WASHINGTON REAL ESTATE INVESTMENT TRUST
Form 10-Q
November 04, 2015

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

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For quarterly period ended September 30, 2015
OR
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.
COMMISSION FILE NO. 1-6622
WASHINGTON REAL ESTATE
INVESTMENT TRUST
(Exact name of registrant as specified in its charter)

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

1775 EYE STREET, NW, SUITE 1000, WASHINGTON, DC 20006
(Address of principal executive office) (Zip code)
Registrant's telephone number, including area code: (202) 774-3200

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

Title of Each Class	Name of exchange on which registered
Shares of Beneficial Interest	New York Stock Exchange

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

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

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

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

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

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

As of October 29, 2015, 68,178,215 common shares were outstanding.

WASHINGTON REAL ESTATE INVESTMENT TRUST
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PART I
FINANCIAL INFORMATION

ITEM 1: FINANCIAL STATEMENTS

The information furnished in the accompanying unaudited Consolidated Balance Sheets, Condensed Consolidated Statements of Income, Condensed Consolidated Statements of Comprehensive Income, Consolidated Statement of Shareholders' Equity and Consolidated Statements of Cash Flows reflects all adjustments, consisting of normal recurring items, which are, in the opinion of management, necessary for a fair presentation of the financial position, results of operations and cash flows for the interim periods. The accompanying financial statements and notes thereto should be read in conjunction with the financial statements and notes for the three years ended December 31, 2014 included in Washington Real Estate Investment Trust’s 2014 Annual Report on Form 10-K.

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

	September 30, 2015 (Unaudited)	December 31, 2014
Assets		
Land	$572,880	$543,546
Income producing property	2,074,425	1,927,407
	2,647,305	2,470,953
Accumulated depreciation and amortization	(677,480)	(640,434)
Net income producing property	1,969,825	1,830,519
Properties under development or held for future development	35,256	76,235
Total real estate held for investment, net	2,005,081	1,906,754
Investment in real estate sold or held for sale, net	5,010	—
Cash and cash equivalents	21,012	15,827
Restricted cash	12,544	10,299
Rents and other receivables, net of allowance for doubtful accounts of $2,945 and $3,392, respectively	62,306	59,745
Prepaid expenses and other assets	122,629	121,082
Other assets related to properties sold or held for sale	278	—
Total assets	$2,228,860	$2,113,707
Liabilities		
Notes payable	$747,540	$747,208
Mortgage notes payable	419,293	418,525
Lines of credit	195,000	50,000
Accounts payable and other liabilities	54,131	54,318
Advance rents	10,766	12,528
Tenant security deposits	9,225	8,899
Liabilities related to properties sold or held for sale	329	—
Total liabilities	1,436,284	1,291,478
Equity		
Shareholders' equity		
Preferred shares; $0.01 par value; 10,000 shares authorized; no shares issued or outstanding	—	—
Shares of beneficial interest; $0.01 par value; 100,000 shares authorized: 68,180 and 67,819 shares issued and outstanding at September 30, 2015 and December 31, 2014, respectively	682	678
Additional paid in capital	1,192,202	1,184,395
Distributions in excess of net income	(399,421)	(365,518)
Accumulated other comprehensive loss	(2,288)	—
Total shareholders' equity	791,175	819,555
Noncontrolling interests in subsidiaries	1,401	2,674
Total equity	792,576	822,229
Total liabilities and equity	$2,228,860	$2,113,707

See accompanying notes to the consolidated financial statements.

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Revenue				
Real estate rental revenue	$78,243	$73,413	$227,325	$214,278
Expenses				
Real estate expenses	28,109	25,914	84,546	77,784
Depreciation and amortization	29,349	24,354	80,127	71,508
Acquisition costs	929	69	1,937	5,047
General and administrative	4,953	4,523	15,339	13,780
Real estate impairment	—	—	5,909	—
	63,340	54,860	187,858	168,119
Other operating income				
Gain on sale of real estate	—	—	31,731	570
Real estate operating income	14,903	18,553	71,198	46,729
Other income (expense)				
Interest expense	(14,486)	(15,087)	(44,534)	(44,602)
Loss on extinguishment of debt	—	—	(119)	—
Other income	163	192	547	634
	(14,323)	(14,895)	(44,106)	(43,968)
Income from continuing operations	580	3,658	27,092	2,761
Discontinued operations:				
Income from operations of properties sold or held for sale	—	—	—	546
Gain on sale of real estate	—	—	—	105,985
Net income	580	3,658	27,092	109,292
Less: Net loss attributable to noncontrolling interests in subsidiaries	67	10	515	17
Net income attributable to the controlling interests	$647	$3,668	$27,607	$109,309
Basic net income per share:				
Continuing operations	$0.01	$0.05	$0.40	$0.04
Discontinued operations	—	—	—	1.59
Net income per share	$0.01	$0.05	$0.40	$1.63
Diluted net income per share:				
Continuing operations	$0.01	$0.05	$0.40	$0.04
Discontinued operations	—	—	—	1.59
Net income per share	$0.01	$0.05	$0.40	$1.63
Weighted average shares outstanding – basic	68,186	66,738	68,168	66,725
Weighted average shares outstanding – diluted	68,305	66,790	68,290	66,760
Dividends declared per share	$0.30	$0.30	$0.90	$0.90

See accompanying notes to the consolidated financial statements.

WASHINGTON REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(IN THOUSANDS)
(UNAUDITED)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Net income	$580	$3,658	$27,092	$109,292
Other comprehensive loss:				
Unrealized loss on interest rate hedge	(2,288)	—	(2,288)	—
Comprehensive (loss) income	(1,708)	3,658	24,804	109,292
Less: Net loss attributable to noncontrolling interests	67	10	515	17
Comprehensive (loss) income attributable to the controlling interests	$(1,641)	$3,668	$25,319	$109,309

See accompanying notes to the financial statements.

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

	Shares Outstanding	Shares of Beneficial Interest at Par Value	Additional Paid in Capital	Distributions in Excess of Net Income Attributable to the Controlling Interests	Accumulated Other Comprehensive Loss	Total Shareholders' Equity	Noncontrolling Interests in Subsidiaries	Total Equity
Balance, December 31, 2014	67,819	$ 678	$ 1,184,395	$ (365,518)	$ —	$ 819,555	$ 2,674	$ 822,229
Net income attributable to the controlling interests	—	—	—	27,607	—	27,607	—	27,607
Net loss attributable to the noncontrolling interests and deconsolidation of noncontrolling interest	—	—	—	—	—	—	(1,278)	(1,278)
Unrealized loss on interest rate hedge					(2,288)	(2,288)		(2,288)
Contributions from noncontrolling interests	—	—	—	—	—	—	5	5
Dividends	—	—	—	(61,510)	—	(61,510)	—	(61,510)
Equity offerings, net of issuance costs	184	2	5,077	—	—	5,079	—	5,079
Share grants, net of share grant amortization and forfeitures	177	2	2,730	—	—	2,732	—	2,732
Balance, September 30, 2015	68,180	$ 682	$ 1,192,202	$ (399,421)	$ (2,288)	$ 791,175	$ 1,401	$ 792,576

See accompanying notes to the consolidated financial statements.

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

	Nine Months Ended September 30,	
	2015	2014
Cash flows from operating activities		
Net income	$27,092	$109,292
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	80,127	71,508
Provision for losses on accounts receivable	1,337	1,335
Real estate impairment	5,909	—
Gain on sale of real estate	(31,731)	(106,555)
Amortization of share grants, net	3,962	3,835
Amortization of debt premiums, discounts and related financing costs	2,661	2,730
Loss on extinguishment of debt	119	—
Changes in operating other assets	(9,733)	(16,255)
Changes in operating other liabilities	(3,531)	(3,013)
Net cash provided by operating activities	76,212	62,877
Cash flows from investing activities		
Real estate acquisitions, net	(151,682)	(154,126)
Net cash received for sale of real estate	53,566	190,864
Capital improvements to real estate	(23,085)	(41,945)
Development in progress	(29,136)	(28,363)
Real estate deposits, net	—	(2,500)
Cash held in replacement reserve escrows	(2,897)	(550)
Non-real estate capital improvements	(2,116)	(44)
Net cash used in investing activities	(155,350)	(36,664)
Cash flows from financing activities		
Line of credit borrowings, net	145,000	5,000
Dividends paid	(61,510)	(60,153)
Principal payments – mortgage notes payable	(3,358)	(2,860)
Borrowings under construction loan	4,017	14,137
Notes payable repayments	(150,000)	(100,000)
Proceeds from term loan	150,000	—
Payment of financing costs	(4,910)	(660)
Contributions from noncontrolling interests	5	5
Distributions to noncontrolling interests	—	(3,454)
Net proceeds from equity offering	5,079	—
Net cash provided by (used in) financing activities	84,323	(147,985)
Net increase (decrease) in cash and cash equivalents	5,185	(121,772)
Cash and cash equivalents at beginning of period	15,827	130,343
Cash and cash equivalents at end of period	$21,012	$8,571
Supplemental disclosure of cash flow information:		
Cash paid for interest, net of amounts capitalized	$38,023	$36,770
Decrease in accrued capital improvements and development costs	656	10,860
Mortgage notes payable assumed in connection with the acquisition of real estate	—	100,861

See accompanying notes to the consolidated financial statements.

WASHINGTON REAL ESTATE INVESTMENT TRUST AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2015
(UNAUDITED)

NOTE 1: NATURE OF BUSINESS

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

Federal Income Taxes

We believe that we qualify as a real estate investment trust ("REIT") under Sections 856-860 of the Internal Revenue Code and intend to continue to qualify as such. To maintain our status as a REIT, we are, among other things, required to distribute 90% of our REIT taxable income (which is, generally, our ordinary taxable income, with certain modifications), excluding any net taxable gains and any deductions for dividends to our shareholders on an annual basis. When selling a property, we generally have the option of (a) reinvesting the sales proceeds of the property sold, in a way that allows us to defer recognition of some or all capital gain realized on the sale, (b) distributing gains to the shareholders with no tax to us or (c) treating net long-term capital gains as having been distributed to the shareholders, paying the tax on the gain deemed distributed and allocating the tax paid as a credit to the shareholders.

Generally, and subject to our ongoing qualification as a REIT, no provisions for income taxes are necessary except for taxes on undistributed taxable income and taxes on the income generated by our taxable REIT subsidiaries ("TRSs"). Our TRSs are subject to corporate federal and state income tax on their taxable income at regular statutory rates, or as calculated under the alternative minimum tax, as appropriate. As of September 30, 2015 and December 31, 2014, our TRSs had no net deferred tax assets and a net deferred tax liability of $0.7 million and $0.6 million, respectively. This deferred tax liability is primarily related to temporary differences in the timing of the recognition of revenue, amortization and depreciation.

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

Significant Accounting Policies

We have prepared our consolidated financial statements using the accounting policies described in our Annual Report on Form 10-K for the year ended December 31, 2014.

New Accounting Pronouncements

In April 2015, the FASB issued ASU No. 2015-03, Interest - Imputation of Interest, which requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by the new standard. The new standard is effective for public entities for fiscal years beginning after December 15, 2015 and for interim periods therein. Early adoption is permitted for financial statements that have not been previously issued. We do not expect this ASU to have a material impact on our consolidated financial statements.

In June 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers, which creates a single source of revenue guidance. The new standard provides accounting guidance for all revenue arising from contracts with customers and affects all entities that enter into contracts to provide goods or services to their customers (unless the contracts are in the scope of other U.S. generally accepted accounting principles ("GAAP") requirements, such as the leasing literature). The guidance also provides a model for the measurement and recognition of gains and losses on the sale of certain nonfinancial assets, such as property and equipment, including real estate. The new standard is effective for public entities for fiscal years beginning after December 15, 2017 and for interim periods therein. Early adoption is permitted for public entities beginning after December 15, 2016. We are currently evaluating the impact the new standard may have on Washington REIT.

Principles of Consolidation and Basis of Presentation

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

We have prepared the accompanying unaudited financial statements pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and note disclosures normally included in annual financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to those rules and regulations, although we believe that the disclosures made are adequate to make the information presented not misleading. In addition, in the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of the results for the periods presented have been included. These unaudited financial statements should be read in conjunction with the financial statements and notes included in our Annual Report on Form 10-K for the year ended December 31, 2014.

Within these notes to the financial statements, we refer to the three months ended September 30, 2015 and September 30, 2014 as the "2015 Quarter" and the "2014 Quarter," respectively, and the nine months ended September 30, 2015 and September 30, 2014 as the "2015 Period" and the "2014 Period," respectively.

Use of Estimates in the Financial Statements

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

Derivatives

We borrow funds at a combination of fixed and variable rates. Borrowings under the our revolving credit facility and term loans bear interest at variable rates. Our interest rate risk management objectives are to minimize interest rate fluctuation on long-term indebtedness and limit the impact of interest rate changes on earnings and cash flows. To achieve these objectives, from time to time, we may enter into interest rate hedge contracts such as collars, swaps, caps and treasury lock agreements in order to mitigate our interest rate risk with respect to various debt instruments. We generally do not hold or issue these derivative contracts for trading or speculative purposes. The interest rate swaps we enter into are recorded at fair value on a recurring basis. We assess effectiveness of our cash flow hedges both at inception and on an ongoing basis. The effective portion of changes in fair value of the interest rate swaps associated with our cash flow hedges is recorded in accumulated other comprehensive loss. Our cash flow hedges become ineffective if critical terms of the hedging instrument and the debt instrument such as notional amounts, settlement dates, reset dates, calculation period and LIBOR do not perfectly match. In addition, we evaluate the default risk of the counterparty by monitoring the creditworthiness of the counterparty. When ineffectiveness of a cash flow hedge exists, the ineffective portion of changes in fair value of the interest rate swaps associated with our cash flow hedges is recognized in earnings in the period affected. Hedge ineffectiveness did not impact earnings in the 2015 and 2014 Periods.

NOTE 3: REAL ESTATE

Acquisition

Our current strategy is focused on properties inside the Washington metro region's Beltway, near major transportation nodes and in areas with strong employment drivers and superior growth demographics as compared to other areas. We seek to upgrade our portfolio with acquisitions as opportunities arise. Properties and land for development acquired during the 2015 Period were as follows:

Acquisition Date	Property	Type	# of units (unaudited)	Contract Purchase Price (In thousands)
July 1, 2015	The Wellington	Multifamily	711	$167,000

The Wellington, which we acquired during the 2015 Quarter, consists of an apartment building and an adjacent parcel of land for potential future multifamily development. The purchase of the Wellington was structured as a reverse exchange under Section

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1031 of the Internal Revenue Code in a manner such that legal title is held by a Qualified Intermediary until certain identified properties are sold and the reverse exchange transaction is completed. We retain essentially all of the legal and economic benefits and obligations related to the Wellington. As such, the Wellington is considered to be a VIE until legal title is transferred to us upon completion of the 1031 exchange, which is expected during the fourth quarter. We have consolidated the assets and liabilities of the Wellington as we have determined that Washington REIT is the primary beneficiary of the VIE. The results of operations from the acquired operating property are included in the consolidated statements of income as of the acquisition date.

The revenue and earnings of the acquisition during the year of acquisition are as follows (in thousands):

	Three and Nine Months Ended September 30, 2015
Real estate rental revenue	$3,441
Net loss	(1,463)

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

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

Land	$30,548
Land for development	15,000
Buildings	116,563
Leasing commissions/absorption costs	4,889
Total	$167,000

The weighted remaining average life for leasing commissions/absorption costs is two months.

The difference in the total contract price of $167.0 million for the acquisition and the acquisition cost per the consolidated statements of cash flows of $166.7 million is primarily due to credits received at settlement totaling $0.3 million.

The following unaudited pro-forma combined condensed statements of operations set forth the consolidated results of operations for the 2015 and 2014 Quarters and Periods as if the above-described acquisition in 2015 had occurred on January 1, 2014. The pro forma adjustments include reclassifying costs related to the above-described acquisition to 2014. The unaudited pro-forma information does not purport to be indicative of the results that actually would have occurred if the acquisitions had been in effect for the 2015 and 2014 Quarters and Periods. The unaudited data presented is in thousands, except per share data.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Real estate rental revenue	$78,243	$76,853	$234,095	$224,488
Income (loss) from continuing operations	1,626	2,205	29,811	(323)
Net income	1,626	2,205	29,811	106,208
Diluted net income per share	0.02	0.03	0.43	1.59

Redevelopment

In the office segment, we had a redevelopment project to renovate Silverline Center, an office property in Tysons, Virginia. As of September 30, 2015, we had invested $35.8 million in the renovation. We completed major construction activities on this project during the second quarter of 2015, and placed into service substantially completed portions of the project totaling $25.8 million. The remaining components of the redevelopment project will be placed into service the earlier of when they are substantially completed and available for occupancy or one year from completion of major construction activities.

Variable Interest Entities

In November 2011, we executed a joint venture operating agreement with a real estate development company to develop a high-rise multifamily property at 1225 First Street in Alexandria, Virginia. Washington REIT and the real estate development company owned 95% and 5% of the joint venture, respectively. During the second quarter of 2015, we determined that we would not develop the property and began negotiations to sell our interest in the joint venture. We recognized a $5.9 million impairment charge for the second quarter of 2015 in order to reduce the carrying value of the property to its estimated fair value. We based this fair value on the contact sale price in the purchase and sale agreement. This fair valuation falls into Level 2 of the fair value hierarchy. During the 2015 Quarter, we sold our 95% interest in the joint venture for a contract sale price of $14.5 million, as this joint venture has previously been consolidated as Washington REIT was the primary beneficiary of the VIE.

In June 2011, we executed a joint venture operating agreement with a real estate development company to develop The Maxwell, a mid-rise multifamily property at 650 North Glebe Road in Arlington, Virginia. Major construction activities at The Maxwell ended during December 2014, and the building became available for occupancy during the first quarter of 2015. Washington REIT is the 90% owner of the joint venture. The real estate development company owns 10% of the joint venture and was responsible for the development and construction of the property.

We have determined that The Maxwell joint venture is a VIE primarily based on the fact that the equity investment at risk is not sufficient to permit the entity to finance its activities without additional financial support. As of September 30, 2015, $31.7 million was outstanding on The Maxwell's construction loan. We have also determined that Washington REIT is the primary beneficiary of the VIE due to the fact that Washington REIT is providing 90% of the equity contributions.

We include joint venture land acquisitions and capitalized development on our consolidated balance sheets in properties under development or held for future development until placed in service or sold. As of December 31, 2014, the land and capitalized development costs for 1225 First Street totaled $20.8 million.

As of September 30, 2015 and December 31, 2014, The Maxwell's assets were as follows (in thousands):

	September 30, 2015	December 31, 2014
Land	$12,851	$12,851
Income producing property	37,914	18,432
Accumulated depreciation and amortization	(1,767)	—
Properties under development or held for future development	—	17,947
Other assets	765	—
	$49,763	$49,230

As of September 30, 2015 and December 31, 2014, The Maxwell's liabilities were as follows (in thousands):

	September 30, 2015	December 31, 2014
Mortgage notes payable	$31,707	$27,690
Accounts payable and other liabilities	669	2,196
Tenant security deposits	66	17
	$32,442	$29,903

Sold and Held for Sale Properties and Discontinued Operations

We dispose of assets that no longer meet our long-term strategy or return objectives and where market conditions for sale are favorable. The proceeds from the sales may be reinvested into other properties, used to fund development operations or to support other corporate needs, or distributed to our shareholders.

During the second quarter of 2015, 15,000 square feet of land at Montrose Shopping Center, a retail property in Rockville, Maryland, was condemned as part of an eminent domain taking action. The taken land was at the periphery of the property and its taking did not impact the property's operations. We received $2.0 million as compensation for the taken land, and recognized a $1.5 million gain on sale of real estate during the second quarter of 2015.

During the 2015 Quarter, we executed a purchase and sale agreement for the sale of Munson Hill Towers, a 279-unit multifamily property in Falls Church, Virginia, for a contract sale price of $57.1 million. We closed on the sale in October 2015 (see note 11). The property met the criteria for classification as held for sale as of September 30, 2015.

Subsequent to the end of the 2015 Period, we executed a purchase and sale agreement for the sale of Montgomery Village Center, a 197,000 square foot retail property in Gaithersburg, Maryland, for a contract sale price of $27.8 million. We expect to close on the sale before the end of 2015. The property did not meet the criteria for classification as held for sale until after the 2015 Period and is included on our consolidated balance sheets as follows:

	September 30, 2015	December 31, 2014
Land	$11,625	$11,625
Income producing property	12,606	12,443
Accumulated depreciation and amortization	(6,081)	(5,832)
Other assets	1,562	1,585
Total assets	$19,712	$19,821

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

The results of the assets in our former medical office segment sold in January 2014 are summarized as follows (amounts in thousands, except per share data):

	Nine Months Ended September 30,	
	2015	2014
Real estate rental revenue	$—	$892
Net income	—	546
Basic net income per share	—	0.01
Diluted net income per share	—	0.01

We sold or classified as held for sale the following properties in 2015 and 2014:

Disposition Date	Property Name	Segment	# of units	Rentable Square Feet	Contract Sales Price (in thousands)	Gain on Sale (in thousands)
March 20, 2015	Country Club Towers (1)	Multifamily	227	N/A	$ 37,800	$ 30,277
September 9, 2015	1225 First Street (1), (2)	Multifamily	N/A	N/A	14,500	—
N/A	Munson Hill Towers (1)	Multifamily	279	N/A	57,100	N/A
		Total 2015			$ 109,400	$ 30,277
January 21, 2014	Medical Office Portfolio Transactions III & IV (3)	Medical Office	N/A	427,000	$ 193,561	$ 105,985
May 2, 2014	5740 Columbia Road (1)	Retail	N/A	3,000	1,600	570
		Total 2014		430,000	$ 195,161	$ 106,555

(1) These properties are classified as continuing operations.
(2) Land held for future development.
(3) Woodburn Medical Park I and II and Prosperity Medical Center I, II and III, which are classified as discontinued operations.

As of September 30, 2015 and December 31, 2014, investment in real estate held for sale was as follows (in thousands):

	September 30, 2015
Land	$322
Income producing property	19,321
Accumulated depreciation and amortization	(14,633)
Total real estate held for investment, net	$5,010

Income from operations of properties classified as discontinued operations for the three and nine months ended September 30, 2015 and 2014 was as follows (in thousands):

	Three Months Ended September 30, 2015	Three Months Ended September 30, 2014	Nine Months Ended September 30, 2015	Nine Months Ended September 30, 2014
Real estate rental revenue	$—	$—	$—	$892
Real estate expenses	—	—	—	(346)
Income from operations classified as discontinued operations	$—	$—	$—	$546

NOTE 4: UNSECURED LINES OF CREDIT PAYABLE

On June 23, 2015, we terminated our $100.0 million unsecured line of credit maturing in June 2015 ("Prior Credit Facility No. 1") and our $400.0 million unsecured line of credit maturing in July 2016 ("Prior Credit Facility No. 2"), and executed a new $600.0 million unsecured credit agreement ("New Credit Facility") that matures in June 2019, unless extended pursuant to one or both of the two six-month extension options. The New Credit Facility has an accordion feature, which we utilized a portion of in September 2015, as described below, that allows us to increase the facility to $1.0 billion, subject to the extent the lenders agree to provide additional revolving loan commitments or term loans. The New Credit Facility bears interest at a rate of either LIBOR plus a margin ranging from 0.875% to 1.55% or the base rate plus a margin ranging from 0.0% to 0.55% (in each case depending upon Washington REIT’s credit rating). The base rate is the highest of the administrative agent's prime rate, the federal funds rate plus 0.50% and the LIBOR market index rate plus 1.0%. In addition, the New Credit Facility requires the payment of a facility fee ranging from 0.125% to 0.30% (depending on Washington REIT’s credit rating) on the $600.0 million committed capacity, without regard to usage. As of September 30, 2015, the interest rate on the facility is LIBOR plus 1.00% and the facility fee is 0.20%.

The amount of the New Credit Facility's unsecured line of credit unused and available at September 30, 2015 is as follows (in thousands):

Committed capacity	$600,000
Borrowings outstanding	(195,000)
Letters of credit issued [1]	(15,474)
Unused and available	$389,526

[1] The letter of credit is provided to the lender for John Marshall II relating to tenant improvements.

We executed borrowings and repayments on the unsecured lines of credit during the 2015 Period as follows (in thousands):

	Prior Credit Facility No. 1	Prior Credit Facility No. 2	New Credit Facility
Balance at December 31, 2014	$5,000	$45,000	$—
Borrowings	3,000	150,000	365,000
Repayments	(8,000)	(195,000)	(170,000)
Balance at September 30, 2015	$—	$—	$195,000

NOTE 5: NOTES PAYABLE

We repaid the remaining $150.0 million of our 5.35% unsecured notes on their maturity date of May 1, 2015 using borrowings on Prior Credit Facility No. 2.

On September 15, 2015, we entered into a $150.0 million unsecured term loan by executing a portion of the accordion feature under the New Credit Facility. The term loan has a 5.5 year maturity and an interest rate of LIBOR plus 110 basis points, based on our current unsecured debt ratings.

NOTE 6: DERIVATIVE INSTRUMENTS

On September 15, 2015, we entered into two interest rate swap arrangements with a total notional amount of $150.0 million to swap the floating interest rate under our term loan (see note 5) to an all-in fixed interest rate of 2.7% starting on October 15, 2015 and extending until the maturity of the term loan on March 15, 2021. The interest rate swaps qualify as cash flow hedges and are recorded at fair value in accordance with GAAP, based on discounted cash flow methodologies and observable inputs. We record the effective portion of changes in fair value of the cash flow hedge in other comprehensive loss. The resulting unrealized loss on the effective portions of the cash flow hedges was the only activity in other comprehensive loss during the periods presented in our consolidated financial statements. We assess the effectiveness of our cash flow hedges both at inception and on an ongoing basis. The cash flow hedges were effective for the 2015 Quarter. We had no derivative instruments outstanding as of December 31, 2014.

The fair value and balance sheet locations of the interest rate swap as of September 30, 2015 and December 31, 2014, are as follows (in thousands):

	September 30, 2015	December 31, 2014
Accounts payable and other liabilities	$2,288	$—

The interest rate swaps have been effective since inception. The gain or loss on the effective swap is recognized in other comprehensive loss, as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Unrealized loss on interest rate hedge	$(2,288)	$—	$(2,288)	$—

Amounts reported in accumulated other comprehensive loss related to derivatives will be reclassified to interest expense as interest payments are made on our variable-rate debt. During the next twelve months, we estimate that an additional $1.8 million will be reclassified as an increase to interest expense.

We have agreements with each of our derivative counterparties that contain a provision whereby we could be declared in default on our derivative obligations if repayment of the underlying indebtedness is accelerated by the lender due to our default on the indebtedness. As of September 30, 2015, the fair value of derivatives is in a net liability position of $2.3 million, which includes accrued interest but excludes any adjustment for nonperformance risk. As of September 30, 2015, we have not posted any collateral related to these agreements. If we had breached any of these provisions at September 30, 2015, we could have been required to settle our obligations under the agreements at their termination value of $2.3 million.

Derivative instruments expose us to credit risk in the event of non-performance by the counterparty under the terms of the interest rate hedge agreement. We believe that we minimize our credit risk on these transactions by dealing with major, creditworthy financial institutions. We monitor the credit ratings of counterparties and our exposure to any single entity, thus minimizing our credit risk concentration.

NOTE 7: STOCK BASED COMPENSATION

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

Total Compensation Expense

Total compensation expense recognized in the consolidated financial statements for all outstanding share based awards was $0.9 million and $1.3 million for the 2015 and 2014 Quarters, respectively, and $4.0 million and $3.8 million for the 2015 and 2014 Periods, respectively.

Restricted Share Awards

The total fair values of restricted share awards vested was $2.6 million and $1.0 million for the 2015 and 2014 Periods, respectively.

The total unvested restricted share awards at September 30, 2015 was 209,560 shares, which had a weighted average grant date fair value of $27.31 per share. As of September 30, 2015, the total compensation cost related to unvested restricted share awards was $2.4 million, which we expect to recognize over a weighted average period of 20 months.

NOTE 8: FAIR VALUE DISCLOSURES

Assets and Liabilities Measured at Fair Value

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

Level 1: Quoted prices in active markets for identical assets
Level 2: Significant other observable inputs
Level 3: Significant unobservable inputs

The only assets or liabilities we had at September 30, 2015 and December 31, 2014 that are recorded at fair value on a recurring basis are the interest rate swaps (see note 6) and the assets held in the Supplemental Executive Retirement Plan ("SERP"), which primarily consists of investments in mutual funds. We base the valuations related to the SERP on assumptions derived from significant other observable inputs and accordingly these valuations fall into Level 2 in the fair value hierarchy.

The valuation of the derivatives is determined using widely accepted valuation techniques, including discounted cash flow analysis on the expected cash flows of each derivative. This analysis reflects the contractual terms of the derivatives, including the period to maturity, and uses observable market-based inputs, including interest rate curves and implied volatilities. The fair values of interest rate swaps are determined using the market standard methodology of netting the discounted future fixed cash payments (or receipts) and the discounted expected variable cash receipts (or payments). The variable cash payments (or receipts) are based on an expectation of future interest rates (forward curves) derived from observable market interest rate curves. To comply with the provisions of ASC 820, we incorporate credit valuation adjustments in the fair value measurements to appropriately reflect both our own nonperformance risk and the respective counterparty’s nonperformance risk. These credit valuation adjustments were concluded to be not significant inputs for the fair value calculations for the periods presented. In adjusting the fair value of our derivative contracts for the effect of nonperformance risk, we have considered the impact of netting and any applicable credit enhancements, such as the posting of collateral, thresholds, mutual puts and guarantees. The valuation of our derivatives fall into Level 2 in the fair value hierarchy.

The fair values of these assets and liabilities at September 30, 2015 and December 31, 2014 were as follows (in thousands):

	September 30, 2015				December 31, 2014			
	Fair Value	Level 1	Level 2	Level 3	Fair Value	Level 1	Level 2	Level 3
Assets:								
SERP	$1,296	$—	$1,296	$—	$2,778	$—	$2,778	$—
Liabilities:								
Derivatives	$2,288	$—	$2,288	$—	$—	$—	$—	$—

Financial Assets and Liabilities Not Measured at Fair Value

The following disclosures of estimated fair value were determined by management using available market information and established valuation methodologies, including discounted cash flow. Many of these estimates involve significant judgment. The estimated fair value disclosed may not necessarily be indicative of the amounts we could realize on disposition of the financial instruments. The use of different market assumptions or estimation methodologies could have an effect on the estimated fair value amounts. In addition, fair value estimates are made at a point in time and thus, estimates of fair value subsequent to September 30, 2015 may differ significantly from the amounts presented.

Following is a summary of significant methodologies used in estimating fair values and a schedule of fair values at September 30, 2015 and December 31, 2014.

Cash and Cash Equivalents and Restricted Cash

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

Notes Receivable

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

Debt

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

As of September 30, 2015 and December 31, 2014, the carrying values and estimated fair values of our financial instruments were as follows (in thousands):

	September 30, 2015		December 31, 2014	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Cash and cash equivalents	$21,012	$21,012	$15,827	$15,827
Restricted cash	12,544	12,544	10,299	10,299
2445 M Street note	4,940	5,160	4,404	5,113
Mortgage notes payable	419,293	434,581	418,525	433,762
Lines of credit	195,000	195,000	50,000	50,000
Notes payable	747,540	781,641	747,208	782,042

NOTE 9: EARNINGS PER COMMON SHARE

We determine “Basic earnings per share” using the two-class method as our unvested restricted share awards and units have non-forfeitable rights to dividends and are therefore considered participating securities. We compute basic earnings per share by dividing net income attributable to the controlling interest less the allocation of undistributed earnings to unvested restricted share awards and units by the weighted-average number of common shares outstanding for the period.

We determine “Diluted earnings per share” as the more dilutive of the two-class method or the treasury stock method with respect to the unvested restricted share awards. We further evaluate any other potentially dilutive securities at the end of the period and adjust the basic earnings per share calculation for the impact of those securities that are dilutive. Our diluted earnings per share calculation includes the dilutive impact of employee stock options (prior to their expiration at December 31, 2014) based on the treasury stock method and our share based awards with performance conditions prior to the grant date and all market condition awards under the contingently issuable method.

The computations of basic and diluted earnings per share for the three and nine months ended September 30, 2015 and 2014 were as follows (in thousands, except per share data):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Numerator:				
Income from continuing operations	$580	$3,658	$27,092	$2,761
Net loss attributable to noncontrolling interests	67	10	515	17
Allocation of earnings to unvested restricted share awards	(47)	(44)	(184)	11
Adjusted income from continuing operations attributable to the controlling interests	600	3,624	27,423	2,789
Income from discontinued operations, including gain on sale of real estate, net of taxes	—	—	—	106,531
Allocation of earnings to unvested restricted share awards	—	—	—	(335)
Adjusted income from discontinuing operations attributable to the controlling interests	—	—	—	106,196
Adjusted net income attributable to the controlling interests	$600	$3,624	$27,423	$108,985
Denominator:				
Weighted average shares outstanding – basic	68,186	66,738	68,168	66,725
Effect of dilutive securities:				
Employee restricted share awards	119	52	122	35
Weighted average shares outstanding – diluted	68,305	66,790	68,290	66,760
Net income per common share, basic:				
Continuing operations	$0.01	$0.05	$0.40	$0.04
Discontinued operations	—	—	—	1.59
	$0.01	$0.05	$0.40	$1.63
Net income per common share, diluted:				
Continuing operations	$0.01	$0.05	$0.40	$0.04
Discontinued operations	—	—	—	1.59
	$0.01	$0.05	$0.40	$1.63

NOTE 10: SEGMENT INFORMATION

We have three reportable segments: office, retail and multifamily. Office buildings provide office space for various types of businesses and professions. Retail shopping centers are typically grocery store-anchored neighborhood centers that include other small shop tenants or regional power centers with several junior box tenants. Multifamily properties provide rental housing for individuals and families throughout the Washington metropolitan area.

We evaluate performance based upon operating income from the combined properties in each segment. Our reportable operating segments are consolidations of similar properties. GAAP requires that segment disclosures present the measure(s) used by the chief operating decision maker for purposes of assessing segments’ performance. Net operating income is a key measurement of our segment profit and loss. Net operating income is defined as segment real estate rental revenue less segment real estate expenses.

The following tables present revenues, net operating income, capital expenditures and total assets for the 2015 and 2014 Quarters and Periods from these segments, and reconciles net operating income of reportable segments to net income attributable to the controlling interests as reported (in thousands):

	Three Months Ended September 30, 2015				
	Office	Retail	Multifamily	Corporate and Other	Consolidated
Real estate rental revenue	$43,616	$15,684	$18,943	$—	$78,243
Real estate expenses	16,612	3,649	7,848	—	28,109
Net operating income	$27,004	$12,035	$11,095	$—	$50,134
Depreciation and amortization					(29,349)
General and administrative					(4,953)
Acquisition costs					(929)
Interest expense					(14,486)
Other income					163
Net income					580
Less: Net loss attributable to noncontrolling interests in subsidiaries					67
Net income attributable to the controlling interests					$647
Capital expenditures	$7,413	$792	$2,489	$280	$10,974
Total assets	$1,266,110	$377,773	$541,480	$43,497	$2,228,860

	Three Months Ended September 30, 2014				
	Office	Retail	Multifamily	Corporate and Other	Consolidated
Real estate rental revenue	$42,628	$14,825	$15,960	$—	$73,413
Real estate expenses	16,066	3,204	6,644	—	25,914
Net operating income	$26,562	$11,621	$9,316	$—	$47,499
Depreciation and amortization					(24,354)
Acquisition costs					(69)
General and administrative					(4,523)
Interest expense					(15,087)
Other income					192
Net income					3,658
Less: Net loss attributable to noncontrolling interests in subsidiaries					10
Net income attributable to the controlling interests					$3,668
Capital expenditures	$7,804	$3,037	$2,157	$3	$13,001
Total assets	$1,277,131	$341,728	$404,596	$35,924	$2,059,379

	Nine Months Ended September 30, 2015				
	Office	Retail	Multifamily	Corporate and Other	Consolidated
Real estate rental revenue	$129,255	$47,754	$50,316	$—	$227,325
Real estate expenses	50,597	12,138	21,811	—	84,546
Net operating income	$78,658				