be deemed to be forward-looking statements. Without limiting the foregoing, the words "may," "believes," "anticipates," "plans," "expects," "seeks," "estimates," "intends," and similar expressions are intended to identify forward-looking statements. There are a number of important factors that could cause the results of the Company to differ materially from those indicated by such forward-looking statements, including those detailed under the heading "Item 1A. Risk Factors" in Part II of this quarterly report on Form 10-Q. In light of the significant uncertainties inherent in the forward-looking statements included herein, the inclusion of such information should not be regarded as a representation by us or any other person that our objectives and plans will be achieved. Moreover, we assume no obligation to update these forward-looking statements to reflect actual results, changes in assumptions or changes in other factors affecting such forward-looking statements.

Overview

The Company owns and operates approximately 19.6 million rentable square feet of flex, industrial and office properties located in eight states.

The Company focuses on increasing profitability and cash flow aimed at maximizing shareholder value. The Company strives to maintain high occupancy levels while increasing rental rates when market conditions allow. The Company also acquires properties which it believes will create long-term value, and disposes of properties which no longer fit within the Company's strategic objectives or in situations where the Company believes it can optimize cash proceeds. Operating results are driven by income from rental operations and are therefore substantially influenced by rental demand for space within our properties.

During the first six months of 2008, the Company successfully leased or re-leased 2.8 million square feet of space while experiencing a slight increase in rental rates and relatively flat transaction costs. Total net operating income for the six months ended June 30, 2008 increased \$5.2 million or 5.7% compared to the six months ended June 30, 2007. See further discussion of operating results below.

Critical Accounting Policies and Estimates:

Our accounting policies are described in Note 2 to the consolidated financial statements included in this Form 10-Q. We believe our most critical accounting policies relate to revenue recognition, allowance for doubtful accounts, impairment of long-lived assets, depreciation, accruals of operating expenses and accruals for contingencies, each of which we discuss below.

Revenue Recognition: We recognize revenue in accordance with Staff Accounting Bulletin No. 104 of the Securities and Exchange Commission, Revenue Recognition in Financial Statements ("SAB 104"), as amended. SAB 104 requires that the following four basic criteria must be met before revenue can be recognized: persuasive evidence of an arrangement exists; the delivery has occurred or services rendered; the fee is fixed or determinable; and collectibility is reasonably assured. All leases are classified as operating leases. Rental income is recognized on a straight-line basis over the terms of the leases. Straight-line rent is recognized for all tenants with contractual increases in rent that are not included on the Company's credit watch list. Deferred rent receivables represent rental revenue recognized on a straight-line basis in excess of billed rents. Reimbursements from tenants for real estate taxes and other recoverable operating expenses are recognized as rental income in the period the applicable costs are incurred.

Property Acquisitions: In accordance with Statement of Financial Accounting Standards ("SFAS") No. 141, "Business Combinations," we allocate the purchase price of acquired properties to land, buildings and equipment and identified tangible and intangible assets and liabilities associated with in-place leases (including tenant improvements, unamortized lease commissions, value of above-market and below-market leases, acquired in-place lease values, and tenant relationships, if any) based on their respective estimated fair values.

In determining the fair value of the tangible assets of the acquired properties, management considers the value of the properties as if vacant as of the acquisition date. Management must make significant assumptions in determining the value of assets acquired and liabilities assumed. Using different assumptions in the allocation of the purchase cost of the acquired properties would affect the timing of recognition of the related revenue and expenses. Amounts allocated to land are derived from comparable sales of land within the same region. Amounts allocated to buildings and improvements, tenant improvements and unamortized lease commissions are based on current market replacement costs and other market rate information.

The value allocable to the above-market or below-market in-place lease values of acquired properties is determined based upon the present value (using a discount rate which reflects the risks associated with the acquired leases) of the difference between (i) the contractual rents to be paid pursuant to the in-place leases, and (ii) management's estimate of fair market lease rates for the corresponding in-place leases, measured over a period equal to the remaining non-cancelable term of the lease. The amounts allocated to above-market or below-market leases are included in other assets or other liabilities in the accompanying consolidated balance sheets and are amortized on a straight-line basis as an increase or reduction of rental income over the remaining non-cancelable term of the respective leases.

Allowance for Doubtful Accounts: Rental revenue from our tenants is our principal source of revenue. We monitor the collectibility of our receivable balances including the deferred rent receivable on an ongoing basis. Based on these reviews, we maintain an allowance for doubtful accounts for estimated losses resulting from the possible inability of our tenants to make required rent payments to us. Tenant receivables and deferred rent receivables are carried net of the allowances for uncollectible tenant receivables and deferred rent. As discussed below, determination of the adequacy of these allowances requires significant judgments and estimates. Our estimate of the required allowance is subject to revision as the factors discussed below change and is sensitive to the effect of economic and market conditions on our tenants.

Tenant receivables consist primarily of amounts due for contractual lease payments, reimbursements of common area maintenance expenses, property taxes and other expenses recoverable from tenants. Determination of the adequacy of the allowance for uncollectible current tenant receivables is performed using a methodology that incorporates specific identification, aging analysis, an overall evaluation of the historical loss trends and the current economic and business environment. The specific identification methodology relies on factors such as the age and nature of the receivables, the payment history and financial condition of the tenant, the assessment of the tenant's ability to meet its lease obligations, and the status of negotiations of any disputes with the tenant. The allowance also includes a reserve based on historical loss trends not associated with any specific tenant. This reserve as well as the specific identification reserve is reevaluated quarterly based on economic conditions and the current business environment.

Deferred rent receivable represents the amount that the cumulative straight-line rental income recorded to date exceeds cash rents billed to date under the lease agreement. Given the long-term nature of these types of receivables, determination of the adequacy of the allowance for unbilled deferred rent receivable is based primarily on historical loss experience. Management evaluates the allowance for unbilled deferred rent receivable using a specific identification methodology for significant tenants designed to assess their financial condition and ability to meet their lease obligations.

Impairment of Long-Lived Assets: The Company evaluates a property for potential impairment whenever events or changes in circumstances indicate that its carrying amount may not be recoverable. On a quarterly basis, we evaluate our whole portfolio for impairment based on current operating information. In the event that these periodic assessments reflect that the carrying amount of a property exceeds the sum of the undiscounted cash flows (excluding interest) that are expected to result from the use and eventual disposition of the property, the Company would recognize an impairment loss to the extent the carrying amount exceeded the estimated fair value of the property. The estimation of expected future net cash flows is inherently uncertain and relies on subjective assumptions dependent upon future and current market conditions and events that affect the ultimate value of the property. Management must make assumptions related to the property such as future rental rates, tenant allowances, operating expenditures, property taxes, capital improvements, occupancy levels and the estimated proceeds generated from the future sale of the property. These assumptions could differ materially from actual results in future periods. Since SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," provides that the future cash flows used in this analysis be considered on an undiscounted basis, our intent to hold properties over the long-term directly decreases the likelihood of recording an impairment loss. If our strategy changes or if market conditions otherwise dictate an earlier sale date, an impairment loss could be recognized and such loss could be material.

Depreciation: We compute depreciation on our buildings and equipment using the straight-line method based on estimated useful lives of generally 30 and five years, respectively. A significant portion of the acquisition cost of each property is allocated to building and building components. The allocation of the acquisition cost to building and building components, as well as the determination of their useful lives are based on estimates. If we do not appropriately allocate to these components or we incorrectly estimate the useful lives of these components, our computation of depreciation expense may not appropriately reflect the actual impact of these costs over future periods, which will affect net income. In addition, the net book value of real estate assets could be overstated or understated. The statement of cash flows, however, would not be affected.

Accruals of Operating Expenses: The Company accrues for property tax expenses, performance bonuses and other operating expenses each quarter based on historical trends and anticipated disbursements. If these estimates are incorrect, the timing and amount of expense recognized will be affected.

Accruals for Contingencies: The Company is exposed to business and legal liability risks with respect to events that may have occurred, but in accordance with U.S. generally accepted accounting principles ("GAAP") has not accrued for such potential liabilities because the loss is either not probable or not estimable. Future events and the result of pending litigation could result in such potential losses becoming probable and estimable, which could have a material adverse impact on our financial condition or results of operations.

Effect of Economic Conditions on the Company's Operations:

The conditions in the sub-prime lending industry and housing market in late 2007 and early 2008 have caused a weakening in the credit market and overall U.S. economy. During the first six months of 2008, these weakening economic conditions were reflected in commercial real estate as the Company experienced a slight increase in rental rates and relatively flat transaction costs. It is uncertain what impact a recession or similar economic conditions may have on the Company's ability to maintain high occupancy levels and increase rents. While the Company has not experienced a significant impact from the slowed economy, conditions may change and the Company may be impacted by lower occupancy and a reduced ability to raise rents.

While the Company historically has experienced a low level of write-offs due to bankruptcy, there is inherent uncertainty in a tenant's ability to continue paying rent when in bankruptcy. As of June 30, 2008, the Company had approximately 13,000 square feet occupied by tenants that are protected by Chapter 11 of the U.S. Bankruptcy Code. Given the historical uncertainty of these tenants' ability to meet their lease obligations, we will continue to reserve any income that would have been realized on a straight-line basis. Several other tenants have contacted us, requesting early termination of their lease, reduction in space under lease, rent deferment or abatement. At this time, the Company cannot anticipate what impact, if any, the ultimate outcome of these discussions will have on our operating results.

Company Performance and Effect of Economic Conditions on Primary Markets:

The Company's operations are substantially concentrated in 10 regions. Current market conditions for each region are summarized below. During the six months ended June 30, 2008, rental rates on new and renewed leases within the Company's overall portfolio increased 1.4%. Excluding a 43,000 square foot lease executed during the first quarter of 2008 on a space previously occupied by a government tenant, the increase would have been 3.2%. These changes are based on comparisons to the most recent in-place rents prior to renewal or replacement. The Company has compiled the market occupancy information set forth below using third party reports for each respective market. The Company considers these sources to be reliable, but there can be no assurance that the information in these reports is accurate.

The Company owns approximately 4.0 million square feet in Southern California. Market vacancies have increased in large part due to the number of sub-prime lenders, mortgage brokers and other related businesses that have vacated space, creating significantly more competition for tenants. The effect of these vacancies however is less on flex space, which comprises 63.7% of the Company's Southern California portfolio. Vacancy rates in Southern California range from 2.0% to 13.3%. The Company's vacancy rate in this region at June 30, 2008 was 6.8%. For the six months ended June 30, 2008, the overall market experienced negative net absorption of 0.2% attributed to the mortgage and housing-related companies as well as newly constructed space completed during 2008. The Company's weighted average occupancy for the region decreased from 93.9% for the first six months in 2007 to 93.6% for the first six months in 2008. Annualized realized rent per square foot increased 3.1% from \$16.96 per square foot for the first six months in 2007 to \$17.49 per square foot for the first six months in 2008. Although these markets continue to experience increasing rental rates, the Company has seen signs of easing rental rate growth and modestly increasing concessions due to higher vacancies in the office market. Additionally, construction of Class A buildings, primarily in Orange County, could have an impact on the Company's ability to maintain occupancy and generate measurable rental rate growth within the office portfolio.

The Company owns approximately 1.8 million square feet in Northern California with a concentration in Sacramento, the East Bay (Hayward and San Ramon) and Silicon Valley (San Jose). The vacancy rates in these submarkets are 16.0%, 18.6% and 14.5%, respectively. The Company's vacancy rate in its Northern California portfolio at June 30, 2008 was 7.4%. Demand in these submarkets has slowed for users over 20,000 square feet and softened for users less than 10,000 square feet. For the six months ended June 30, 2008, the combined submarkets experienced positive net absorption of 0.7%, however, the time necessary to execute a transaction has lengthened as tenants weigh their options and negotiate on tenant improvements. The Company's weighted average occupancy in this region increased from 90.7% for the first six months in 2007 to 92.1% for the first six months in 2008. Positively affected by the growth and stability of the technology industry, annualized realized rent per square foot increased 3.3% from \$13.84 per square foot for the first six months in 2007 to \$14.29 per square foot for the first six months in 2008.

The Company owns approximately 1.2 million square feet in Southern Texas, which includes the Austin and Houston markets. Market vacancy rates are 10.2% in the Austin market and 11.7% in the Houston market. The Company's vacancy rate for the combined markets at June 30, 2008 was 4.1%. The job growth in both the Austin and Houston markets and the strong oil and gas industry in the Houston market helped increase leasing activity in the Company's Southern Texas portfolio, which is evidenced in the occupancy and rental rate improvement within the portfolio. For the six months ended June 30, 2008, the combined markets experienced positive net absorption of 0.5%. The Company's weighted average occupancy in this region increased from 92.2% for the first six months in 2007 to 95.6% for the first six months in 2008. Annualized realized rent per square foot increased 6.7% from \$10.63 per square foot for the first six months in 2007 to \$11.34 per square foot for the first six months in 2008. Texas leads the nation in scheduled construction projects and as construction outweighs demand, it could have an impact on the Company's ability to maintain occupancy and generate measurable rental rate growth within the Company's portfolio.

The Company owns approximately 1.7 million square feet in Northern Texas, which includes the Dallas Metroplex market. The market vacancy rate in Las Colinas, where most of the Company's properties are located, is 9.2%. The Company's vacancy rate at June 30, 2008 in this market was 7.7%. For the six months ended June 30, 2008, the market experienced positive net absorption of 0.8% as the result of continued job growth in Northern Texas. During 2008, modest new construction continued, which included both speculative construction, as well as owner-user construction. Despite the new construction, the Company has experienced a modest level of leasing activity during the first six months of 2008 with stable rental rates and higher occupancy levels. The Company's weighted average occupancy for the region increased from 83.8% for the first six months in 2007 to 93.0% for the first six months in 2008. Annualized realized rent per square foot increased 2.7% from \$10.37 per square foot for the first six months in 2007 to \$10.65 per square foot for the first six months in 2008 as rental rates have increased modestly over expiring leases. However, new supply completed during the year could have an impact on the Company's ability to maintain occupancy and generate measurable rental rate growth within the Company's portfolio.

The Company owns approximately 3.6 million square feet in South Florida. The Company owns Miami International Commerce Center ("MICC") located in the Airport West submarket of Miami-Dade County. While the saturation of the condominium and housing markets in Miami has negatively impacted its overall economy, it has had little impact on international trade-based assets, such as industrial and flex space, which comprises 88.6% of the Company's South Florida portfolio. MICC is located less than one mile from the cargo entrance of the Miami International Airport, which is one of the most active ports in the United States. The Company acquired two assets in Palm Beach County at the end of 2006, comprising 398,000 square feet. The downturn in the housing market and slowing economy have adversely affected Palm Beach County. Market vacancy rates for Miami-Dade County and Palm Beach County are 8.4% and 10.2%, respectively, compared with the Company's South Florida region vacancy rate of 4.0% at June 30, 2008. For the six months ended June 30, 2008, the combined markets experienced positive net absorption of 0.2%. The Company's weighted average occupancy in this region outperformed the market despite a decrease from 98.1% for the first six months in 2007 to 96.4% for the first six months in 2008. Annualized realized rent per square foot increased 4.9% from \$8.81 per square foot for the first six months in 2007 to \$9.24 per square foot for the first six months in 2008.

The Company owns approximately 3.0 million square feet in the Northern Virginia submarket of Washington D.C., where the average market vacancy rate is 11.8%. Vacancy rates in this market increased as new supply continues to outpace the demand. The Company's vacancy rate in this market at June 30, 2008 was 2.7%. Most submarkets in the greater Washington D.C. market continue to demonstrate stable fundamentals. A major contributor to the market strength is tied to government contracting and defense spending. For the six months ended June 30, 2008, the market experienced positive net absorption of 1.0%. During 2007 and continuing into 2008, construction of Class A buildings has had a modest impact on the Company's portfolio. The amount of sublease space available in the market has increased throughout the year and could limit the Company's ability to generate measurable rental rate growth and place pressure on occupancy. Annualized realized rent per square foot increased 3.3% from \$19.36 per square foot for the first six months in 2007 to \$20.00 per square foot for the first six months in 2008. The Company's weighted average occupancy increased from 93.4% for the first six months in 2007 to 97.2% for the first six months in 2008.

The Company owns approximately 1.8 million square feet in the Maryland submarket of Washington D.C. The Company's portfolio is primarily located in Montgomery County and Silver Spring. The business of the federal government, healthcare, education and life sciences continue to be the primary drivers within the Company's portfolio. The Company's vacancy rate in the region at June 30, 2008 was 9.4% compared to 11.4% for the market as a whole. The market vacancy rate increased as new constructions are completed with limited preleasing activities. For the six months ended June 30, 2008, the market experienced negative net absorption of 0.5%, which is attributed to a decrease in demand for large blocks of space due to the slowing economy. The Company's weighted average occupancy decreased from 95.0% for the first six months in 2007 to 90.7% for the first six months in 2008, modestly outperforming the market. The decrease in occupancy was primarily related to a 67,000 square foot tenant vacating its space at the end of 2007. Annualized realized rent per square foot increased 0.1% from \$23.06 per square foot for the first six months in 2007 to \$23.08 per square foot for the first six months in 2008.

The Company owns approximately 1.3 million square feet in the Beaverton submarket of Portland, Oregon. The market vacancy rate in this region is 16.6%. The Company's vacancy rate in the market was 16.7% at June 30, 2008. The recent economic trends and slowdown have resulted in increases in both vacancy rates and rent concessions in the market. For the six months ended June 30, 2008, the market experienced negative net absorption of 1.3%. The Company's weighted average occupancy decreased from 91.4% for the first six months in 2007 to 84.4% for the first six months in 2008 primarily related to a 120,000 square foot tenant vacating its space during the second quarter of 2008 combined with the loss of three tenants during 2007 due to business failures. Despite the recent trends and slowdown, annualized realized rent per square foot increased 6.3% from \$15.67 per square foot for the first six months in 2007 to \$16.66 per square foot for the first six months in 2008. The increase was primarily the result of the six months in 2007 being negatively impacted by the business failures combined with a modest increase in rental rates.

The Company owns approximately 679,000 square feet in the Phoenix and Tempe submarkets of Arizona. Market vacancies increased significantly due to the number of housing-related tenants who have vacated space, creating significantly more competition for tenants. During 2007 and continuing into 2008, significant construction of buildings has impacted the Company's portfolio and may result in higher lease concessions while limiting the Company's ability to generate measurable rental rate growth. The market vacancy rate is 11.1% compared to the Company's vacancy rate of 13.1% at June 30, 2008. For the six months ended June 30, 2008, despite new supply outpacing demand, the market experienced positive net absorption of 0.3%. Although demand for space has subsided, annualized realized rent per square foot increased 4.9% from \$11.21 per square foot for the first six months in 2007 to \$11.76 per square foot for the first six months in 2008. The Company's weighted average occupancy in the region decreased from 90.2% for the first six months in 2007 to 87.1% for the first six months in 2008.

The Company owns approximately 521,000 square feet in the state of Washington. On February 16, 2007, the Company acquired Overlake Business Center, a 493,000 square foot multi-tenant office and flex business park located in Redmond, Washington. The commercial airline and technology industries continue to drive the market. As a result of these industries, the market experienced positive net absorption of 0.4% for the six months ended June 30, 2008. The Company's vacancy rate in this region at June 30, 2008 was 4.3% compared to 9.4% for the market as a whole. The Company's weighted average occupancy increased from 88.7% for the first six months in 2007 to 94.3% for the first six months in 2008. Annualized realized rent per square foot increased 11.5% from \$17.11 per square foot for the first six months in 2007 to \$19.08 per square foot for the first six months in 2008.

Growth of the Company's Operations and Acquisitions and Dispositions of Properties:

The Company is focused on maximizing cash flow from its existing portfolio of properties by expanding its presence in existing and new markets through strategic acquisitions and through the disposition of non-strategic assets. The Company has historically maintained a low-leverage-level approach intended to provide the Company with the flexibility for future growth.

In 2007, the Company acquired 870,000 square feet for an aggregate cost of \$140.6 million. The Company acquired Overlake Business Center, a 493,000 square foot multi-tenant office and flex business park located in Redmond, Washington, for \$76.0 million; Commerce Campus, a 252,000 square foot multi-tenant office and flex business park located in Santa Clara, California, for \$39.2 million; and Fair Oaks Corporate Center, a 125,000 square foot multi-tenant office park located in Fairfax, Virginia, for \$25.4 million.

Scheduled Lease Expirations:

In addition to the 1.3 million square feet, or 6.5%, of currently available space in our total portfolio, leases representing approximately 10.2% of the leased square footage of our total portfolio are scheduled to expire during the remainder of 2008. Leases comprising approximately 267,000 square feet of currently vacant space have been executed as of the date of this report and are expected to commence during the third and fourth quarters of 2008. Our ability to re-lease available space depends upon the market conditions in the specific submarkets in which our properties are located.

Impact of Inflation:

Although inflation has not been significant in recent years, it remains a factor in our economy, and the Company continues to seek ways to mitigate its potential impact. A substantial portion of the Company's leases require tenants to pay operating expenses, including real estate taxes, utilities, and insurance, as well as increases in common area expenses, partially reducing the Company's exposure to inflation. During 2007 and 2008, the Company experienced modest increases in certain operating costs, including repairs and maintenance, property insurance and utility costs affecting the Company's overall profit margin.

Concentration of Portfolio by Region:

Rental income, cost of operations and rental income less cost of operations, excluding depreciation and amortization, or net operating income prior to depreciation and amortization (defined as "NOI" for purposes of the following tables), are summarized for the three and six months ended June 30, 2008 by major geographic region below. The Company uses NOI and its components as a measurement of the performance of its commercial real estate. Management believes that these financial measures provide them as well as the investor the most consistent measurement on a comparative basis of the performance of the commercial real estate and its contribution to the value of the Company. Depreciation and amortization has been excluded from these financial measures as they are generally not used in determining the value of commercial real estate by management or the investment community. Depreciation and amortization is generally not used in determining value as they consider the historical costs of an asset compared to its current value; therefore, to understand the effect of the assets' historical cost on the Company's results, investors should look at GAAP financial measures, such as total operating costs including depreciation and amortization. The Company's calculation of NOI may not be comparable to those of other companies and should not be used as an alternative to measures of performance calculated in accordance with GAAP. The tables below reflect rental income, operating expenses and NOI for the three and six months ended June 30, 2008 based on geographical concentration. The total of all regions is equal to the amount of rental income and cost of operations recorded by the Company in accordance with GAAP. As part of the tables below, we have shown the effect of depreciation and amortization on NOI. We have reconciled NOI to consolidated income before minority interests in the table under "Results of Operations" below. The percent of total by region reflects the actual contribution to rental income, cost of operations and NOI during the period (in thousands):

Three Months Ended June 30, 2008:

Region	Weighted Square Footage	Percent of Total	Rental Income	Percent of Total	Cost of Operations	Percent of Total	NOI	Percent of Total
Southern California	3,988	20.4%	\$16,421	23.3%	\$ 4,134	18.8%	\$ 12,287	25.3%
Northern California	1,819	9.3%	6,043	8.6%	1,866	8.5%	4,177	8.6%
Southern Texas	1,161	5.9%	3,218	4.6%	1,481	6.8%	1,737	3.6%
Northern Texas	1,689	8.6%	4,207	6.0%	1,670	7.6%	2,537	5.2%
South Florida	3,598	18.4%	7,980	11.3%	2,622	12.0%	5,358	11.1%
Virginia	3,019	15.4%	14,749	20.9%	4,286	19.5%	10,463	21.6%
Maryland	1,770	9.1%	9,118	12.9%	2,855	13.0%	6,263	12.9%
Oregon	1,313	6.7%	4,591	6.5%	1,618	7.4%	2,973	6.1%
Arizona	679	3.5%	1,731	2.5%	761	3.5%	970	2.0%
Washington	521	2.7%	2,388	3.4%	646	2.9%	1,742	3.6%
Total before depreciation and amortization	<u>19,557</u>	<u>100.0%</u>	<u>70,446</u>	<u>100.0%</u>	<u>21,939</u>	<u>100.0%</u>	<u>48,507</u>	<u>100.0%</u>
Depreciation and amortization			<u>—</u>		<u>25,120</u>		<u>(25,120)</u>	
Total based on GAAP			<u>\$70,446</u>		<u>\$ 47,059</u>		<u>\$ 23,387</u>	

Six Months Ended June 30, 2008:

Region	Weighted Square Footage	Percent of Total	Rental Income	Percent of Total	Cost of Operations	Percent of Total	NOI	Percent of Total
Southern California	3,988	20.4%	\$ 32,661	23.2%	\$ 8,381	18.9%	\$ 24,280	25.3%
Northern California	1,819	9.3%	11,960	8.5%	3,567	8.0%	8,393	8.7%
Southern Texas	1,161	5.9%	6,292	4.5%	2,821	6.4%	3,471	3.6%
Northern Texas	1,689	8.6%	8,372	5.9%	3,108	7.0%	5,264	5.5%
South Florida	3,598	18.4%	16,006	11.4%	5,370	12.1%	10,636	11.1%
Virginia	3,019	15.4%	29,326	20.9%	8,927	20.1%	20,399	21.2%
Maryland	1,770	9.1%	18,531	13.2%	5,929	13.3%	12,602	13.1%
Oregon	1,313	6.7%	9,243	6.6%	3,434	7.7%	5,809	6.0%
Arizona	679	3.5%	3,476	2.5%	1,540	3.5%	1,936	2.0%
Washington	521	2.7%	4,690	3.3%	1,352	3.0%	3,338	3.5%
Total before depreciation and amortization	<u>19,557</u>	<u>100.0%</u>	<u>140,557</u>	<u>100.0%</u>	<u>44,429</u>	<u>100.0%</u>	<u>96,128</u>	<u>100.0%</u>
Depreciation and amortization			—		50,567		(50,567)	
Total based on GAAP			<u>\$140,557</u>		<u>\$ 94,996</u>		<u>\$ 45,561</u>	

Concentration of Credit Risk by Industry:

The information below depicts the industry concentration of our tenant base as of June 30, 2008. The Company analyzes this concentration to understand significant industry exposure risk.

Industry	% of Total Annual Rents
Business Services	13.3%
Computer Hardware, Software and Related Service	9.8%
Health Services	9.8%
Warehouse, Transportation and Logistics	8.7%
Government	8.7%
Financial Services	8.3%
Contractors	7.5%
Retail	6.3%
Communications	5.6%
Home Furnishings	3.8%
Electronics	3.2%
Educational Services	2.8%
Total	<u>87.8%</u>

The information below depicts the Company's top 10 customers by annual rents as of June 30, 2008 (in thousands):

Tenants	Square Footage	Annualized Rental Income (1)	% of Total Annualized Rental Income
U.S. Government	462	\$ 12,035	4.3%
Kaiser Permanente	186	4,447	1.6%
Wells Fargo	102	1,701	0.6%
AARP	102	1,610	0.6%
Northrop Grumman	58	1,587	0.6%
Raytheon	78	1,471	0.5%
Intel	94	1,333	0.5%
American Intercontinental University	75	1,330	0.5%
Montgomery County Public Schools	47	1,268	0.5%
American Systems	63	1,205	0.4%
Total	<u>1,267</u>	<u>\$ 27,987</u>	<u>10.1%</u>

(1) For leases expiring prior to December 31, 2008, annualized rental income represents income to be received under existing leases from June 30, 2008 through the date of expiration.

Comparative Analysis of the Three and Six Months Ended June 30, 2008 to the Three and Six Months Ended June 30, 2007

Results of Operations: In order to evaluate the performance of the Company’s overall portfolio over two comparable periods, management analyzes the operating performance of a consistent group of properties owned and operated throughout both periods (herein referred to as “Same Park”). Operating properties that the Company acquired subsequent to January 1, 2007 are referred to as “Non-Same Park.” For the six months ended June 30, 2008 and 2007, the Same Park facilities constitute 18.7 million rentable square feet, which includes all assets the Company owned and operated from January 1, 2007 through June 30, 2008, representing approximately 95.6% of the total square footage of the Company’s portfolio as of June 30, 2008.

Rental income, cost of operations and rental income less cost of operations, excluding depreciation and amortization or net operating income prior to depreciation and amortization (defined as “NOI” for purposes of the following table) are summarized for the three and six months ended June 30, 2008 and 2007. The Company’s property operations account for substantially all of the net operating income earned by the Company. See “Concentration of Portfolio by Region” above for more information on NOI, including why the Company presents NOI and how the Company uses NOI. The Company’s calculation of NOI may not be comparable to those of other companies and should not be used as an alternative to measures of performance calculated in accordance with GAAP.

The following table presents the operating results of the Company’s properties for the three and six months ended June 30, 2008 and 2007 in addition to other income and expense items affecting income from operations. The Company breaks out Same Park operations to provide information regarding trends for properties the Company has held for the periods being compared (in thousands, except per square foot data):

	For the Three Months Ended June 30,			For the Six Months Ended June 30,		
	2008	2007	Change	2008	2007	Change
Rental income:						
Same Park (18.7 million rentable square feet) (1)	\$ 66,638	\$ 64,675	3.0%	\$ 133,034	\$ 128,822	3.3%
Non-Same Park (870,000 square feet) (2)	3,808	2,600	46.5%	7,523	3,577	110.3%
Total rental income	70,446	67,275	4.7%	140,557	132,399	6.2%
Cost of operations:						
Same Park	20,763	20,251	2.5%	42,006	40,423	3.9%
Non-Same Park	1,176	771	52.5%	2,423	1,038	133.4%
Total cost of operations	21,939	21,022	4.4%	44,429	41,461	7.2%
Net operating income (3):						
Same Park	45,875	44,424	3.3%	91,028	88,399	3.0%
Non-Same Park	2,632	1,829	43.9%	5,100	2,539	100.9%
Total net operating income	48,507	46,253	4.9%	96,128	90,938	5.7%
Other income and expenses:						
Facility management fees	177	182	(2.7%)	372	365	1.9%
Interest and other income	282	1,189	(76.3%)	610	2,990	(79.6%)
Interest expense	(990)	(1,012)	(2.2%)	(1,983)	(2,119)	(6.4%)
Depreciation and amortization	(25,120)	(24,916)	0.8%	(50,567)	(46,556)	8.6%
General and administrative	(2,085)	(2,112)	(1.3%)	(4,131)	(3,814)	8.3%
Income before minority interest	\$ 20,771	\$ 19,584	6.1%	\$ 40,429	\$ 41,804	(3.3%)
Same Park gross margin (4)	68.8%	68.7%	0.1%	68.4%	68.6%	(0.3%)
Same Park weighted average for the period:						
Occupancy	93.7%	93.5%	0.2%	94.0%	93.3%	0.8%
Annualized realized rent per square foot (5)	\$ 15.22	\$ 14.81	2.8%	\$ 15.15	\$ 14.78	2.5%

(1) See above for a definition of Same Park.

(2) Represents operating properties owned by the Company as of June 30, 2008 that are not included in Same Park.

- (3) Net operating income (“NOI”) is an important measurement in the commercial real estate industry for determining the value of the real estate generating the NOI. See “Concentration of Portfolio by Region” above for more information on NOI. The Company’s calculation of NOI may not be comparable to those of other companies and should not be used as an alternative to measures of performance calculated in accordance with GAAP.
- (4) Same Park gross margin is computed by dividing Same Park NOI by Same Park rental income.
- (5) Same Park realized rent per square foot represents the annualized Same Park rental income earned per occupied square foot.

The following tables summarize the Same Park operating results by major geographic region for the three and six months ended June 30, 2008 and 2007. In addition, the tables reflect the comparative impact on the overall rental income, cost of operations and NOI from properties that have been acquired since January 1, 2007, and the impact of such is included in Non-Same Park facilities in the tables below (in thousands):

Three Months Ended June 30, 2008 and 2007:

Region	Rental Income June 30, 2008	Rental Income June 30, 2007	Increase (Decrease)	Cost of Operations June 30, 2008	Cost of Operations June 30, 2007	Increase (Decrease)	NOI June 30, 2008	NOI June 30, 2007	Increase (Decrease)
Southern California	\$ 16,421	\$ 15,918	3.2%	\$ 4,134	\$ 4,216	(1.9%)	\$ 12,287	\$ 11,702	5.0%
Northern California	5,297	4,906	8.0%	1,543	1,503	2.7%	3,754	3,403	10.3%
Southern Texas	3,218	2,892	11.3%	1,481	1,257	17.8%	1,737	1,635	6.2%
Northern Texas	4,207	3,697	13.8%	1,670	1,508	10.7%	2,537	2,189	15.9%
South Florida	7,980	7,802	2.3%	2,622	2,569	2.1%	5,358	5,233	2.4%
Virginia	13,986	13,181	6.1%	4,052	3,800	6.6%	9,934	9,381	5.9%
Maryland	9,118	9,861	(7.5%)	2,855	3,042	(6.1%)	6,263	6,819	(8.2%)
Oregon	4,591	4,555	0.8%	1,618	1,561	3.7%	2,973	2,994	(0.7%)
Arizona	1,731	1,778	(2.6%)	761	770	(1.2%)	970	1,008	(3.8%)
Washington	89	85	4.7%	27	25	8.0%	62	60	3.3%
Total Same Park	66,638	64,675	3.0%	20,763	20,251	2.5%	45,875	44,424	3.3%
Non-Same Park	3,808	2,600	46.5%	1,176	771	52.5%	2,632	1,829	43.9%
Total before depreciation and amortization	70,446	67,275	4.7%	21,939	21,022	4.4%	48,507	46,253	4.9%
Depreciation and amortization	—	—	—	25,120	24,916	0.8%	(25,120)	(24,916)	0.8%
Total based on GAAP	\$ 70,446	\$ 67,275	4.7%	\$ 47,059	\$ 45,938	2.4%	\$ 23,387	\$ 21,337	9.6%

Six Months Ended June 30, 2008 and 2007:

Region	Rental Income June 30, 2008	Rental Income June 30, 2007	Increase (Decrease)	Cost of Operations June 30, 2008	Cost of Operations June 30, 2007	Increase (Decrease)	NOI June 30, 2008	NOI June 30, 2007	Increase (Decrease)
Southern California	\$ 32,661	\$ 31,728	2.9%	\$ 8,381	\$ 8,396	(0.2%)	\$ 24,280	\$ 23,332	4.1%
Northern California	10,497	9,943	5.6%	2,959	2,803	5.6%	7,538	7,140	5.6%
Southern Texas	6,292	5,694	10.5%	2,821	2,597	8.6%	3,471	3,097	12.1%
Northern Texas	8,372	7,334	14.2%	3,108	3,042	2.2%	5,264	4,292	22.6%
South Florida	16,006	15,549	2.9%	5,370	5,040	6.5%	10,636	10,509	1.2%
Virginia	27,781	26,172	6.1%	8,410	7,865	6.9%	19,371	18,307	5.8%
Maryland	18,531	19,392	(4.4%)	5,929	6,030	(1.7%)	12,602	13,362	(5.7%)
Oregon	9,243	9,415	(1.8%)	3,434	3,142	9.3%	5,809	6,273	(7.4%)
Arizona	3,476	3,433	1.3%	1,540	1,459	5.6%	1,936	1,974	(1.9%)
Washington	175	162	8.0%	54	49	10.2%	121	113	7.1%
Total Same Park	133,034	128,822	3.3%	42,006	40,423	3.9%	91,028	88,399	3.0%
Non-Same Park	7,523	3,577	110.3%	2,423	1,038	133.4%	5,100	2,539	100.9%
Total before depreciation and amortization	140,557	132,399	6.2%	44,429	41,461	7.2%	96,128	90,938	5.7%
Depreciation and amortization	—	—	—	50,567	46,556	8.6%	(50,567)	(46,556)	8.6%
Total based on GAAP	\$ 140,557	\$ 132,399	6.2%	\$ 94,996	\$ 88,017	7.9%	\$ 45,561	\$ 44,382	2.7%

Revenues: Revenues increased \$3.2 million for the three months ended June 30, 2008, over the same period in 2007 driven primarily by an increase of \$2.0 million from the Company’s Same Park portfolio as a result of a slight improvement in occupancy and higher realized rental rates. In addition, the Company had an increase of \$1.2 million from assets acquired during 2007. Revenues increased \$8.2 million for the six months ended June 30, 2008, over the same period in 2007 driven primarily by an increase of \$4.2 million from the Company’s Same Park portfolio which was also due to a slight improvement in occupancy and higher rental rates combined with an increase of \$3.9 million from assets acquired during 2007.

Facility Management Operations: The Company’s facility management operations account for a small portion of the Company’s net income. During the three months ended June 30, 2008, \$177,000 in revenue was recognized from facility management operations compared to \$182,000 for the same period in 2007. During the six months ended June 30, 2008, \$372,000 in revenue was recognized from facilities management operations compared to \$365,000 for the same period in 2007.

Cost of Operations: Cost of operations for the three months ended June 30, 2008 was \$21.9 million compared to \$21.0 million for the same period in 2007, an increase of \$917,000 or 4.4%. Assets acquired in 2007 accounted for \$405,000 or 44.2% of the increase. Cost of operations as a percentage of rental income remained fairly consistent for the three months ended June 30, 2008 and 2007 at 31.1% and 31.2%, respectively. The higher levels of operating costs is driven by an increase in property taxes of \$816,000 as a result of increases in both rates and assessed values, utilities costs of \$208,000 and repairs and maintenance costs of \$194,000 offset with a decrease in other expenses of \$406,000 as a result of a decrease in personnel procurement cost, marketing materials and third party services. Cost of operations for the six months ended June 30, 2008 was \$44.4 million compared to \$41.5 million for the same period in 2007, an increase of \$3.0 million or 7.2%. Assets acquired in 2007 accounted for \$1.4 million or 46.7% of the increase. Cost of operations as a percentage of rental income increased slightly for the six months ended June 30, 2008 and 2007 at 31.6% and 31.3%, respectively. The increase as a percentage of rental income is primarily due to an increase in property taxes of \$1.4 million as a result of increase in both rates and assessed values, repairs and maintenance costs of \$740,000, utilities cost of \$486,000 and payroll costs of \$379,000 offset by a decrease in other expenses of \$278,000 due to a decrease in personnel procurement costs, marketing materials and third party services.

Depreciation and Amortization Expense: Depreciation and amortization expense for the three months ended June 30, 2008 was \$25.1 million compared to \$24.9 million for the same period in 2007. Depreciation and amortization expense for the six months ended June 30, 2008 was \$50.6 million compared to \$46.6 million for the same period in 2007. This increase is primarily due to the acquisition of 870,000 square feet during 2007, as well as depreciation expense on capital and tenant improvements acquired during 2008 and 2007.

General and Administrative Expense: General and administrative expense consisted of the following expenses (in thousands):

	For the Three Months Ended		Increase (Decrease)
	June 30,		
	2008	2007	
Compensation expense	\$ 855	\$ 815	4.9%
Stock compensation expense	727	808	(10.0%)
Professional and investor services	309	302	2.3%
Other expenses	194	187	3.7%
Total	\$ 2,085	\$ 2,112	(1.3%)

	For the Six Months Ended		Increase (Decrease)
	June 30,		
	2008	2007	
Compensation expense	\$ 1,766	\$ 1,649	7.1%
Stock compensation expense	1,415	1,171	20.8%
Professional and investor services	583	597	(2.3%)
Other expenses	367	397	(7.6%)
Total	\$ 4,131	\$ 3,814	8.3%

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For the three months ended June 30, 2008, general and administrative costs have decreased \$27,000 or 1.3% over the same period in 2007. For the six months ended June 30, 2008, general and administrative costs have increased \$317,000 or 8.3% over the same period in 2007. The increase was primarily the result of higher stock compensation expense related to the long-term incentive plan for senior management.

Interest and Other Income: Interest and other income reflect earnings on cash balances in addition to miscellaneous income items. Interest income was \$255,000 for the three months ended June 30, 2008 compared to \$1.2 million for the same period in 2007. Interest income was \$561,000 and \$2.9 million for the six months ended June 30, 2008 and 2007, respectively. The decrease is attributable to lower cash balances and lower effective interest rates. Average cash balances and effective interest rates for the six months ended June 30, 2008 were \$43.2 million and 2.6%, respectively, compared to \$114.5 million and 5.1%, respectively, for the same period in 2007.

Interest Expense: Interest expense was \$990,000 for the three months ended June 30, 2008 compared to \$1.0 million for the same period in 2007. Interest expense was \$2.0 million and \$2.1 million for the six months ended June 30, 2008 and 2007, respectively. The decrease is primarily attributable to the repayment of a mortgage note of \$5.0 million during the first quarter of 2007.

Minority Interest in Income: Minority interest in income reflects the income allocable to equity interests in the Operating Partnership that are not owned by the Company. Minority interest in income was \$3.4 million (\$1.8 million allocated to preferred unit holders and \$1.6 million allocated to common unit holders) for the three months ended June 30, 2008 compared to \$3.0 million (\$1.8 million allocated to preferred unit holders and \$1.3 million allocated to common unit holders) for the same period in 2007. The increase in minority interest in income for the three months ended June 30, 2008 over the same period of 2007 was primarily due to an increase in income allocated to common unit holders. Minority interest in income was \$6.5 million (\$3.5 million allocated to preferred unit holders and \$3.0 million allocated to common unit holders) for the six months ended June 30, 2008 compared to \$6.7 million (\$3.4 million allocated to preferred unit holders and \$3.3 million allocated to common unit holders) for the same period in 2007. The decrease in minority interest in income for the six months ended June 30, 2008 over the same period of 2007 was primarily due to a decrease in interest and other income partially offset by an increase in cash distributions to preferred unit holders.

Liquidity and Capital Resources

Cash and cash equivalents increased \$3.3 million from \$35.0 million at December 31, 2007 to \$38.3 million at June 30, 2008. The increase was primarily due to retained cash from operations offset by the repurchase of common stock.

Net cash provided by operating activities for the six months ended June 30, 2008 and 2007 was \$98.4 million and \$91.6 million, respectively. Management believes that the Company's internally generated net cash provided by operating activities will be sufficient to enable it to meet its operating expenses, capital improvements, debt service requirements and distributions to shareholders in addition to providing additional cash for future growth and debt repayment.

Net cash used in investing activities was \$19.9 million and \$131.1 million for the six months ended June 30, 2008 and 2007, respectively. The change of \$111.1 million was primarily due to property acquisitions in Washington and California for a combined total of \$113.8 million during the first quarter of 2007 offset with an increase in capital improvements of \$2.7 million.

Net cash used in financing activities for the six months ended June 30, 2008 was \$75.2 million compared to net cash provided by financing activities for the six months ended June 30, 2007 of \$46.3 million. The change of \$121.5 million was primarily due to a decrease of \$151.2 million in net proceeds from the issuance of preferred equity, an increase of cash paid for common stock repurchases of \$21.6 million and an increase in preferred and common equity distributions of \$3.7 million offset with a decrease of \$50.0 million in preferred equity redemptions.

The Company's preferred equity outstanding increased to 35.2% of its market capitalization during the six months ended June 30, 2008. The Company's capital structure is characterized by a low level of leverage. As of June 30, 2008, the Company had six fixed-rate mortgages totaling \$60.0 million, which represented 2.6% of its total market capitalization. The Company calculates market capitalization by adding (1) the liquidation preference of the Company's outstanding preferred equity, (2) principal value of the Company's outstanding mortgages and (3) the total number of common shares and common units outstanding at June 30, 2008 multiplied by the closing price of the stock on that date. The weighted average interest rate for the mortgages is approximately 5.9% per annum. The Company had approximately 7.6% of its properties, in terms of net book value, encumbered at June 30, 2008.

The Company focuses on retaining cash for reinvestment as we believe that this provides the greatest level of financial flexibility. During the six months ended June 30, 2008 and 2007, the Company generated approximately \$20.7 million and \$25.4 million, respectively, of retained cash. The Company defines retained cash as funds from operations less recurring capital expenditures, distributions and other non-cash adjustments. The amount of cash we retain depends in part on the amount of distributions we make to our shareholders, and, because the U.S. federal income tax rules applicable to real estate investment trusts ("REIT") require us to distribute 90% of our taxable income to our shareholders, the amount of our distributions depends in part on the amount of our taxable income. Taxable income is a function of many factors which include, among others, the Company's operating income, acquisition activity and preferred distributions. The Company takes these requirements into account when formulating strategies to increase the amount of its retained cash. As the Company continues to grow as a function of improving operating fundamentals and acquisitions, taxable income has and will likely continue to increase, requiring increased distributions to the Company's common shareholders. During the second quarter of 2007, the Company increased its quarterly dividend from \$0.29 per common share to \$0.44 per common share. With retained cash of \$9.9 million for the three months ended June 30, 2008, the Company believes it has sufficient cash flow to cover the increased dividend. Going forward, the Company will continue to monitor its taxable income and the corresponding dividend requirements.

Subsequent to June 30, 2008, the Company extended the term of its line of credit (the "Credit Facility") with Wells Fargo Bank to August 1, 2010. The Credit Facility has a borrowing limit of \$100.0 million. Interest on outstanding borrowings is payable monthly. At the option of the Company, the rate of interest charged is equal to (i) the prime rate or (ii) a rate ranging from the London Interbank Offered Rate ("LIBOR") plus 0.70% to LIBOR plus 1.50% depending on the Company's credit ratings and coverage ratios, as defined (currently LIBOR plus 0.85%). In addition, the Company is required to pay an annual commitment fee ranging from 0.15% to 0.30% of the borrowing limit (currently 0.20%). In connection with the modification of the Credit Facility, the Company paid a fee of \$300,000, which will be amortized over the life of the Credit Facility. The Company had no balance outstanding as of June 30, 2008 or December 31, 2007.

Non-GAAP Supplemental Disclosure Measure: Funds from Operations: Management believes that Funds from Operations ("FFO") is a useful supplemental measure of the Company's operating performance. The Company computes FFO in accordance with the White Paper on FFO approved by the Board of Governors of the National Association of Real Estate Investment Trusts ("NAREIT"). The White Paper defines FFO as net income, computed in accordance with GAAP, before depreciation, amortization, minority interest in income, gains or losses on asset dispositions and extraordinary items. Management believes that FFO provides a useful measure of the Company's operating performance and when compared year over year, reflects the impact to operations from trends in occupancy rates, rental rates, operating costs, development activities, general and administrative expenses and interest costs, providing a perspective not immediately apparent from net income.

FFO should be analyzed in conjunction with net income. However, FFO should not be viewed as a substitute for net income as a measure of operating performance or liquidity as it does not reflect depreciation and amortization costs or the level of capital expenditure and leasing costs necessary to maintain the operating performance of the Company's properties, which are significant economic costs and could materially impact the Company's results from operations.

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Management believes FFO provides useful information to the investment community about the Company's operating performance when compared to the performance of other real estate companies, as FFO is generally recognized as the industry standard for reporting operations of REITs. Other REITs may use different methods for calculating FFO and, accordingly, our FFO may not be comparable to other real estate companies.

FFO for the Company is computed as follows (in thousands):

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
Net income allocable to common shareholders	\$ 4,623	\$ 3,781	\$ 8,425	\$ 9,704
Depreciation and amortization	25,120	24,916	50,567	46,556
Minority interest in income — common units	1,639	1,294	2,987	3,324
Consolidated FFO allocable to common shareholders and minority interests	31,382	29,991	61,979	59,584
FFO allocated to minority interests — common units	(8,222)	(7,648)	(16,238)	(15,194)
FFO allocated to common shareholders	<u>\$ 23,160</u>	<u>\$ 22,343</u>	<u>\$ 45,741</u>	<u>\$ 44,390</u>

FFO allocated to common shareholders and minority interests for the six months ended June 30, 2008 increased 4.0% from the same period in 2007. The increase in FFO for the six months ended June 30, 2008 over the same period of 2007 was primarily due to an increase in net operating income partially offset by a decrease in interest income.

Capital Expenditures: During the six months ended June 30, 2008, the Company expended \$18.8 million in recurring capital expenditures or \$0.96 per weighted average square foot owned. The Company defines recurring capital expenditures as those necessary to maintain and operate its commercial real estate at its current economic value. During the six months ended June 30, 2007, the Company expended \$14.8 million in recurring capital expenditures or \$0.77 per weighted average square foot owned. The following table shows total capital expenditures for the stated periods (in thousands):

	For the Six Months Ended June 30,	
	2008	2007
Recurring capital expenditures	\$ 18,838	\$ 14,805
Property renovations and other capital expenditures	1,098	2,467
Total capital expenditures	<u>\$ 19,936</u>	<u>\$ 17,272</u>

Stock Repurchase: The Company's Board of Directors previously authorized the repurchase, from time to time, of up to 6.5 million shares of the Company's common stock on the open market or in privately negotiated transactions. During the six months ended June 30, 2008, the Company repurchased 370,042 shares of common stock at an aggregate cost of \$18.3 million or an average cost per share of \$49.52. Since inception of the program, the Company has repurchased an aggregate of 4.3 million shares of common stock at an aggregate cost of \$152.8 million or an average cost per share of \$35.84. Under existing board authorizations, the Company can repurchase an additional 2.2 million shares.

Distributions: The Company has elected and intends to qualify as a REIT for federal income tax purposes. In order to maintain its status as a REIT, the Company must meet, among other tests, sources of income, share ownership and certain asset tests. As a REIT, the Company is not taxed on that portion of its taxable income that is distributed to its shareholders provided that at least 90% of its taxable income is distributed to its shareholders prior to the filing of its tax return.

Related Party Transactions: At June 30, 2008, Public Storage ("PS") owned 26.5% of the outstanding shares of the Company's common stock and 26.3% of the outstanding common units of the Operating Partnership (100% of the common units not owned by the Company). Assuming conversion of its partnership units, PS would own 45.9% of the outstanding shares of the Company's common stock. Ronald L. Havner, Jr., the Company's chairman, is also the Chief Executive Officer, President and a Director of PS. Harvey Lenkin is a Director of both the Company and PS.

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Pursuant to a cost sharing and administrative services agreement, the Company shares costs with PS and affiliated entities for certain administrative services, which are allocated among PS and its affiliates in accordance with a methodology intended to fairly allocate those costs. These costs totaled \$97,000 and \$76,000 for the three months ended June 30, 2008 and 2007, respectively and \$195,000 and \$152,000 for the six months ended June 30, 2008 and 2007, respectively. In addition, the Company provides property management services for properties owned by PS and its affiliates for a fee of 5% of the gross revenues of such properties in addition to reimbursement of direct costs. These management fee revenues recognized under management contracts with affiliated parties totaled \$177,000 and \$182,000 for the three months ended June 30, 2008 and 2007, respectively and \$372,000 and \$365,000 for the six months ended June 30, 2008 and 2007, respectively. In December, 2006, PS also began providing property management services for the mini storage component of two assets owned by the Company for a fee of 6% of the gross revenues of such properties in addition to reimbursement of certain costs. Management fee expense recognized under the management contracts with PS totaled approximately \$13,000 and \$12,000 for the three months ended June 30, 2008 and 2007, respectively and \$24,000 for the six months ended June 30, 2008 and 2007.

Off-Balance Sheet Arrangements: The Company does not have any off-balance sheet arrangements.

Contractual Obligations: The Company is scheduled to pay cash dividends of approximately \$58.0 million per year on its preferred equity outstanding as of June 30, 2008. Dividends are paid when and if declared by the Company's Board of Directors and accumulate if not paid. Shares and units of preferred equity are redeemable by the Company in order to preserve its status as a REIT and are also redeemable five years after issuance.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

To limit the Company's exposure to market risk, the Company principally finances its operations and growth with permanent equity capital consisting of either common or preferred stock. At June 30, 2008, the Company's debt as a percentage of shareholders' equity and minority interest (based on book values) was 4.4%.

The Company's market risk sensitive instruments at June 30, 2008 include mortgage notes payable of \$60.0 million and the Company's Credit Facility. All of the Company's mortgage notes payable bear interest at fixed rates. At June 30, 2008, the Company had no balance outstanding under its Credit Facility. See Notes 5 and 6 to the consolidated financial statements for terms, valuations and approximate principal maturities of the mortgage notes payable and line of credit as of June 30, 2008. Based on borrowing rates currently available to the Company, combined with the amount of fixed-rate debt financing, the difference between the carrying amount of debt and its fair value is insignificant.

ITEM 4. CONTROLS AND PROCEDURES

The Company's management, with the participation of the Company's chief executive officer and chief financial officer, evaluated the effectiveness of the Company's disclosure controls and procedures as of June 30, 2008. The term "disclosure controls and procedures," as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of the Company's disclosure controls and procedures as of June 30, 2008, the Company's chief executive officer and chief financial officer concluded that, as of such date, the Company's disclosure controls and procedures were effective at the reasonable assurance level.

No change in the Company's internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the fiscal quarter ended June 30, 2008 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The information contained in Note 10 to the consolidated financial statements in this Form 10-Q regarding legal proceedings is incorporated by reference in this Item 1.

ITEM 1A. RISK FACTORS

In addition to the other information in this Form 10-Q, the following factors should be considered in evaluating our company and our business. There have been no material changes from the risk factors set forth in our Annual Report on Form 10-K for the year ended December 31, 2007.

PS has significant influence over us.

At June 30, 2008, PS and its affiliates owned 26.5% of the outstanding shares of the Company's common stock and 26.3% of the outstanding common units of the Operating Partnership (100% of the common units not owned by the Company). Assuming conversion of its partnership units, PS would own 45.9% of the outstanding shares of the Company's common stock. Ronald L. Havner, Jr., the Company's chairman, is also the Chief Executive Officer, President and a Director of PS. Harvey Lenkin is a Director of both the Company and PS. Consequently, PS has the ability to significantly influence all matters submitted to a vote of our shareholders, including electing directors, changing our articles of incorporation, dissolving and approving other extraordinary transactions such as mergers, and all matters requiring the consent of the limited partners of the Operating Partnership. PS's interest in such matters may differ from other shareholders. In addition, PS's ownership may make it more difficult for another party to take over our company without PS's approval.

Provisions in our organizational documents may prevent changes in control.

Our articles generally prohibit owning more than 7% of our shares: Our articles of incorporation restrict the number of shares that may be owned by any other person, and the partnership agreement of our Operating Partnership contains an anti-takeover provision. No shareholder (other than PS and certain other specified shareholders) may own more than 7% of the outstanding shares of our common stock, unless our board of directors waives this limitation. We imposed this limitation to avoid, to the extent possible, a concentration of ownership that might jeopardize our ability to qualify as a REIT. This limitation, however, also makes a change of control much more difficult (if not impossible) even if it may be favorable to our public shareholders. These provisions will prevent future takeover attempts not approved by PS even if a majority of our public shareholders consider it to be in their best interests because they would receive a premium for their shares over market value or for other reasons.

Our board can set the terms of certain securities without shareholder approval: Our board of directors is authorized, without shareholder approval, to issue up to 50.0 million shares of preferred stock and up to 100.0 million shares of Equity Stock, in each case in one or more series. Our board has the right to set the terms of each of these series of stock. Consequently, the board could set the terms of a series of stock that could make it difficult (if not impossible) for another party to take over our company even if it might be favorable to our public shareholders. Our articles of incorporation also contain other provisions that could have the same effect. We can also cause our Operating Partnership to issue additional interests for cash or in exchange for property.

The partnership agreement of our Operating Partnership restricts mergers: The partnership agreement of our Operating Partnership generally provides that we may not merge or engage in a similar transaction unless the limited partners of our Operating Partnership are entitled to receive the same proportionate payments as our shareholders. In addition, we have agreed not to merge unless the merger would have been approved had the limited partners been able to vote together with our shareholders, which has the effect of increasing PS's influence over us due to PS's ownership of operating partnership units. These provisions may make it more difficult for us to merge with another entity.

Our Operating Partnership poses additional risks to us.

Limited partners of our Operating Partnership, including PS, have the right to vote on certain changes to the partnership agreement. They may vote in a way that is against the interests of our shareholders. Also, as general partner of our Operating Partnership, we are required to protect the interests of the limited partners of the Operating Partnership. The interests of the limited partners and of our shareholders may differ.

We would incur adverse tax consequences if we fail to qualify as a REIT.

Our cash flow would be reduced if we fail to qualify as a REIT: While we believe that we have qualified since 1990 to be taxed as a REIT, and will continue to be so qualified, we cannot be certain. To continue to qualify as a REIT, we need to satisfy certain requirements under the federal income tax laws relating to our income, assets, distributions to shareholders and shareholder base. In this regard, the share ownership limits in our articles of incorporation do not necessarily ensure that our shareholder base is sufficiently diverse for us to qualify as a REIT. For any year we fail to qualify as a REIT, we would be taxed at regular corporate tax rates on our taxable income unless certain relief provisions apply. Taxes would reduce our cash available for distributions to shareholders or for reinvestment, which could adversely affect us and our shareholders. Also we would not be allowed to elect REIT status for five years after we fail to qualify unless certain relief provisions apply.

We may need to borrow funds to meet our REIT distribution requirements:To qualify as a REIT, we must generally distribute to our shareholders 90% of our taxable income. Our income consists primarily of our share of our Operating Partnership's income. We intend to make sufficient distributions to qualify as a REIT and otherwise avoid corporate tax. However, differences in timing between income and expenses and the need to make nondeductible expenditures such as capital improvements and principal payments on debt could force us to borrow funds to make necessary shareholder distributions.

Since we buy and operate real estate, we are subject to general real estate investment and operating risks.

Summary of real estate risks: We own and operate commercial properties and are subject to the risks of owning real estate generally and commercial properties in particular. These risks include:

- the national, state and local economic climate and real estate conditions, such as oversupply of or reduced demand for space and changes in market rental rates;
- how prospective tenants perceive the attractiveness, convenience and safety of our properties;
- difficulties in consummating and financing acquisitions and developments on advantageous terms and the failure of acquisitions and developments to perform as expected;
- our ability to provide adequate management, maintenance and insurance;
- our ability to collect rent from tenants on a timely basis;
- the expense of periodically renovating, repairing and reletting spaces;
- environmental issues;
- compliance with the Americans with Disabilities Act and other federal, state, and local laws and regulations;
- increasing operating costs, including real estate taxes, insurance and utilities, if these increased costs cannot be passed through to tenants;
- changes in tax, real estate and zoning laws;
- increase in new commercial properties in our market;
- tenant defaults and bankruptcies;
- tenants' right to sublease space; and
- concentration of properties leased to non-rated private companies.

Certain significant costs, such as mortgage payments, real estate taxes, insurance and maintenance, generally are not reduced even when a property's rental income is reduced. In addition, environmental and tax laws, interest rate levels, the availability of financing and other factors may affect real estate values and property income. Furthermore, the supply of commercial space fluctuates with market conditions.

If our properties do not generate sufficient income to meet operating expenses, including any debt service, tenant improvements, lease commissions and other capital expenditures, we may have to borrow additional amounts to cover fixed costs, and we may have to reduce our distributions to shareholders.

We may be unable to consummate acquisitions and developments on advantageous terms, or new acquisitions and developments may fail to perform as expected: We continue to seek to acquire and develop flex, industrial and office properties where they meet our criteria and we believe that they will enhance our future financial performance and the value of our portfolio. Our belief, however, is based on and is subject to risks, uncertainties and other factors, many of which are forward-looking and are uncertain in nature or are beyond our control, including the risks that our acquisitions and developments may not perform as expected, that we may be unable to quickly integrate new acquisitions and developments into our existing operations and that any costs to develop projects or redevelop acquired properties may exceed estimates. Further, we face significant competition for suitable acquisition properties from other real estate investors, including other publicly traded real estate investment trusts and private institutional investors. As a result, we may be unable to acquire additional properties we desire or the purchase price for desirable properties may be significantly increased. In addition, some of these properties may have unknown characteristics or deficiencies or may not complement our portfolio of existing properties. In addition, we may finance future acquisitions and developments through a combination of borrowings, proceeds from equity or debt offerings by us or the Operating Partnership, and proceeds from property divestitures. These financing options may not be available when desired or required or may be more costly than anticipated, which could adversely affect our cash flow. Real property development is subject to a number of risks, including construction delays, complications in obtaining necessary zoning, occupancy and other governmental permits, cost overruns, financing risks, and the possible inability to meet expected occupancy and rent levels. If any of these problems occur, development costs for a project may increase, and there may be costs incurred for projects that are not completed. As a result of the foregoing, some properties may be worth less or may generate less revenue than, or simply not perform as well as, we believed at the time of acquisition or development, negatively affecting our operating results. Any of the foregoing risks could adversely affect our financial condition, operating results and cash flow, and our ability to pay dividends on, and the market price of, our stock. In addition, we may be unable to successfully integrate and effectively manage the properties we do acquire and develop, which could adversely affect our results of operations.

We may encounter significant delays and expense in reletting vacant space, or we may not be able to relet space at existing rates, in each case resulting in losses of income: When leases expire, we will incur expenses in retrofitting space, and we may not be able to re-lease the space on the same terms. Certain leases provide tenants with the right to terminate early if they pay a fee. As of June 30, 2008, our properties generally have lower vacancy rates than the average for the markets in which they are located, and leases accounting for 9.6% of our total annualized rental income expire in 2008 and 22.1% in 2009. While we have estimated our cost of renewing leases that expire in 2008 and 2009, our estimates could be wrong. If we are unable to re-lease space promptly, if the terms are significantly less favorable than anticipated or if the costs are higher, we may have to reduce our distributions to shareholders.

Tenant defaults and bankruptcies may reduce our cash flow and distributions: We may have difficulty in collecting from tenants in default, particularly if they declare bankruptcy. This could affect our cash flow and distributions to shareholders. Since many of our tenants are non-rated private companies, this risk may be enhanced. There is inherent uncertainty in a tenant's ability to continue paying rent if they are in bankruptcy. As of June 30, 2008, the Company had approximately 13,000 square feet occupied by tenants that are protected by Chapter 11 of the U.S. Bankruptcy Code. Several other tenants have contacted us requesting early termination of their lease, reduction in space under lease, rent deferment or abatement. At this time, the Company cannot anticipate what effect, if any, the ultimate outcome of these discussions will have on our operating results.

We may be adversely affected by significant competition among commercial properties: Many other commercial properties compete with our properties for tenants. Some of the competing properties may be newer and better located than our properties. We also expect that new properties will be built in our markets. In addition, we compete with other buyers, many of which are larger than us, for attractive commercial properties. Therefore, we may not be able to grow as rapidly as we would like.

We may be adversely affected if casualties to our properties are not covered by insurance: We could suffer uninsured losses or losses in excess of our insurance policy limits for occurrences such as earthquakes that adversely affect us or even result in loss of the property. We might still remain liable on any mortgage debt or other unsatisfied obligations related to that property.

The illiquidity of our real estate investments may prevent us from adjusting our portfolio to respond to market changes: There may be delays and difficulties in selling real estate. Therefore, we cannot easily change our portfolio when economic conditions change. Also, tax laws limit a REIT's ability to sell properties held for less than four years.

We may be adversely affected by changes in laws: Increases in income and service taxes may reduce our cash flow and ability to make expected distributions to our shareholders. Our properties are also subject to various federal, state and local regulatory requirements, such as state and local fire and safety codes. If we fail to comply with these requirements, governmental authorities could fine us or courts could award damages against us. We believe our properties comply with all significant legal requirements. However, these requirements could change in a way that would reduce our cash flow and ability to make distributions to shareholders.

We may incur significant environmental remediation costs: Under various federal, state and local environmental laws, an owner or operator of real estate may have to clean spills or other releases of hazardous or toxic substances on or from a property. Certain environmental laws impose liability whether or not the owner knew of, or was responsible for, the presence of the hazardous or toxic substances. In some cases, liability may exceed the value of the property. The presence of toxic substances, or the failure to properly remedy any resulting contamination, may make it more difficult for the owner or operator to sell, lease or operate its property or to borrow money using its property as collateral. Future environmental laws may impose additional material liabilities on us.

We depend on external sources of capital to grow our company.

We are generally required under the Internal Revenue Code to distribute at least 90% of our taxable income. Because of this distribution requirement, we may not be able to fund future capital needs, including any necessary building and tenant improvements, from operating cash flow. Consequently, we may need to rely on third-party sources of capital to fund our capital needs. We may not be able to obtain the financing on favorable terms or at all. Access to third-party sources of capital depends, in part, on general market conditions, the market's perception of our growth potential, our current and expected future earnings, our cash flow, and the market price per share of our common stock. If we cannot obtain capital from third-party sources, we may not be able to acquire properties when strategic opportunities exist, satisfy any debt service obligations, or make cash distributions to shareholders.

Our ability to control our properties may be adversely affected by ownership through partnerships and joint ventures.

We own most of our properties through our Operating Partnership. Our organizational documents do not prevent us from acquiring properties with others through partnerships or joint ventures. This type of investment may present additional risks. For example, our partners may have interests that differ from ours or that conflict with ours, or our partners may become bankrupt.

We can change our business policies and increase our level of debt without shareholder approval.

Our board of directors establishes our investment, financing, distribution and our other business policies and may change these policies without shareholder approval. Our organizational documents do not limit our level of debt. A change in our policies or an increase in our level of debt could adversely affect our operations or the price of our common stock.

We can issue additional securities without shareholder approval.

We can issue preferred equity, common stock and Equity stock without shareholder approval. Holders of preferred stock have priority over holders of common stock, and the issuance of additional shares of stock reduces the interest of existing holders in our company.

Increases in interest rates may adversely affect the market price of our common stock.

One of the factors that influences the market price of our common stock is the annual rate of distributions that we pay on our common stock, as compared with interest rates. An increase in interest rates may lead purchasers of REIT shares to demand higher annual distribution rates, which could adversely affect the market price of our common stock.

Shares that become available for future sale may adversely affect the market price of our common stock.

Substantial sales of our common stock, or the perception that substantial sales may occur, could adversely affect the market price of our common stock. As of June 30, 2008, PS and its affiliates owned 26.5% of the outstanding shares of the Company's common stock and 26.3% of the outstanding common units of the Operating Partnership (100% of the common units not owned by the Company). Assuming conversion of its partnership units, PS would own 45.9% of the outstanding shares of the Company's common stock. These shares, as well as shares of common stock held by certain other significant shareholders, are eligible to be sold in the public market, subject to compliance with applicable securities laws.

We depend on key personnel.

We depend on our key personnel, including Joseph D. Russell, Jr., our President and Chief Executive Officer. The loss of Mr. Russell or other key personnel could adversely affect our operations. We maintain no key person insurance on our key personnel.

Change in taxation of corporate dividends may adversely affect the value of our shares.

The Jobs and Growth Tax Relief Reconciliation Act of 2003, enacted on May 28, 2003, generally reduces to 15% the maximum marginal rate of federal tax payable by individuals on dividends received from a regular C corporation. This reduced tax rate, however, does not apply to dividends paid to individuals by a REIT on its shares except for certain limited amounts. The earnings of a REIT that are distributed to its shareholders are generally subject to less federal income taxation on an aggregate basis than earnings of a regular C corporation that are distributed to its shareholders net of corporate-level income tax. The Jobs and Growth Tax Act, however, could cause individual investors to view stocks of regular C corporations as more attractive relative to shares of REITs than was the case prior to the enactment of the legislation because the dividends from regular C corporations, which previously were taxed at the same rate as REIT dividends, now will be taxed at a maximum marginal rate of 15% while REIT dividends will be taxed at a maximum marginal rate of 35%.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The Company's Board of Directors has authorized the repurchase, from time to time, of up to 6.5 million shares of the Company's common stock on the open market or in privately negotiated transactions. The program does not expire. Purchases will be made subject to market conditions and other investment opportunities available to the Company.

During the three months ended June 30, 2008, there were no shares of the Company's common stock repurchased. As of June 30, 2008, the Company has 2,206,221 shares available for purchase under the program.

See Note 9 to the consolidated financial statements for additional information on repurchases of equity securities.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The Company held its annual meeting of shareholders on May 5, 2008, and the following matters were voted on at the meeting:

1. The election of the following members of our Board for the succeeding year or until their successors are duly qualified and elected:

	Total Votes	
	Voted For	Withheld
Ronald L. Havner, Jr.	17,531,435	1,686,008
Joseph D. Russell, Jr.	17,659,689	1,557,754
R. Wesley Burns	19,059,261	158,182
Arthur M. Friedman	19,039,841	177,602
James H. Kropp	19,060,061	157,382
Harvey Lenkin	17,043,996	2,173,447
Michael V. McGee	19,039,647	177,796
Alan K. Pribble	18,394,689	822,754

2. The shareholders approved ratification of the appointment of Ernst & Young LLP as the Company's registered public accountants for the fiscal year ended December 31, 2008. There were 19,043,123 votes cast for ratification; 170,488 votes cast against ratification; 3,832 votes abstained; and there were no broker non-votes.

ITEM 6. EXHIBITS

Exhibits

- | | |
|--------------|--|
| Exhibit 3.1 | Restated Bylaws of PS Business Parks, Inc., as amended. Filed herewith. |
| Exhibit 12 | Statement re: Computation of Ratio of Earnings to Fixed Charges. Filed herewith. |
| Exhibit 31.1 | Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. Filed herewith. |
| Exhibit 31.2 | Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. Filed herewith. |
| Exhibit 32.1 | Certifications of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. Filed herewith. |

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Dated: August 6, 2008

PS BUSINESS PARKS, INC.

BY: /s/ Edward A. Stokx

Edward A. Stokx
Executive Vice President and Chief Financial Officer
(Principal Financial Officer)

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RESTATED BYLAWS
OF PS BUSINESS PARKS, INC.

ADOPTED ON MARCH 17, 1998, as amended

ARTICLE I

Definitions

Section 1. "Bylaws" shall mean these bylaws as amended, restated or modified from time to time. References in these bylaws to "hereof," "herein" and "hereunder" shall be deemed to refer to these bylaws and shall not be limited to the particular article or section in which such words appear.

Section 2. "Code" shall mean the Internal Revenue Code of 1986, as now enacted or hereafter amended, or successor statutes and regulations promulgated thereunder.

Section 3. "Independent Directors" shall mean directors who are not affiliated with the corporation or any of its affiliates (other than by reason of the person's status as a director of the corporation), whether by ownership of, ownership interest in, employment by, service as an officer of, or material business or professional relationship with the corporation or its affiliates.

Section 4. "REIT" and "real estate investment trust" shall mean a real estate investment trust as defined in Sections 856 to 860 of the Code.

Section 5. "Securities of the corporation" shall mean any securities issued by the corporation.

Section 6. "Shareholders" shall mean, as of any particular time, all holders of record of outstanding shares at such time.

Section 7. "shares" shall mean shares of the common stock of the corporation.

Section 8. General. Whenever a term is defined in these bylaws in the singular, the plural of such term may also be used in these bylaws as a defined term and, similarly, whenever a term is defined in the plural, the singular of such term may also be used as a defined term hereunder.

ARTICLE II

Offices

Section 1. Principal Executive Office. The principal executive office for the transaction of the business of the corporation is hereby fixed and located at 701 Western Avenue, in the City of Glendale, County of Los Angeles, State of California. The Board of Directors may change the principal executive office from one location to another. Any such change shall be noted on the bylaws opposite this section, or this section may be amended to state the new location.

Section 2. Other Offices. The board of directors may at any time establish branch or subordinate offices at any place or places where the corporation is qualified to do business.

ARTICLE III

Meetings of Shareholders

Section 1. Place of Meetings. Meetings of shareholders shall be held at any place within or outside the State of California designated by the board of directors. In the absence of any such designation, shareholders' meetings shall be held at the principal executive office of the corporation.

Section 2. Annual Meeting. The annual meeting of shareholders shall be held each year on a date and at a time designated by the board of directors. The date so designated shall be within fifteen (15) months after the last annual meeting. At each annual meeting directors shall be elected and any other proper business may be transacted.

Section 3. Special Meeting. A special meeting of the shareholders may be called at any time by the board of directors, or by the chairman of the board, or by the president, or by one or more shareholders holding shares in the aggregate entitled to cast not less than ten percent (10%) of the votes at that meeting.

If a special meeting is called by any person or persons other than the board of directors, the request shall be in writing, specifying the time of such meeting and the general nature of the business proposed to be transacted, and shall be delivered personally or sent by registered mail or by telegraphic or other facsimile transmission to the chairman of the board, the president, any vice president or the secretary of the corporation. The officer receiving the request shall cause the notice to be promptly given to the shareholders entitled to vote, in accordance with the provisions of Sections 4 and 5 of this Article III, that a meeting will be held at the time requested by the person or persons calling the meeting not less than thirty-five (35) nor more than sixty (60) days after the receipt of the request. If the notice is not given within twenty (20) days after receipt of the request, the person or persons requesting the meeting may give the notice. Nothing contained in this paragraph of this Section 3 shall be construed as limiting, fixing or affecting the time when a meeting of shareholders called by action of the board of directors may be held.

Section 4. Notice of Shareholders' Meetings. All notices of meetings of shareholders shall be sent or otherwise given in accordance with Section 5 of this Article III not less than ten (10) nor more than sixty (60) days before the date of the meeting. The notice shall specify the place, date and hour of the meeting and (i) in the case of a special meeting, the general nature of the business to be transacted, or (ii) in the case of the annual meeting, those matters which the board of directors, at the time of giving notice, intends to present for action by the shareholders. The notice of any meeting at which directors are to be elected shall include the name of any nominee or nominees whom, at the time of the notice, management intends to present for election.

If action is proposed to be taken at any meeting for approval of (i) a contract or transaction in which a director has a direct or indirect financial interest within the meaning of Section 310 of the Corporations Code of California, (ii) an amendment of the articles of incorporation pursuant to Section 902 of the Code, (iii) a reorganization of the corporation pursuant to Section 1201 of that Code, (iv) a voluntary dissolution of the corporation pursuant to Section 1900 of that Code, or (v) a distribution in dissolution other than in accordance with the rights of outstanding preferred shares pursuant to Section 2007 of that Code, the notice shall also state the general nature of that proposal.

Section 5. Manner of Giving Notice; Affidavit of Notice. Notice of any meeting of shareholders shall be given either personally or by first-class mail or telegraphic or other written communication, charges prepaid, addressed to the shareholder at the address of that shareholder appearing on the books of the corporation or given by the shareholder to the corporation for the purpose of notice. If no such address appears on the corporation's books or is so given, notice shall be deemed to have been given if sent to that shareholder by first-class mail or telegraphic or other written communication to the corporation's principal executive office, or if published at least once in a newspaper of general circulation in the county where that office is located. Notice shall be deemed to have been given at the time when delivered personally or deposited in the mail or sent by telegram or other means of written communication.

If any notice addressed to a shareholder at the address of that shareholder appearing on the books of the corporation is returned to the corporation by the United States Postal Service marked to indicate that the United States Postal Service is unable to deliver the notice to the shareholder at that address, all future notices or reports shall be deemed to have been duly given without further mailing if these shall be available to the shareholder on written demand of the shareholder at the principal executive office of the corporation for a period of one (1) year from the date of the giving of the notice.

An affidavit of the mailing or other means of giving any notice of any shareholders' meeting shall be executed by the secretary, assistant secretary or any transfer agent of the corporation giving the notice, and shall be filed and maintained in the minute book of the corporation.

Section 6. Quorum. The presence in person or by proxy of the holders of a majority of the shares entitled to vote in any meeting of shareholders shall constitute a quorum for the transaction of business. The shareholders present at a duly called or held meeting at which a quorum is present may continue to do business until adjournment, notwithstanding the withdrawal of enough shareholders to leave less than a quorum, if any action taken (other than adjournment) is approved by at least a majority of the shares required to constitute a quorum.

Section 7. Adjourned Meeting; Notice. Any shareholders' meeting, annual or special, whether or not a quorum is present, may be adjourned from time to time by the vote of the majority of the shares represented at that meeting, either in person or by proxy, but in the absence of a quorum, no other business may be transacted at that meeting, except as provided in Section 6 of this Article III.

When any meeting of shareholders, either annual or special, is adjourned to another time or place, notice need not be given of the adjourned meeting if the time and place are announced at a meeting at which the adjournment is taken, unless a new record date for the adjourned meeting is fixed, or unless the adjournment is for more than forty-five (45) days from the date set for the original meeting, in which case the board of directors shall set a new record date. Notice of any such adjourned meeting shall be given to each shareholder of record entitled to vote at the adjourned meeting in accordance with the provisions of Sections 4 and 5 of this Article III. At any adjourned meeting the corporation may transact any business which might have been transacted at the original meeting.

Section 8. Voting. The shareholders entitled to vote at any meeting of shareholders shall be determined in accordance with the provisions of Section 11 of this Article III, subject to the provisions of Sections 702 to 704, inclusive, of the Corporations Code of California (relating to voting shares held by a fiduciary, in the name of a corporation or in joint ownership). The shareholders' vote may be by voice vote or by ballot; provided, however, that any election for directors must be by ballot if demanded by any shareholder before the voting has begun. On any matter other than elections of directors, any shareholder may vote part of the shares in favor of the proposal and refrain from voting the remaining shares or vote them against the proposal, but, if the shareholder fails to specify the number of shares which the shareholder is voting affirmatively, it will be conclusively presumed that the shareholder's approving vote is with respect to all shares that the shareholder is entitled to vote. If a quorum is present, the affirmative vote of the majority of the shares represented at the meeting and entitled to vote on any matter (other than the election of directors) shall be the act of the shareholders, unless the vote of a greater number or voting by classes is required by California General Corporation Law or by the articles of incorporation or by these bylaws.

At a shareholders' meeting at which directors are to be elected, no shareholder shall be entitled to cumulate votes (*i.e.*, cast for any one or more candidates a number of votes greater than the number of the shareholder's shares) unless the candidates' names have been placed in nomination prior to commencement of the voting and a shareholder has given notice prior to commencement of the voting of the shareholder's intention to cumulate votes. If any shareholder has given such a notice, then every shareholder entitled to vote may cumulate votes for candidates in nomination and give one candidate a number of votes equal to the number of directors to be elected multiplied by the number of votes to which that shareholder's shares are entitled, or distribute the shareholder's votes on the same principle among any or all of the candidates, as the shareholder thinks fit. The candidates receiving the highest number of votes, up to the number of directors to be elected, shall be elected.

Section 9. Waiver of Notice of Consent by Absent Shareholders. The transactions of any meeting of shareholders, either annual or special, however called and noticed and wherever held, shall be as valid as though had a meeting duly held after regular call and notice, if a quorum be present either in person or by proxy, and if, either before or after the meeting, each person entitled to vote who was not present in person or by proxy, or who, though present, has at the beginning of the meeting properly objected to the transaction of any business because the meeting was not lawfully called or convened, or to particular matters of business legally required to be included in the notice but not so included, signs a written waiver of notice or a consent to a holding of the meeting or an approval of the minutes. The waiver of notice or consent need not specify either the business to be transacted or the purpose of any annual or special meeting of shareholders, except that if action is taken or proposed to be taken for approval of any of those matters specified in the second paragraph of Section 4 of this Article III, the waiver of notice or consent shall state the general nature of the proposal. All such waivers, consents or approvals shall be filed with the corporate records or made a part of the minutes of the meeting.

Section 10. Shareholder Action by Written Consent Without a Meeting. Any action which may be taken at any annual or special meeting of shareholders may be taken without a meeting and without prior notice if a consent, in writing, setting forth the action so taken is signed by the holders of outstanding shares having not less than the minimum number of votes that would be necessary to authorize or take that action at a meeting at which all shares entitled to vote on that action were present and voted. In the case of election of directors, such a consent shall be effective only if signed by the holders of all outstanding shares entitled to vote for the election of directors; provided, however, that a director may be elected at any time to fill a vacancy on the board of directors that has not been filled by the directors by the written consent of the holders of a majority of the outstanding shares entitled to vote for the election of directors. All such consents shall be filed with the secretary of the corporation and shall be maintained in the corporate records. Any shareholder giving a written consent, or the shareholder's proxy holders, or a transferee of the shares, or a personal representative of the shareholder or their respective proxy holders may revoke the consent by a writing received by the secretary of the corporation before written consents of the number of shares required to authorize the proposed action have been filed with the secretary.

If the consents of all shareholders entitled to vote have not been solicited in writing and if the unanimous written consent of all such shareholders shall not have been received, the secretary shall give prompt notice of the corporate action approved by the shareholders without a meeting. This notice shall be given in the manner specified in Section 5 of this Article III. In the case of approval of (i) contracts or transactions in which a director has a direct or indirect financial interest pursuant to Section 310 of the Corporations Code of California, (ii) indemnification of agents of the corporation pursuant to Section 317 of that Code, (iii) a reorganization of the corporation pursuant to Section 1201 of that Code, and (iv) a distribution in dissolution other than in accordance with the rights of outstanding preferred shares pursuant to Section 2007 of that Code, the notice shall be given at least ten (10) days before the consummation of any action authorized by that approval.

Section 11. Record Date for Shareholder Notice, Voting, and Giving Consents. For purposes of determining the shareholders entitled to notice of any meeting or to vote or entitled to give consent to corporate action without a meeting, the board of directors may fix, in advance, a record date which shall not be more than sixty (60) days nor less than ten (10) days before the date of any such meeting nor more than sixty (60) days before any such action without a meeting, and in this event only shareholders of record on the date so fixed are entitled to notice and to vote or to give consents, as the case may be, notwithstanding any transfer of any shares on the books of the corporation after the record date, except as otherwise provided in the California General Corporation Law.

If the board of directors does not so fix a record date:

(a) The record date for determining shareholders entitled to notice of or to vote at a meeting of shareholders shall be at the close of business on the business day next preceding the day on which notice is given or, if notice is waived, at the close of business on the business day next preceding the day on which the meeting is held.

(b) The record date for determining shareholders entitled to give consent to corporate action in writing without a meeting (i) when no prior action by the board has been taken, shall be the day on which the first written consent is given, or (ii) when prior action of the board has been taken, shall be at the close of business on the day on which the board adopts the resolution relating to that action, or the sixtieth (60th) day before the date of such other action, whichever is later.

Section 12. Proxies. Every person entitled to vote for directors or on any other matter shall have the right to do so either in person or by one or more agents authorized by a written proxy signed by the person and filed with the secretary of the corporation. A proxy shall be deemed signed if the shareholder's name is placed on the proxy (whether by manual signature, typewriting, telegraphic transmission or otherwise) by the shareholder or the shareholder's attorney-in-fact. A validly executed proxy which does not state that it is irrevocable shall continue in full force and effect unless (i) revoked by the person executing it, before the vote pursuant to that proxy, by a writing delivered to the corporation stating that the proxy is revoked, or by a subsequent proxy executed by, or attendance at the meeting and voting in person by, the person executing the proxy; or (ii) written notice of the death or incapacity of the maker of that proxy is received by the corporation before the vote pursuant to that proxy is counted; provided, however, that no proxy shall be valid after the expiration of eleven (11) months from the date of the proxy unless otherwise provided in the proxy. The revocability of a proxy that states on its face that it is irrevocable shall be governed by the provisions of Sections 705(e) and 705(f) of the Corporations Code of California.

Section 13. Inspectors of Election. Before any meeting of shareholders, the board of directors may appoint any persons other than nominees for office to act as inspectors of election at the meeting or its adjournment. If no inspectors of election are so appointed, the chairman of the meeting may, and on the request of any shareholder or a shareholder's proxy shall, appoint inspectors of election at the meeting. The number of inspectors shall be either one (1) or three (3). If inspectors are appointed at a meeting on the request of one or more shareholders or proxies, the holders of a majority of shares or their proxies present at the meeting shall determine whether one (1) or three (3) inspectors are to be appointed. If any person appointed as inspector fails to appear or fails or refuses to act, the chairman of the meeting may, and upon the request of any shareholder or a shareholder's proxy shall, appoint a person to fill that vacancy.

These inspectors shall:

- (a) determine the number of shares outstanding and the voting power of each, the shares represented at the meeting, the existence of a quorum, and the authenticity, validity and effect of proxies;
- (b) receive votes, ballots or consents;
- (c) hear and determine all challenges and questions in any way arising in connection with the right to vote;
- (d) count and tabulate all votes or consents;
- (e) determine when the polls shall close;
- (f) determine the result; and
- (g) do any other acts that may be proper to conduct the election or vote with fairness to all shareholders.

ARTICLE IV

Directors

Section 1. Powers. Subject to the provisions of the California General Corporation Law and any limitations in the articles of incorporation and these bylaws relating to action required to be approved by the shareholders or by the outstanding shares, the business and affairs of the corporation shall be managed and all corporate powers shall be exercised by or under the direction of the board of directors.

Without prejudice to these general powers and subject to the same limitations, the directors shall have the power to:

- (a) select and remove all officers, agents and employees of the corporation; prescribe any powers and duties for them that are consistent with law, with the articles of incorporation and with these bylaws; fix their compensation; and require from them security for faithful service.
- (b) change the principal executive office or the principal business office in the State of California from one location to another; cause the corporation to be qualified to do business in any other state, territory, dependency or country and conduct business within or without the State of California; and designate any place within or without the State of California for the holding of any shareholders' meeting or meetings, including annual meetings.
- (c) adopt, make and use a corporate seal; prescribe the forms of certificates of stock; and alter the form of the seal and certificates.

(d) authorize the issuance of shares of stock of the corporation on any lawful terms, in consideration of money paid, labor done, services actually rendered, debts or securities cancelled, or tangible or intangible property actually received.

(e) borrow money and incur indebtedness on behalf of the corporation and cause to be executed and delivered for the corporation's purposes, in the corporate name, promissory notes, bonds, debentures, deeds of trust, mortgages, pledges, hypothecations and other evidences of debt and securities.

Section 2.1 Number and Qualification of Directors. The number of directors of the corporation shall be not less than seven (7) nor more than thirteen (13). The exact number of directors shall be eight (8) until changed, within the limits specified above, by a bylaw amending this Section 2, duly adopted by the board of directors or by the shareholders. The indefinite number of directors may be changed, or a definite number fixed without provision for an indefinite number, by a duly adopted amendment to the articles of incorporation or by an amendment to this bylaw duly adopted by the vote or written consent of holders of a majority of the outstanding shares entitled to vote; subject, however, to such additional voting requirement or limitation as is imposed under applicable law in the case of an amendment reducing the number of directors to a number less than five (5).

Section 3. Independent Directors. A majority of directors of the corporation shall be Independent Directors, except for a period of 90 days after the death, removal or resignation of an Independent Director.

Section 4. Election and Term of Office of Directors. Directors shall be elected at each annual meeting of the shareholders to hold office until the next annual meeting. Each director, including a director elected to fill a vacancy, shall hold office until the expiration of the term for which elected and until a successor has been elected and qualified.

Section 5. Vacancies. Except as otherwise agreed by the corporation, vacancies in the board of directors may be filled by a majority of the remaining directors, though less than a quorum, or by a sole remaining director, except that a vacancy created by the removal of a director by the vote or written consent of the shareholders or by court order may be filled only by the vote of a majority of the shares entitled to vote represented at a duly held meeting at which a quorum is present, or by the written consent of holders of a majority of the outstanding shares entitled to vote. Each director so elected shall hold office until the next annual meeting of the shareholders and until a successor has been elected and qualified.

A vacancy or vacancies in the board of directors shall be deemed to exist in the event of the death, resignation or removal of any director, or if the board of directors by resolution declares vacant the office of a director who has been declared of unsound mind by an order of court or convicted of a felony, or if the authorized number of directors is increased, or if the shareholders fail, at any meeting of shareholders at which any director or directors are elected, to elect the number of directors to be voted for at that meeting.

The shareholders may elect a director or directors at any time to fill any vacancy or vacancies not filled by the directors, but any such election by written consent shall require the consent of a majority of the outstanding shares entitled to vote.

Any director may resign effective on giving written notice to the chairman of the board, the president, the secretary or the board of directors, unless the notice specifies a later time for that resignation to become effective. If the resignation of a director is effective at a future time, the board of directors may elect a successor to take office when the resignation becomes effective.

No reduction of the authorized number of directors shall have the effect of removing any director before that director's term of office expires.

¹ Amended May 1, 2006

Section 6. Place of Meetings and Meetings by Telephone. Regular meetings of the board of directors may be held at any place within or outside the State of California that has been designated from time to time by resolution of the board. In the absence of such a designation, regular meetings shall be held at the principal executive office of the corporation. Special meetings of the board shall be held at any place within or outside the State of California that has been designated in the notice of the meeting or, if not stated in the notice or there is no notice, at the principal executive office of the corporation. Any meeting, regular or special, may be held by conference telephone or similar communication equipment, so long as all directors participating in the meeting can hear one another, and all such directors shall be deemed to be present in person at the meeting.

Section 7. Annual Meeting. Immediately following each annual meeting of shareholders, the board of directors shall hold a regular meeting for the purpose of organization, any desired election of officers and the transaction of other business. Notice of this meeting shall not be required.

Section 8. Other Regular Meetings. Other regular meetings of the board of directors shall be held without call at such time as shall from time to time be fixed by the board of directors. Such regular meetings may be held without notice.

Section 9. Special Meetings. Special meetings of the board of directors for any purpose or purposes may be called at any time by the chairman of the board or the president or any vice president or the secretary or any two directors.

Notice of the time and place of special meetings shall be delivered personally or by telephone to each director or sent by first class mail or telegram, charges prepaid, addressed to each director at that director's address as it is shown on the records of the corporation. In case the notice is mailed, it shall be deposited in the United States mail at least four (4) days before the time of the holding of the meeting. In case the notice is delivered personally or by telephone or telegram, it shall be delivered personally or by telephone or to the telegraph company at least forty-eight (48) hours before the time of the holding of the meeting. Any oral notice given personally or by telephone may be communicated either to the director or to a person at the office of the director who the person giving the notice has reason to believe will promptly communicate it to the director. The notice need not specify the purpose of the meeting. In addition, the place of the meeting need not be specified if it is to be held at the principal executive office of the corporation.

Section 10. Quorum. A majority of the authorized number of directors shall constitute a quorum for the transaction of business, except to adjourn as provided in Section 12 of this Article IV. Every act or decision done or made by a majority of the directors present at a meeting duly held at which a quorum is present shall be regarded as the act of the board of directors, subject to the provisions of Section 310 of the Corporations Code of California (as to approval of contracts or transactions in which a director has a direct or indirect material financial interest), Section 311 of that Code (as to appointment of committees), and Section 317(e) of that Code (as to indemnification of directors). A meeting at which a quorum is initially present may continue to transact business notwithstanding the withdrawal of directors, if any action taken is approved by at least a majority of the required quorum for that meeting.

Section 11. Waiver of Notice. The transactions of any meeting of the board of directors, however called and noticed or wherever held, shall be as valid as though had at a meeting duly held after regular call and notice if a quorum is present and if, either before or after the meeting, each of the directors not present or who though present or who though present has prior to the meeting or at its commencement protested the lack of proper notice to him, signs a written waiver of notice, a consent to holding the meeting or an approval of the minutes. The waiver of notice or consent need not specify the purpose of the meeting. All such waivers, consents and approvals shall be filed with the corporate records or made a part of the minutes of the meeting.

Section 12. Adjournment. A majority of the directors present, whether or not constituting a quorum, may adjourn any meeting to another time and place.

Section 13. Notice of Adjournment. Notice of the time and place of holding an adjourned meeting need not be given unless the meeting is adjourned for more than twenty-four (24) hours, in which case notice of the time and place shall be given before the time of the adjourned meeting in the manner specified in Section 9 of this Article IV to the directors who were not present at the time of the adjournment.

Section 14. Action Without Meetings. Any action required or permitted to be taken by the board of directors may be taken without a meeting if all members of the board shall individually or collectively consent in writing to that action. Such action by written consent shall have the same force and effect as a unanimous vote of the board of directors. Such written consent or consents shall be filed with the minutes of the proceedings of the board.

Section 15. Fees and Compensation of Directors. Directors and members of committees may receive such compensation, if any, for their services and such reimbursement of expenses as may be fixed or determined by resolution of the board of directors. This Section 15 shall not be construed to preclude any director from serving the corporation in any other capacity as an officer, agent, employee or otherwise, and receiving compensation for those services.

ARTICLE V

Committees

Section 1. Committees Of Directors. The board of directors may, by resolution adopted by a majority of the authorized number of directors, designate one or more committees, each consisting of two or more directors, to serve at the pleasure of the board. The board may designate one or more directors as alternate members of any committee who may replace any absent member at any meeting of the committee. Any committee, to the extent provided in the resolution of the board, shall have all the authority of the board, except with respect to:

- (a) the approval of any action which, under the General Corporation Law of California, also requires shareholders' approval or approval of the outstanding shares;
- (b) the filling of vacancies on the board of directors or in any committee;
- (c) the fixing of compensation of the directors for serving on the board or on any committee;
- (d) the amendment or repeal of bylaws or the adoption of new bylaws;
- (e) the amendment or repeal of any resolution of the board of directors which by its express terms is not so amendable or repealable;
- (f) a distribution to the shareholders of the corporation, except at a rate or in a periodic amount or within a price range determined by the board of directors; or
- (g) the appointment of any other committees of the board of directors or the members of these committees.

Section 2. Meetings and Action of Committees. Meetings and action of committees shall be governed by, and held and taken in accordance with, the provisions of Article IV of these bylaws, Sections 6 (place of meetings), 8 (regular meetings), 9 (special meetings and notice), 10 (quorum), 11 (waiver of notice), 12 (adjournment), 13 (notice of adjournment), and 14 (action without meeting), with such changes in the context of those bylaws as are necessary to substitute the committee and its members for the board of directors and its members, except that the time of regular meetings of committees may be determined either by resolution of the board of directors or by resolution of the committee; special meetings of committees may also be called by resolution of the board of directors; and notice of special meetings of committees shall also be given to all alternate members who shall have the right to attend all meetings of the committee. The board of directors may adopt rules for the government of any committee not inconsistent with the provisions of these bylaws.

ARTICLE VI

Officers

Section 1. Officers. The officers of the corporation shall include a president, a secretary and a chief financial officer. The corporation may also have, at the discretion of the board of directors, a chairman of the board, one or more vice presidents, a treasurer, one or more assistant secretaries, one or more assistant treasurers and such other officers as may be appointed in accordance with the provisions of Section 3 of this Article VI. If there is a treasurer, he shall be the chief financial officer unless some other person is so appointed by the board of directors. Any number of offices may be held by the same person.

Section 2. Election of Officers. The officers of the corporation, except such officers as may be appointed in accordance with the provisions of Section 3 or Section 5 of this Article VI, shall be chosen by the board of directors, and each shall service at the pleasure of the board, subject to the rights, if any, of an officer under any contract of employment.

Section 3. Subordinate Officers. The board of directors may appoint, and may empower the chairman of the board or president to appoint, such other officers as the business of the corporation may require, each of whom shall hold office for such period, have such authority and perform such duties as are provided in the bylaws or as the board of directors *may* from time to time determine.

Section 4. Removal and Resignation of Officer. Subject to the rights, if any, of an officer under any contract of employment, any officer may be removed, either with or without cause, by the board of directors, at any regular or special meeting of the board or, except in case of an officer chosen by the board of directors, by an officer upon whom such power of removal may be conferred by the board of directors. Any officer may resign at any time by giving written notice to the corporation. Any resignation shall take effect at the date of the receipt of that notice or at any later time specified in that notice; and, unless otherwise specified in that notice, the acceptance of the resignation shall not be necessary to make it effective. Any resignation is without prejudice to the rights, if any, of the corporation under any contract to which the officer is a party.

Section 5. Vacancies in Offices. A vacancy in any office because of death, resignation, removal, disqualification or any other cause shall be filled in the manner prescribed in these bylaws for regular appointments to that office.

Section 6. Chairman of the Board. The chairman of the board, if such an officer be elected, shall, if present, preside at meetings of the board of directors and exercise and perform such other powers and duties as may be from time to time assigned to him by the board of directors or prescribed by the bylaws. If there is no president, the chairman of the board shall in addition be the chief executive officer of the corporation and shall have the powers and duties prescribed in Section 7 of this Article VI. The chairman of the board may be the chief executive officer of the corporation, notwithstanding that there is a president, if the board of directors so determines.

Section 7. President. Subject to such supervisory powers, if any, as may be given by the board of directors to the chairman of the board, if there be such an officer, the president shall, subject to the control of the board of directors, have general supervision, direction and control of the business and the officers of the corporation. In the absence of the chairman of the board, or if there be none, he shall preside at all meetings of the shareholders and at all meetings of the board of directors. He shall have the general powers and duties of management usually vested in the office of president of a corporation and shall have such powers and duties as may be prescribed by the board of directors or the bylaws. The president shall be the chief executive officer of the corporation unless the chairman of the board, if any, is so designated.

Section 8. Vice Presidents. In the absence or disability of the president, the vice presidents, if any, in order of their rank as fixed by the board of directors or, if not ranked, a vice president designated by the board of directors, shall perform all duties of the president, and when so acting shall have all the powers of, and be subject to all the restrictions upon, the president. The vice presidents shall have such other powers and perform such other duties as from time to time may be prescribed for them respectively by the board of directors or the bylaws and the president or the chairman of the board.

Section 9. Secretary. The secretary shall keep or cause to be kept, at the principal executive office or such other place as the board of directors may direct, a book of minutes of all meetings and actions of directors, committees of directors and shareholders, with the time and place of holding, whether regular or special and, if special, how authorized, the notice given, the names of those present at directors' meetings or committee meetings, the number of shares present or represented at shareholders' meetings and the proceedings.

The secretary shall keep, or cause to be kept, at the principal executive office or at the office of the corporation's transfer agent or registrar, as determined by resolution of the board of directors, a share register, or a duplicate share register, showing the names of shareholders and their addresses, the number and classes of shares held by each, the number and date of certificates issued for the same, and the number and date of cancellation of every certificate surrendered for cancellation.

The secretary shall give, or cause to be given, notice of all meetings of the shareholders and of the board of directors required by the bylaws or by law to be given, and he shall keep the seal of the corporation if one be adopted, in safe custody, and shall have such other powers and perform such other duties as may be prescribed by the board of directors or by the bylaws.

Section 10. Chief Financial Officer. The chief financial officer shall keep and maintain, or cause to be kept and maintained, adequate and correct books and records of accounts of the properties and business transactions of the corporation, including accounts of its assets, liabilities, receipts, disbursements, gains, losses, capital, retained earnings and shares. The books of account shall at all reasonable times be open to inspection by any director.

The chief financial officer shall deposit all moneys and other valuables in the name and to the credit of the corporation with such depositories as may be designated by the board of directors. He shall disburse the funds of the corporation as may be ordered by the board of directors, shall render to the president and directors, whenever they request it, an account of all of his transactions as chief financial officer and of the financial condition of the corporation, and shall have other powers and perform such other duties as may be prescribed by the board of directors or the bylaws.

ARTICLE VII

Indemnification

Section 1. Indemnification of Directors, Officers, Employees and Other Agents. The corporation shall indemnify each of its agents to the maximum extent permitted by the California General Corporation Law, as the same exists on the date of adoption of this Article VII or may hereafter be amended or interpreted (but in the case of any such amendment or interpretation, only to the extent that such amendment or interpretation permits the corporation to provide broader indemnification rights than were permitted prior to such amendment or interpretation), against expenses, judgments, fines, settlements and other amounts actually and reasonably incurred in connection with any proceeding arising by reason of the fact any such person is or was an agent of the corporation. For purposes of this Article, an "agent" of the corporation includes any person who is or was a director, officer, employee, or other agent of the corporation, or is or was serving at the request of the corporation as a director, officer, employee, or agent of another corporation, partnership, joint venture, trust, or other enterprise, or was a director, officer, employee or agent of a corporation which was a predecessor corporation of the corporation or of another enterprise at the request of such predecessor corporation.

Section 2. Insurance. Upon and in the event of a determination by the board of directors of this corporation to purchase such insurance, this corporation shall purchase and maintain insurance on behalf of any agent of the corporation against any liability asserted against or incurred by the agent in such capacity or arising out of the agent's status as such whether or not this corporation would have the obligation to indemnify the agent against that liability under the provisions of this Article VII.

ARTICLE VIII

Records and Reports

Section 1. Maintenance and Inspection of Share Register. The corporation shall keep at its principal executive office, or at the office of its transfer agent or registrar, if either be appointed and as determined by resolution of the board of directors, a record of its shareholders, giving the names and addresses of all shareholders, the number of shares and the class or series of shares held by each shareholder and the number of certificates, if any, representing the shares.

A shareholder or shareholders of the corporation holding at least five percent (5%) in the aggregate of the outstanding voting shares of the corporation may (i) inspect and copy the records of shareholders' names and addresses and shareholdings during usual business hours on five (5) days prior written demand on the corporation, and (ii) obtain from the transfer agent of the corporation, on written demand and on the tender of such transfer agent's usual charges for such list, a list of the shareholders' name and addresses who are entitled to vote for the election of directors and their shareholdings as of the most recent record date for which that list has been compiled or as of a date specified by the shareholder after the date of demand. This list shall be made available to any such shareholder by the transfer agent on or before the later of five (5) days after the demand is received or the date specified in the demand as the date as of which the list is to be compiled. The record of shareholders shall also be open to inspection on the written demand of any shareholder or holder of a voting trust certificate, at any time during usual business hours, for a purpose reasonably related to the holder's interests as a shareholder or as the holder of a voting trust certificate. Any inspection and copying under this Section 1 may be made in person or by an agent or attorney of the shareholder or holder of a voting trust certificate making the demand.

Section 2. Maintenance and Inspection of Bylaws. The corporation shall keep at its principal executive office, or if its principal executive office is not in the State of California, at its principal business office in this state, the original or a copy of the bylaws as amended to date, which shall be open to inspection by the shareholders at all reasonable times during office hours. If the principal executive office of the corporation is outside the State of California and the corporation has no principal business office in this state, the secretary shall, upon the written request of any shareholder, furnish to that shareholder a copy of the bylaws as amended to date.

Section 3. Maintenance and Inspection of Other Corporate Records. The accounting books and records and minutes of proceedings of the shareholders and the board of directors and any committee or committees of the board of directors shall be kept at such place or places designated by the board of directors or, in the absence of such designation, at the principal executive office of the corporation. The minutes shall be kept in written form and the accounting books and records shall be kept either in written form or in any other form capable of being converted into written form. The minutes and accounting books and records shall be open to inspection upon the written demand of any shareholder or holder of a voting trust certificate, at any reasonable time during usual business hours, for a purpose reasonably related to the holder's interests as a shareholder or as the holder of a voting trust certificate. The inspection may be made in person or by an agent or attorney and shall include the right to copy and make extracts. These rights of inspection shall extend to the records of each subsidiary corporation of the corporation.

Section 4. Inspection by Director. Every director shall have the absolute right at any reasonable time to inspect all books, records and documents of every kind and the physical properties of the corporation and each of its subsidiary corporations. This inspection by a director may be made in person or by an agent or attorney and the right of inspection includes the right to copy and make extracts of documents.

Section 5. Annual Report to Shareholders. The board of directors shall cause an annual report to be sent to the shareholders not later than one hundred twenty (120) days after the close of the fiscal year adopted by the corporation. This report shall be sent at least fifteen (15) (or if sent by third-class mail, thirty-five (35)) days before the annual meeting of shareholders to be held during the next fiscal year and in the manner specified in Section 5 of Article III of these bylaws for giving notice to shareholders of the corporation. The annual report shall contain a balance sheet as of the end of the fiscal year and an income statement and statement of changes in financial position for the fiscal year, prepared in accordance with generally accepted accounting principles applied on a consistent basis and accompanied by any report of independent accountants.

Section 6. Disclosure on Distribution. Any distribution of income or capital assets of the corporation to holders of securities of the corporation other than its promissory notes shall be accompanied by a written statement disclosing the source of the funds distributed. If, at the time of distribution, this information is not available, a written explanation of the relevant circumstances shall accompany the distribution and the written, statement disclosing the source of the funds distributed shall be sent to such holders not later than seventy-five (75) days after the close of the fiscal year in which the distribution was made.

Section 7. Financial Statements. A copy of any annual financial statement and any income statement of the corporation for each quarterly period of each fiscal year and any accompanying balance sheet of the corporation as of the end of each such period that has been prepared by the corporation shall be kept on file in the principal executive office of the corporation for twelve (12) months, and each such statement shall be exhibited at all reasonable times to any shareholder demanding an examination of any such statement or a copy shall be mailed to any such shareholder.

If a shareholder or shareholders holding at least five percent (5%) of the outstanding shares of any class of stock of the corporation makes a written request to the corporation for an income statement of the corporation for the three-month, six-month or nine-month period of the then current fiscal year ended more than thirty (30) days before the date of the request, and a balance sheet of the corporation as of the end of that period, the chief financial officer shall cause that statement to be prepared, if not already prepared, and shall deliver personally or mail that statement or statements to the person making the request within thirty (30) days after the receipt of the request. If the corporation has not sent to the shareholders its annual report for the last fiscal year, this report shall likewise be delivered or mailed to the shareholder or shareholders within thirty (30) days after the request.

The corporation shall also, on the written request of any shareholder, mail to the shareholder a copy of the last annual, semi-annual or quarterly income statement which it has prepared, and a balance sheet as of the end of that period.

The quarterly income statements and balance sheets referred to in this section shall be accompanied by the report, if any, of any independent accountants engaged by the corporation or the certificate of an authorized officer of the corporation that the financial statements were prepared without audit from the books and records of the corporation.

Section 8. Annual Statement of General Information. The corporation shall, during the period commencing on January 1st and ending on June 30th in each year, file with the Secretary of State of the State of California, on the prescribed form, a statement setting forth the authorized number of directors, the number of vacancies on the board of directors the names and complete business or residence addresses of all incumbent directors, the names and complete business or residence addresses of the chief executive officer, secretary and chief financial officer, the street address of its principal executive office or principal business office in this state, and the general type of business constituting the principal business activity of the corporation, together with a designation of the agent of the corporation for the purpose of service of process, all in compliance with Section 1502 of the Corporations Code of California.

ARTICLE IX

General Corporate Matters

Section 1. Record Date for Purposes Other than Notice and Voting. For purposes of determining the shareholders entitled to receive payment of any dividend or other distribution or allotment of any rights or entitled to exercise any rights in respect of any other lawful action (other than action by shareholders by written consent without a meeting), the board of directors may fix, in advance, a record date which shall not be more than sixty (60) days before any such action, and in that case only shareholders of record on the date so fixed are entitled to receive the dividend, distribution or allotment of rights or to exercise the rights, as the case may be, notwithstanding any transfer of any shares on the books of the corporation after the record date so fixed, except as otherwise provided in the California General Corporation law.

If the board of directors does not so fix a record date, the record date for determining shareholders for any such purpose shall be at the close of business on the day on which the board adopts the applicable resolution or the sixtieth (60th) day before the date of that action, whichever is later.

Section 2. Checks, Drafts, Evidence of Indebtedness. All checks, drafts or other orders for payment of money, notes or other evidences of indebtedness, issued in the name of or payable to the corporation, shall be signed or endorsed by such person or persons and in such manner as set from time to time shall be determined by resolution of the board of directors.

Section 3. Corporate Contracts and Instruments; How Executed. The board of directors, except as otherwise provided in these bylaws, may authorize any officer or officers, agent or agents, to enter into any contract or execute any instrument in the name of and on behalf of the corporation, and this authority may be general or confined to specific instances; and, unless so authorized or ratified by the board of directors or within the agency power of an officer, no officer, agent or employee shall have any power or authority to bind the corporation by any contract or engagement or to pledge its credit or to render it liable for any purpose or for any amount.

Section 4. Certificates for Shares. Each shareholder shall be entitled to a certificate or certificates for shares of the capital stock of the corporation signed in the name of the corporation by the chairman of the board or vice chairman of the board, or the president or vice president, and by the chief financial officer or an assistant treasurer or the secretary or any assistant secretary, certifying the number of shares and the class or series of shares owned by the shareholder. Any or all of the signatures on the certificate may be facsimile. In case any officer, transfer agent or registrar who has signed or whose facsimile signature has been placed on a certificate shall have ceased to be that officer, transfer agent or registrar before that certificate is issued, it may be issued by the corporation with the same effect as if that person were an officer, transfer agent or registrar at the date of issue.

Section 5.2 Stock Certificates and Uncertificated Stock. Shares of the corporation's stock may be certificated or uncertificated, as provided under California law. Every certificate of stock of the corporation shall be signed in the name of the corporation by the chairman of the board or vice chairman of the board, or the president or a vice president, and by the chief financial officer or an assistant treasurer or the secretary or any assistant secretary, certifying the number of shares and the class or series of shares owned by the shareholder. Any or all of the signatures on the certificate may be facsimile. In case any officer, transfer agent or registrar who has signed or whose facsimile signature has been placed on a certificate shall have ceased to be that officer, transfer agent or registrar before that certificate is issued, it may be issued by the corporation with the same effect as if that person were an officer, transfer agent or registrar at the date of issue.

Certificates for shares and uncertificated shares may be issued prior to full payment under such restrictions and for such purposes as the board of directors may provide; provided, however, that on any certificate issued to represent any partly paid shares, or, for uncertificated shares, on the initial transaction statement for such partly paid shares, the total amount of the consideration to be paid therefor and the amount paid thereon shall be stated.

Section 6.2 Lost Certificates. The board of directors may, in case any share certificate or certificate for any other security is alleged to have been lost, stolen, or destroyed, authorize the issuance of a replacement certificate or uncertificated shares in lieu thereof on such terms and conditions as the board may require, including provision for indemnification of the corporation secured by a bond or other adequate security sufficient to protect the corporation against any claim that may be made against it, including any expense or liability, on account of the alleged loss, theft or destruction of the certificate or the issuance of the replacement certificate or uncertificated shares.

Section 7. Restrictions on Transactions with Affiliates. The corporation may engage in transactions with affiliates provided that a purchase or sale transaction with an affiliate is (i) approved by a majority of the corporation's Independent Directors and (ii) fair to the corporation based on an independent appraisal or fairness opinion.

Section 8. Repurchase of Shares. The corporation may purchase or reacquire its shares and invest its assets in its own shares, provided that in each case the consent of the board of directors shall have been obtained.

Section 9. Provisions in Conflict with Law or Regulations. The provisions of these bylaws are severable, and if the directors shall determine, with the advice of counsel, that any one or more of such provisions (the "Conflicting Provisions") are in conflict with the provisions of Section 850 through 860 of the Code or with other applicable federal or California laws and regulations, the Conflicting Provisions shall be deemed never to have constituted a part of these bylaws; provided, however, that such determination by the directors shall not affect or impair any of the remaining provisions of these bylaws or render invalid or improper any action taken or omitted (including but not limited to the election of directors) prior to such determination. Such determination shall become effective when a certificate signed by a majority of the directors setting forth any such determination and reciting that it was duly adopted by the directors, shall be filed with the books and records of the corporation. The directors shall not be liable for failure to make any determination under this Section. Nothing in this Section shall in any way limit or affect the right of the directors or the shareholders to amend these bylaws.

2 Amended May 5, 2008

Section 10. Construction. Unless the context requires otherwise, the general provisions, rules of construction and definitions in the California General Corporation Law shall govern the construction of these bylaws.

Section 11. Proposal for Sale or Financing of Properties. During 1997, unless shareholders had previously approved such a proposal, the shareholders will be presented with a proposal to approve or disapprove (a) the sale or financing of all or substantially all of the corporation's properties and (b) the distribution of the proceeds from such transaction and, in the case of a sale, the liquidation of the corporation, unless the proceeds of such sale include deferred payments, in which case the corporation would be liquidated following receipt of all deferred payments; provided, however, that this provision shall not be applicable if the merger of American Office Park Properties, Inc. into the corporation is completed. This provision may not be amended or repealed without the vote or written consent of holders of a majority of the outstanding shares entitled to vote.

ARTICLE X

Investment Policy

Section 1. Statement of Investment Policy. The general investment policy of the corporation shall be to engage in any lawful activity for which a corporation may be organized under applicable law.

ARTICLE XI

Amendments

Section 1. Amendment by Shareholders. New bylaws may be adopted or these bylaws may be amended or repealed by the vote or written consent of holders of a majority of the outstanding shares entitled to vote; provided, however, that if the articles of incorporation of the corporation are amended in accordance with Section 2302 of the Corporations Code of California and if such articles of incorporation thereafter set forth the number of authorized directors of the corporation, the authorized number of directors may be changed only by an amendment of the articles of incorporation.

Section 2. Amendment by Directors. Subject to the rights of the shareholders as provided in Section 1 of this Article XI, to adopt, amend or repeal bylaws, bylaws may be adopted, amended or repealed by the board of directors; provided, however, that after the issuance of shares, the board of directors may adopt a bylaw or amendment of a bylaw changing the authorized number of directors only for the purpose of fixing the exact number of directors within the limits specified in the articles of incorporation or in Section 2 of Article IV of these bylaws, and provided further that bylaws relating to the corporation's qualification as a real estate investment trust (Section 9 of Article IX), bylaws requiring that a majority of the directors be Independent Directors (Section 3 of Article IV), bylaws relating to restrictions on transactions with affiliates (Section 7 of Article IX) and bylaws relating to restrictions on the repurchase by the corporation of its shares (Section 8 of Article IX), may not be amended or repealed without the vote or written consent of holders of a majority of the outstanding shares entitled to vote.

PS BUSINESS PARKS, INC.

EXHIBIT 12
STATEMENT RE: COMPUTATION OF RATIO OF EARNINGS TO FIXED CHARGES
(Unaudited, in thousands, except ratio data)

	Three Months Ended June 30,		Six Months Ended June 30,		
	2008	2007	2008	2007	
Net income	\$ 17,380	\$ 16,538	\$ 33,938	\$ 35,129	
Minority interests	3,391	3,046	6,491	6,675	
Interest expense	990	1,012	1,983	2,119	
Earnings from operations available to cover fixed charges	\$ 21,761	\$ 20,596	\$ 42,412	\$ 43,923	
Fixed charges	\$ 990	\$ 1,012	\$ 1,983	\$ 2,119	
Preferred stock dividends	12,757	12,757	25,513	25,425	
Preferred partnership distributions	1,752	1,752	3,504	3,351	
Combined fixed charges and preferred distributions	\$ 15,499	\$ 15,521	\$ 31,000	\$ 30,895	
Ratio of earnings from operations to fixed charges	22.0	20.4	21.4	20.7	
Ratio of earnings from operations to combined fixed charges and preferred distributions	1.4	1.3	1.4	1.4	
	2007	2006	2005	2004	2003
Income from continuing operations	\$ 68,666	\$ 62,937	\$ 59,674	\$ 46,564	\$ 46,326
Minority interests in continuing operations	13,009	16,268	16,262	24,785	29,638
Interest expense	4,130	2,575	1,330	3,054	4,015
Earnings from continuing operations available to cover fixed charges	\$ 85,805	\$ 81,780	\$ 77,266	\$ 74,403	\$ 79,979
Fixed charges	\$ 4,130	\$ 2,575	\$ 1,330	\$ 3,054	\$ 4,015
Preferred stock dividends	50,937	47,933	43,011	33,020	15,784
Preferred partnership distributions	6,854	11,155	10,651	20,245	19,240
Combined fixed charges and preferred distributions	\$ 61,921	\$ 61,663	\$ 54,992	\$ 56,319	\$ 39,039
Ratio of earnings from continuing operations to fixed charges	20.8	31.8	58.1	24.4	19.9
Ratio of earnings from continuing operations to combined fixed charges and preferred distributions	1.4	1.3	1.4	1.3	2.0

PS BUSINESS PARKS, INC.
EXHIBIT 12
STATEMENT RE: COMPUTATION OF RATIO OF EARNINGS TO FIXED CHARGES
(Unaudited, in thousands, except ratio data)

Supplemental Disclosure of Ratio of Funds from Operations (“FFO”) to Fixed Charges:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
FFO	\$ 31,382	\$ 29,991	\$ 61,979	\$ 59,584
Interest expense	990	1,012	1,983	2,119
Minority interest in income — preferred units	1,752	1,752	3,504	3,351
Preferred stock dividends	12,757	12,757	25,513	25,425
FFO available to cover fixed charges	<u>\$ 46,881</u>	<u>\$ 45,512</u>	<u>\$ 92,979</u>	<u>\$ 90,479</u>
Fixed charges	\$ 990	\$ 1,012	\$ 1,983	\$ 2,119
Preferred stock dividends	12,757	12,757	25,513	25,425
Preferred partnership distributions	1,752	1,752	3,504	3,351
Combined fixed charges and preferred distributions paid	<u>\$ 15,499</u>	<u>\$ 15,521</u>	<u>\$ 31,000</u>	<u>\$ 30,895</u>
Ratio of adjusted FFO to fixed charges	<u>47.4</u>	<u>45.0</u>	<u>46.9</u>	<u>42.7</u>
Ratio of adjusted FFO to combined fixed charges and preferred distributions paid	<u>3.0</u>	<u>2.9</u>	<u>3.0</u>	<u>2.9</u>

	2007	2006	2005	2004	2003
FFO (1)	\$ 122,405	\$ 106,235	\$ 102,463	\$ 97,214	\$ 97,448
Interest expense	4,130	2,575	1,330	3,054	4,015
Minority interest in income — preferred units	6,854	11,155	10,651	20,245	19,240
Preferred stock dividends	50,937	47,933	43,011	33,020	15,784
FFO available to cover fixed charges	<u>\$ 184,326</u>	<u>\$ 167,898</u>	<u>\$ 157,455</u>	<u>\$ 153,533</u>	<u>\$ 136,487</u>
Fixed charges	\$ 4,130	\$ 2,575	\$ 1,330	\$ 3,054	\$ 4,015
Preferred stock dividends (2)	50,937	44,553	43,011	31,154	15,784
Preferred partnership distributions (2)	6,854	9,789	10,350	17,106	19,240
Combined fixed charges and preferred distributions paid	<u>\$ 61,921</u>	<u>\$ 56,917</u>	<u>\$ 54,691</u>	<u>\$ 51,314</u>	<u>\$ 39,039</u>
Ratio of adjusted FFO to fixed charges	<u>44.6</u>	<u>65.2</u>	<u>118.4</u>	<u>50.3</u>	<u>34.0</u>
Ratio of adjusted FFO to combined fixed charges and preferred distributions paid	<u>3.0</u>	<u>2.9</u>	<u>2.9</u>	<u>3.0</u>	<u>3.5</u>

(1) FFO has been adjusted to include the effect of impairment charges.

(2) Excludes EITF Topic D-42 distributions.

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Joseph D. Russell, Jr., certify that:

1. I have reviewed this quarterly report on Form 10-Q of PS Business Parks, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Joseph D. Russell, Jr.

Name: Joseph D. Russell, Jr.

Title: Chief Executive Officer

Date: August 6, 2008

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Edward A. Stokx, certify that:

1. I have reviewed this quarterly report on Form 10-Q of PS Business Parks, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Edward A. Stokx

Name: Edward A. Stokx

Title: Chief Financial Officer

Date: August 6, 2008

**Certification of CEO and CFO Pursuant to
18 U.S.C. Section 1350,
as Adopted Pursuant to
Section 906 of the Sarbanes-Oxley Act of 2002**

In connection with the Quarterly Report on Form 10-Q of PS Business Parks, Inc. (the "Company") for the period ending June 30, 2008 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), Joseph D. Russell Jr., as Chief Executive Officer of the Company, and Edward A. Stokx, as Chief Financial Officer of the Company, each hereby certifies, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that, to his knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Joseph D. Russell, Jr.
Name: Joseph D. Russell, Jr.
Title: Chief Executive Officer
Date: August 6, 2008

/s/ Edward A. Stokx
Name: Edward A. Stokx
Title: Chief Financial Officer
Date: August 6, 2008