CARRAMERICA REALTY CORP
Form 10-K
February 28, 2003

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

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

For fiscal year ended December 31, 2002

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 1-11706

CARRAMERICA REALTY CORPORATION

(Exact name of registrant as specified in its charter)

Maryland	**52-1796339**
(State of Incorporation)	**(I.R.S. Employer Identification No.)**

1850 K Street, N.W.

Washington, D.C.	**20006**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (202) 729-1700

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

Title of each class	Name of each exchange on which registered
Common Stock, $0.01 Par Value	New York Stock Exchange
Series B Cumulative Redeemable Preferred Stock, $0.01 Par Value	New York Stock Exchange
Series C Depositary Cumulative Redeemable Preferred Stock, $0.001 Par Value	New York Stock Exchange
Series D Depositary Cumulative Redeemable Preferred Stock, $0.001 Par Value	New York Stock Exchange

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

None

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

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

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

As of June 28, 2002, the aggregate market value of Common Stock held by non-affiliates of the registrant was approximately $1,536.8 million, based upon the closing price of $30.85 on the New York Stock Exchange composite tape on such date.

Number of shares of Common Stock outstanding as of February 24, 2003: 51,737,323

DOCUMENTS INCORPORATED BY REFERENCE: Portions of the proxy statement for the Annual Stockholders Meeting to be held in 2003 are incorporated by reference into Part III.

PART 1

Item 1. Business

THE COMPANY

General

CarrAmerica Realty Corporation is a fully integrated, self-administered and self-managed publicly traded real estate investment trust (REIT). We focus on the acquisition, development, ownership and operation of office properties, located primarily in selected markets across the United States. As of December 31, 2002, we owned greater than 50% interests in 260 operating office buildings and two office buildings and one residential property under construction. The 260 operating office buildings contain a total of approximately 20.3 million square feet of net rentable area. The two office buildings under construction will contain approximately 70,000 square feet of net rentable area. The stabilized operating buildings (those in operation more than one year) in which we owned a controlling interest as of December 31, 2002 were 92.3% leased. These properties had approximately 1,050 tenants. As of December 31, 2002, we also owned minority interests (ranging from 15% to 50%) in 36 operating office buildings and two buildings under construction. The 36 operating office buildings contain a total of approximately 4.9 million square feet of net rentable area. The two office buildings under construction will contain approximately 608,000 square feet of net rentable area. The stabilized operating buildings in which we owned a minority interest as of December 31, 2002 were 92.3% leased.

We were organized as a Maryland corporation on July 9, 1992. We or our predecessor, The Oliver Carr Company (OCCO), have developed, owned and operated office buildings in the Washington, D.C. metropolitan area for more than 40 years. Our experienced staff of approximately 780 employees, including about 470 on-site building employees, provides a broad range of real estate services. Our principal executive offices are located at 1850 K Street, NW, Washington, DC 20006. Our telephone number is 202-729-1700. Our web site can be found at www.carramerica.com.

Business Strategy

Our primary business objectives are to achieve long-term sustainable per share earnings and cash flow growth and to maximize stockholder value by acquiring, developing, owning and operating office properties primarily in markets throughout the United States that we believe exhibit strong, long-term growth characteristics. We believe we utilize our knowledge of our core markets to evaluate market conditions in order to maintain strategic flexibility and determine whether those conditions favor acquisition, development or disposition of assets. During the last five years, we have actively deployed capital between acquisitions and development in order to create a portfolio with strong long-term growth prospects.

Our principal segment of operations is real estate property operations, which consist primarily of commercial property ownership. Approximately 95.4% of our operating revenues for the year ended December 31, 2002 were associated with our real estate property operations. Other business activities, including development and property management services, are included in other operations.

<u>Local Market Focus</u>

We focus our acquisition and development activity in U.S. markets that possess favorable long-term growth characteristics.

We have established a local presence in each of our existing markets by acquiring and/or developing a critical mass of properties. This local presence is maintained through continuing investment and development activity and relationships established by our Market Managing Directors.

Activities in each of the markets in which we own property are overseen by a Market Managing Director. Our Market Managing Directors are responsible for maximizing the performance of our properties in their respective markets, ensuring that we are consistently meeting the needs of our customers, identifying new growth opportunities and maintaining active relationships with real estate brokers. Because they meet with our customers and local brokers on a regular basis, the Market Managing Directors have extensive knowledge of local conditions in their respective markets and are invaluable in building our local operations and investment strategies.

Our property net operating income by market for the year ended December 31, 2002 was as follows:

Market	Percent of Property Operating Income for the Year Ended 12/31/2002
San Francisco Bay Area	33.6
Washington, D.C. Metro	21.4
Southern California	14.2
Seattle/Portland	7.8
Dallas	3.6
Atlanta	5.0
Chicago	4.9
Phoenix	3.0
Denver	2.9
Salt Lake City	2.3
Austin	1.3
	100.0

As a result of the ongoing weak economic climate, the real estate markets have been materially affected. The sustained lack of job growth has reduced demand for office space and overall vacancy rates for office properties have increased in most of our markets. In reviewing various outlooks for the economy, we believe that the vacancy rates will not improve in any material fashion until at least 2004. During 2002, our markets weakened significantly and our operations in those markets were adversely impacted. The occupancy in our portfolio of stabilized operating properties decreased to 92.3% at December 31, 2002 compared to 95.3% at December 31, 2001 and 97.4% at December 31, 2000. Market rental rates have declined in most markets from peak levels and we believe there will be additional declines in some markets in 2003. Rental rates on space that was re-leased in 2002 decreased an average of 12.1% in comparison to rates that were in effect under expiring leases.

Flexible Investment Strategy

We have established a set of general guidelines and physical criteria to evaluate how we allocate our capital resources among investments, including acquisition, disposition and development opportunities. Our capital allocation decisions are driven by real estate research, which focuses on variables such as the economic growth rate, the composition of job growth and the office space supply and demand fundamentals of a particular market.

Acquisitions

From time to time, we have been very active in acquiring office properties. During 2002, we acquired five operating properties totaling almost 900,000 rentable square feet for approximately $216.1 million, including assumed debt. We will continue to selectively pursue acquisitions in our markets where attractive opportunities exist, particularly when pricing yields make acquisitions of existing properties attractive in comparison to new property development. However, competition for available properties and unattractive yields may limit our acquisition activities in 2003.

Dispositions

We also may dispose of assets that become inconsistent with our long-term strategic or return objectives. We may then redeploy the proceeds from the dispositions into other office properties, or use them to fund development operations or to support other corporate needs. We also may contribute properties that we own to joint ventures with third parties.

Development

Development of office properties is a component of our growth strategy. We believe that long-term investment returns resulting from properties we develop should generally exceed those from properties we acquire, without the assumption of significantly increased investment risks inherent in development properties. We seek to control development risks by:

* Employing extensively trained and experienced development personnel;
* Avoiding the assumption of entitlement risk in conjunction with land acquisitions;
* Entering into guaranteed maximum price construction contracts with seasoned and credible contractors;
* Focusing on pre-leasing space and build-to-suit opportunities with our customer network; and
* Analyzing the supply and demand characteristics of a market before commencing inventory development in that market.

In the current environment, we have reduced our speculative development activities significantly and we are now primarily focused on the development of build-to-suit, substantially pre-leased projects and managing projects for third parties. Our research-driven development program enables us to tailor our development activities in each market, from inventory development, build-to-suit projects and acquiring and holding land for future development.

Financing

We manage our capital structure to reflect a long-term investment approach, generally seeking to match the stable return nature of our assets with a mix of equity and various debt instruments. We mainly use fixed rate debt instruments in order to match the returns from our real estate assets. We also utilize variable rate debt for short-term financing purposes or to reduce the risk that fixed rates may overstate our long-term costs of borrowing if assumed inflation or growth in the economy implicit in higher fixed interest rates do not materialize. At times, our mix of variable and fixed rate debt may not suit our needs. At those times, we may enter into interest rate swaps, forward interest rate options or interest rate options in order to assist us in managing our debt mix. We could either hedge our variable rate debt to give it a fixed interest rate or hedge fixed rate debt to give it a variable interest rate, depending upon the interest rate environment we perceive from time to time.

Stock Repurchases

Our Board of Directors has authorized us to spend up to $400.0 million to repurchase our common stock, preferred stock and debt securities, excluding the 9.2 million shares repurchased from Security Capital Group, Incorporated (Security Capital) in November 2001 and our preferred stock redemption of 4.0 million shares in September 2002, which were separately approved. Since the start of this program in mid-2000 through December 31, 2002, we have acquired approximately 10.1 million of our common shares for an aggregate purchase price of approximately $289.0 million. Additionally, during 2002, we repurchased 1.8 million shares of our preferred stock for approximately $45.5 million, in addition to the 4.0 million shares we redeemed in September 2002 for $100.0 million. We continue to monitor market conditions and other alternative investments in order to evaluate whether repurchase of our securities represents an appropriate investment.

Joint Ventures

Joint venture arrangements provide us with opportunities to reduce investment risk by diversifying capital deployment and enhancing returns on invested capital from fee arrangements. We principally utilize these arrangements on projects characterized by large dollar-per-square foot costs and/or when we desire to limit capital deployment in certain of our markets. For example, in August 2000, we consummated a joint venture with the New York State Teachers Retirement System. The transaction allowed us to further our business strategy of increasing returns on our invested capital and to recycle capital into and out of markets based on market dynamics. We received approximately $249.6 million in cash from the transaction at closing. In June 2001, the joint venture obtained third-party financing, and we received $77.9 million of the financing proceeds.

2002 Activities

Acquisition Activity

During 2002, we acquired five operating properties totaling almost 900,000 rentable square feet for approximately $216.1 million including assumed debt. The table below details our 2002 acquisitions.

Property Name	Market	Month Acquired	Number of Buildings	Rentable Square Footage	Purchase Price (000)
11119 Torrey Pines Rd.	Southern California	May-02	1	76,701	$ 19,000
Canal Center	Washington, DC Metro	Aug-02	4	492,001	121,779
TransPotomac V Plaza	Washington, DC Metro	Aug-02	1	96,960	19,721
Carroll Vista I & II	Southern California	Sep-02	3	107,579	24,600
Stanford Research Park	San Francisco Bay Area	Oct-02	2	89,595	31,000
			11	862,836	$ 216,100

Disposition Activity

During 2002, we sold three operating properties totaling almost 900,000 square feet for approximately $169.3 million in cash recognizing a total gain on the sales of $29.8 million. The table below details our 2002 dispositions.

2002				
Property Name	Market	Month Sold	Number of Buildings	Rentable Square Footage
Wasatch 17	Salt Lake City	May-02	1	72,088
Commons at Las Colinas	Dallas	Aug-02	3	604,234
Braker Point	Austin	Aug-02	1	195,230

	5	871,552

Development Activity

During 2002, we placed in service projects with approximately 114,000 rentable square feet of office space that were previously under development. The total cost of these projects was approximately $15.8 million. We expect that the first year stabilized unleveraged return on this square footage will be approximately 8.5%. As of December 31, 2002, we had approximately 70,000 square feet of office space under construction in two projects that we wholly owned. Our total investment in these projects is expected to be $9.5 million. Through December 31, 2002, we had expended $7.4 million or 77.9% of the total expected investment for these projects. In conjunction with an office property development project through a joint venture, we are also developing a residential property. Total project costs for the residential property are expected to be $19.9 million of which $5.4 million had been expended as of December 31, 2002.

Development of properties for others has become a more significant part of this segment of our business. This includes development of properties for joint ventures in which we are partners and for unaffiliated parties.

As of December 31, 2002, we also had approximately 608,000 rentable square feet of office space under construction in two projects in which we own minority interests. These projects are expected to cost approximately $188.3 million. Our total investment in these projects is expected to be approximately $57.7 million. Through December 31, 2002, approximately 53.7% or $101.2 million of the total project costs had been expended, of which our portion was $31.3 million.

HQ Global Workplaces, Inc.

In 1997, we began making investments in HQ Global Workplaces, Inc. (HQ Global), a provider of executive office suites. On June 1, 2000, we, along with HQ Global, VANTAS Incorporated (VANTAS) and FrontLine Capital Group (FrontLine), consummated several transactions including (i) the merger of VANTAS with and into HQ Global, (ii) the acquisition by FrontLine of shares of HQ Global common stock from us and other stockholders of HQ Global, and (iii) the acquisition by VANTAS of our debt and equity interests in OmniOffices (UK) Limited and OmniOffices LUX 1929 Holding Company S.A. We received $377.3 million in cash in connection with these transactions. In addition, $140.5 million of debt which we had guaranteed was repaid with a portion of the cash proceeds. Following the transaction, we owned approximately 16% of the equity of HQ Global on a diluted basis and our investment had a carrying value of $42.2 million.

FrontLine, the majority stockholder of HQ Global, announced in October 2001 that HQ Global was in default with respect to certain covenant and payment obligations under its senior and mezzanine term indebtedness, was in a forbearance period with HQ Global lenders and was actively negotiating with those lenders. In November 2001, FrontLine disclosed that it had recognized an impairment in the value of intangible assets relating to HQ Global due to HQ Global s trend of operating losses and its inability to remain in compliance with the terms of its debt arrangements. Based on these factors, our analysis of the financial condition and operating results of HQ Global (which deteriorated significantly during 2001 as the economic slowdown reduced the demand for temporary office space, particularly from technology-related tenants) and the losses of key board members and executives by HQ Global, particularly in the last half of 2001, we determined in the fourth quarter of 2001, that our investment in HQ Global was impaired. We recorded a $42.2 million impairment charge, reducing the carrying value of our remaining investment in HQ Global to zero.

On March 13, 2002, HQ Global filed for bankruptcy protection under Chapter 11 of the federal bankruptcy laws. During 1997 and 1998, to assist HQ Global as it grew its business, we provided guarantees of HQ Global s performance under four office leases. To our knowledge, all monthly rental payments were made by HQ Global under two of these leases through January 2002, and rental payments under the other two leases were made through February 2002. In connection with the June 2000 merger transaction, FrontLine agreed to indemnify us against any losses incurred with respect to guarantees of the four office leases. However, on June 12, 2002, FrontLine also filed for bankruptcy protection under Chapter 11 of the federal bankruptcy laws, and therefore it is unlikely that we will recover any resulting losses from FrontLine under this indemnity.

In the course of its bankruptcy proceedings, HQ Global has filed motions to reject two of these four leases. One lease is for space in San Jose, California. This lease is for approximately 22,000 square feet of space at two adjacent buildings and runs through October 2008. Total aggregate remaining lease payments under this lease as of February 1, 2002 were approximately $6.2 million (approximately $0.7 million of which was payable in 2002); however, our liability under this guarantee was limited to approximately $2.0 million. We reached an agreement with the landlord of this lease under which we paid $1.75 million in full satisfaction of the guarantee in January 2003. We recognized this expense in 2002.

The second lease that was rejected by HQ Global is a sublease for space in downtown Manhattan. This lease is for approximately 26,000 square feet of space and runs through March 2008, with total aggregate remaining lease payments as of February 1, 2002 of approximately $5.4 million (approximately $0.8 million of which was payable in 2002). In June 2002, we received a demand for payment of the full amount of the guarantee. However, we believe that we have defenses to payment under this guarantee available to us and joined with HQ Global in filing suit on July 24, 2002 in HQ Global s bankruptcy proceedings asking the bankruptcy court to declare that the lease was terminated by the landlord of the sublease not later than February 28, 2002. On July 26, 2002, the landlord under the sublease filed suit in federal court in New York seeking payment from us under this guarantee. In light of our defenses and these proceedings, we have not accrued any expense relating to this guarantee; however, there can be no assurance as to the outcome of the pending litigation or that we will not incur expense or be required to make cash payments relating to this guarantee up to the full amount of the guarantee. As of December 31, 2002, we had not made any payments under this guarantee.

HQ Global has not filed a motion seeking to reject the remaining two leases that we have guaranteed, although it could do so in the future. Even if the leases are not rejected, we may ultimately be liable to the lessors for payments due under the leases. In one case, the lease is for approximately 25,000 square feet of space in midtown Manhattan, and our liability is currently capped at approximately $0.5 million, which liability reduces over the life of the lease until its expiration in September 2007. As of December 31, 2002, we have not accrued any expense related to or made any payments under this guarantee.

The remaining lease is for space in San Mateo, California. This lease is for approximately 19,000 square feet of space and runs through January 2013, with total aggregate remaining lease payments as of March 1, 2002 of approximately $10.4 million (approximately $0.6 million of which was payable in 2002). We initially recognized an expense of $0.4 million under this guarantee in the first quarter of 2002 based on a tentative agreement with HQ Global under which HQ Global would not reject this lease obligation and we would fund HQ Global s operating losses at this location for a limited period of time. Due to deteriorating conditions in the local commercial real estate market, HQ Global subsequently determined that the tentative agreement was not in its best interest. HQ Global indicated to us that it intended to reject this lease unless its rent was reduced to current market rates. As an interim measure, we entered into an agreement with HQ Global as of June 30, 2002 to fund operating losses at this location up to an aggregate amount of $130,000 in exchange for HQ Global forbearing from rejecting this lease until September 15, 2002, or if it obtained from the bankruptcy court an extension of time within which to reject leases, November 1, 2002. Because the bankruptcy court has since twice extended the time period within which HQ Global may reject this lease to May 9, 2003, we have twice extended the existing forbearance agreement in exchange for funding operating losses up to an additional aggregate amount of $245,000. As a result of our efforts to mitigate our exposure under this guarantee, we entered into agreements with HQ Global in January 2003 under which HQ Global assigned its interest as a tenant in this lease to us and we in turn subleased the space back to HQ Global at current market rates. These agreements remain subject to approval by both the bankruptcy court and the landlord under the lease. In addition, these agreements will not be enforceable if HQ Global fails to successfully reorganize and emerge from the bankruptcy proceedings. There can be no assurance that the necessary approvals will be granted, that material changes to the agreements will not be required to gain approvals, or that HQ Global will successfully reorganize and emerge from the bankruptcy proceedings. We increased our provision for loss under this guarantee to $6.9 million in the second quarter of 2002 and this continues to represent the amount we have determined to be our likely exposure under this guarantee as of December 31, 2002. However, there can be no assurance that we will not be required to further increase our provision or make cash payments related to this guarantee in future periods up to, in the aggregate, the full amount of the guarantee. As of December 31, 2002, we had not made any payments under this guarantee.

Financing Activity

In January 2002, we issued $400.0 million of senior unsecured notes. The notes bear interest at 7.125% per annum payable semi-annually beginning on July 15, 2002. The notes mature on January 15, 2012. The notes are unconditionally guaranteed by CarrAmerica Realty, L.P., one of our subsidiaries.

On May 8, 2002, we entered into interest rate swap agreements with JP Morgan Chase and Bank of America, N.A. (both rated A+ by Standard & Poors), hedging $150.0 million of senior unsecured notes due July 2004. We receive interest at a fixed rate of 7.2% and pay interest at a variable rate of six-month LIBOR in arrears plus 2.72%. The interest rate swaps mature at the same time the notes are due and qualify for accounting purposes as fair value hedges.

In November 2002, we issued $50.0 million of 5.261% and $175.0 million of 5.25% senior unsecured notes. The notes mature on November 30, 2007. The interest on the notes is payable semi-annually beginning May 30, 2003. All the notes are unconditionally guaranteed by CarrAmerica Realty, L.P.

In conjunction with the issuance of the $175.0 million of 5.25% senior unsecured notes, in November 2002, we entered into interest rate swap agreements with JP Morgan Chase, Bank of America, N.A. and Goldman Sachs & Co. (all rated A+ by Standard & Poors). We receive interest at a fixed rate of 5.25% and pay interest at a variable rate of six-month LIBOR in arrears plus 1.405%. The interest rate swaps mature at the same time the notes are due and qualify as fair value hedges for accounting purposes.

As of December 31, 2002, 74.3% of our debt carried a fixed rate of interest and 25.7% is subject to a variable rate of interest, including the debt effectively converted to a variable rate though the use of interest rate swap agreements.

During 2002, we repurchased 1.8 million shares of our preferred stock for approximately $45.5 million, redeemed 4.0 million shares of our preferred stock for $100.0 million. We also repurchased 1.4 million shares of our common stock for approximately $35.9 million.

Forward-Looking Statements

Certain statements contained herein constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 (the Reform Act). Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our, and our affiliates, or the industry s actual results, performance, achievements or transactions to be materially different from any future results, performance, achievements or transactions expressed or implied by such forward-looking statements. Such factors include, among others, the following:

* National and local economic, business and real estate conditions that will, among other things, affect:
    * Demand for office properties,
    * The ability of the general economy to recover timely from the current economic downturn,
    * Availability and creditworthiness of tenants,
    * The level of lease rents, and
    * The availability of financing for both tenants and us;
* Adverse changes in the real estate markets, including, among other things:
    * Competition with other companies, and
    * Risks of real estate acquisition and development (including the failure of pending developments to be completed on time and within budget);
* Possible charges or payments resulting from our guarantees of certain leases of HQ Global Workplaces, Inc.;
* Actions, strategies and performance of affiliates that we may not control or companies in which we have made investments;
* Ability to obtain insurance at a reasonable cost;
* Ability to maintain our status as a REIT for federal and state income tax purposes;
* Governmental actions and initiatives; and
* Environmental/safety requirements.

Available Information

The address of our site on the World Wide Web is www.carramerica.com. You may obtain on our web site, free of charge, a copy of this Form 10-K, our quarterly reports on Form 10-Q, current reports on Form 8-K, and any amendments filed to those reports, as soon as reasonably practicable after we electronically file such reports with the Securities and Exchange Commission.

Our Directors

The current members of our Board of Directors are as follows:

* *Thomas A. Carr*, 44, has been our Chairman of the Board of Directors since May 2000 and a director since 1993 and Chief Executive Officer since 1997. Mr. Carr was our President from 1993 until March 2002, our Chief Operating Officer from April 1995 to May 1997 and our Chief Financial Officer from February 1993 to April 1995. Mr. Carr holds a Master of Business Administration degree from Harvard Business School and a Bachelor of Arts degree from Brown University. Mr. Carr is a member of the Board of Governors of the National Association of Real Estate Investment Trusts, the Young Presidents Organization and Federal City Council. He is a member of the Board of Directors of The Oliver Carr Company and V Technologies International Corp. (d\b\a AgilQuest). Mr. Carr is the son of Oliver T. Carr, Jr. and the brother of Robert O. Carr. Mr. Carr is chairman of the Executive Committee and a member of the Investment Committee of the Board of Directors. In addition, Mr. Carr is a member of management s Operating and Investment Committees.

* *Oliver T. Carr*, *Jr.*, 77, was Chairman of our Board of Directors from February 1993 until May 2000. He also served as our Chief Executive Officer from 1993 to 1997. Mr. Carr founded The Oliver Carr Company in 1962 and since that time he has been its Chairman of the Board and a director as well as President from 1962 to 2000. He also is Chairman Emeritus of the Board of Trustees of The George Washington University. Mr. Carr is the father of both our current Chairman, President and Chief Executive Officer, Thomas A. Carr, and Robert O. Carr, the President of Carr Urban Development, LLC. Mr. Carr is chairman of the Investment Committee of the Board of Directors.

* *Andrew F. Brimmer*, 76, has been a director since February 1993. He has been President of Brimmer & Company, Inc., an economic and financial consulting firm, since 1976. Dr. Brimmer is the Wilmer D. Barrett Professor of Economics at the University of Massachusetts, Amherst. He also serves as a director of BlackRock Investment Income Trust, Inc. (and other funds) and Borg-Warner Automotive, Inc. From June 1995 through August 1998, Dr. Brimmer served as chairman of the District of Columbia Financial Control Board. He was a member of the Board of Governors of the Federal Reserve System from March 1966 through August 1974. Dr. Brimmer received a B.A. degree and a master s degree in economics from the University of Washington and a Ph.D. in economics from Harvard University. Dr. Brimmer is chairman of the Audit Committee and a member of the Conflicts Committee, the Executive Compensation Committee and the Nominating and Corporate Governance Committee of the Board of Directors.

* *A. James Clark*, 75, has been a director since February 1993. He is Chairman of the Board and CEO of Clark Enterprises, Inc. (CEI), a Bethesda, Maryland-based holding company. CEI has been involved in real estate and commercial and residential construction since 1972. CEI includes the Clark Construction Group, one of the United States largest general contractors. Mr. Clark is on the Board of Trustees of the University of Maryland College Park Foundation, and is a Trustee Emeritus of the Johns Hopkins University and the Johns Hopkins Board of Medicine. He is also a member of the PGA Tour Golf Course Properties Advisory Board. Mr. Clark is a graduate of the University of Maryland. He is a member of the Investment Committee of the Board of Directors.

* *Philip L. Hawkins,* 47, has been a director since March 2002. Mr. Hawkins has been President since March 2002 and Chief Operating Officer since October 1998. From February 1996 to October 1998, Mr. Hawkins served as Managing Director Asset Management. Prior to that time Mr. Hawkins was employed by Jones Lang LaSalle, a real estate services company, since 1982. He holds a Masters in Business Administration from the University of Chicago Graduate School of Business and a Bachelors of Arts degree from Hamilton College. Mr. Hawkins is a member of the Investment Committee of the Board of Directors. In addition, Mr. Hawkins is a member of management s Operating and Investment Committees.

* *Timothy Howard*, 54, has been a director since August 1998. Mr. Howard has been the Executive Vice President and Chief Financial Officer of Fannie Mae since 1990 and a member of Fannie Mae s Office of the Chairman since November 2000. Mr. Howard has been proposed for election to Fannie Mae s Board of Directors as Vice Chairman in May 2003. From 1988 to 1990, Mr. Howard was Executive Vice President Asset Management of Fannie Mae. Mr. Howard has held positions of increasing responsibility with Fannie Mae since beginning with the company in 1982. Mr. Howard received a Masters degree in economics and Bachelors in economics, magna cum laude, from the University of California, Los Angeles. Mr. Howard chairs the Executive Compensation Committee and is a member of the Audit Committee and the Conflicts Committee of the Board of Directors.

* *Robert E. Torray,* 65, has been a director since February 2002. Mr. Torray is the founder and has been Chairman of Robert E. Torray & Co., Inc., an institutional investment firm since 1972. Mr. Torray is also the founder and President of Torray Corporation, a mutual fund manager and is founder and Chairman of Birmingham Capital Management Company, an investment management company. Mr. Torray received his B.A. from Duke University. Mr. Torray is chairman of the Conflicts Committee and a member of the Nominating and Corporate Governance Committee, the Investment Committee and the Executive Compensation Committee of the Board of Directors.

* *Wesley S. Williams, Jr.*, 60, has been a director since February 1993. Mr. Williams has been a partner of the law firm of Covington & Burling since 1975. After serving as a junior member of the Faculty of Law of Columbia University, Mr. Williams was adjunct professor of real estate finance law at Georgetown University Law Center from 1971 to 1973. In addition, he is an author or contributing author of several texts on banking law and on real estate investment and finance, and served for more than a decade on the Editorial Advisory Board of the District of Columbia Real Estate Reporter. Mr. Williams is currently Chairman of the Board of Directors of the Federal Reserve Bank of Richmond. Mr. Williams is Co-Chairman of the Board of Directors of Lockhart Companies, Inc. and of its real estate, insurance, consumer finance and miscellaneous Internet and venture subsidiaries. Mr. Williams is a member of the Executive Committee of the Board of Trustees of Penn Mutual Life Insurance Company, of which he is the Senior Trustee. He is also Chairman of the Executive Committee of the Board of Regents of the Smithsonian Institution. Mr. Williams received B.A. and J.D.

degrees from Harvard University, an M.A. degree from the Fletcher School of Law and Diplomacy and an LL.M. degree from Columbia University. Mr. Williams is chairman of the Nominating and Corporate Governance Committee and a member of the Audit Committee, Executive Committee and the Conflicts Committee of the Board of Directors.

Our Executive Officers and Certain Key Employees

Our executive officers and key employees (including executive officers and key employees of CarrAmerica Development, Inc. and other affiliates) are as follows:

* Karen B. Dorigan, 38, has been Chief Investment Officer since November 2000. Prior to that time, she was Managing Director Capital Markets and Investments since April 1999. Prior to that time, Ms. Dorigan served as a Senior Vice President since May 1997. Prior to that, Ms. Dorigan served as one of our Vice Presidents since January 1996. Prior to that, Ms. Dorigan served for more than nine years in a variety of capacities in the development business of The Oliver Carr Company, including from February 1993 to January 1996 as a Vice President. Ms. Dorigan holds a Bachelor of Science degree in Economics from the University of Pennsylvania, Wharton School. Ms. Dorigan is a member of management s Operating and Investment Committees.

* Linda A. Madrid, 43, has been Managing Director, General Counsel and Corporate Secretary since November 1998. Prior to that time Ms. Madrid served as Senior Vice President and General Counsel since March 1998. Prior to that time, Ms. Madrid had been Senior Vice President, Managing Director of Legal Affairs and Corporate Secretary of Riggs National Corporation/Riggs Bank N.A. since February 1996 and Vice President and Litigation Manager from September 1993 to January 1996. Before joining Riggs, Ms. Madrid practiced law in several law firms in Washington, D.C. and served as Assistant General Counsel for Amtrak. Ms. Madrid is a member of the Executive Committee of the American Corporate Counsel Association. Ms. Madrid holds a J.D. from Georgetown University Law Center and a Bachelor of Arts degree from Arizona State University. Ms. Madrid is a member of management s Operating Committee.

* Stephen E. Riffee, 45, has been Chief Financial Officer since April 1, 2002. Prior to that time, he served as Senior Vice President, Controller and Treasurer since July 1999. Prior to that time, Mr. Riffee served as Vice President Finance and Chief Accounting Officer of Marriott International, Inc. for three years. Prior to joining Marriott International, Inc., Mr. Riffee served as Assistant Vice President at Burlington Northern Railroad after having previously worked in the National Transportation Practice of KPMG Peat Marwick. Mr. Riffee holds a Bachelor of Science in Commerce degree from the McIntire School of Commerce of the University of Virginia. Mr. Riffee is a member of management s Operating and Investment Committees.

* Paul R. Adkins, 44, was appointed President, Carr Real Estate Services, Inc. in 2002. From 1999 to 2002, he was Managing Director Private Capital. From 1996 to 1999, Mr. Adkins served as the Company s Senior Vice President, Market Managing Director for Washington, D.C. Mr. Adkins has been with the Company for over 17 years, including serving as Vice President of Acquisitions from May 1994 to August 1996. Prior to that, Mr. Adkins served in a variety of other capacities with the Company, with over 12 years in commercial real estate leasing. Mr. Adkins is a member of the District of Columbia s Building Industry Association and Northern Virginia s National Association of Industrial and Office Parks. Mr. Adkins holds a Bachelor of Arts degree in Economics from Bucknell University. Mr. Adkins is a member of management s Operating and Investment Committees.

* Steven N. Bralower, 54, has been Executive Vice President of Carr Real Estate Services, Inc., an affiliate that conducts management and leasing operations, since January 1999, and Senior Vice President of Carr Realty, L.P., a subsidiary, since May 1996. Mr. Bralower was Senior Vice President of Carr Real Estate Services, Inc. from 1993 to May 1996. Mr. Bralower is a member of the Greater Washington Commercial Association of Realtors. Mr. Bralower has been a member of the Georgetown University Law Center adjunct faculty since 1987. Mr. Bralower holds a Bachelor of Arts degree from Kenyon College.

* Robert O. Carr, 53, has been President of CarrAmerica Urban Development, LLC, a subsidiary of CarrAmerica Development, since June 1998, and Chairman of the Board of Directors of Carr Real Estate Services, Inc., since February 1993. Mr. Carr served as President of Carr Real Estate Services, Inc. from 1993 to 1998. Mr. Carr is a director of The Oliver Carr Company. From 1987 until February 1993, he served as President and Chief

Executive Officer of The Oliver Carr Company. Mr. Carr is a member of the Boards of Directors of the Greater Washington Research Center, the Corcoran School of Art and the National Cathedral School for Girls. Mr. Carr is also a member of the Greater Washington Board of Trade, the Urban Land Institute and the D.C. Chamber of Commerce. Mr. Carr holds a Bachelor of Arts degree from Trinity College. Mr. Carr is the son of Oliver T. Carr, Jr. and the brother of Thomas A. Carr.

* Clete Casper, 43, has been Market Managing Director Seattle since July 1999. Prior to that time Mr. Casper served as the Company s Vice President, Market Managing Director for Seattle since July 1996. Mr. Casper has over 10 years of experience in real estate and marketing. Mr. Casper s most recent experience includes one year as a Senior Associate with CB Commercial Real Estate Group Inc., Seattle, Washington. Prior to that, Mr. Casper was with Sabey Corporation in Seattle, Washington, serving as Development Manager for four years and as a Marketing Associate for five years. Mr. Casper is a graduate of Washington State University. Mr. Casper is a member of management s Operating Committee.

* John J. Donovan, Jr., 59, has been a Market Managing Director since July 1999 and was President of Carr Real Estate Services, Inc., from 1999 to 2002. Prior to that time, Mr. Donovan served as Senior Vice President of Carr Real Estate Services, Inc. from 1993 to 1998. He is a member of the Advisory Board for Jubilee Enterprise of Greater Washington, the Economic Club of Washington, the Greater Washington Board of Trade and the Greater Washington Commercial Association of Realtors. Mr. Donovan holds a Bachelor of Arts degree from Georgetown University. Mr. Donovan is a member of management s Operating Committee.

* J. Thad Ellis, 42, has been Market Managing Director Atlanta since July 1999. Prior to that time Mr. Ellis served as the Company s Vice President, Market Managing Director for Atlanta since November 1996. Mr. Ellis has over 15 years of experience in real estate. Mr. Ellis most recent experience includes 10 years with Peterson Properties. At Peterson Properties, his primary responsibility was to oversee and coordinate leasing and property management for the management services portfolio. Mr. Ellis is a graduate of Washington & Lee University and is a member of the National Association of Industrial and Office Parks and Atlanta s Chamber of Commerce and is on the Advisory Board of Black s Guide. Mr. Ellis is a member of management s Operating and Investment Committees.

* Richard W. Greninger, 51, has been Managing Director Property Operations since May 1999. Prior to that time Mr. Greninger served as Senior Vice President Operations since January 1998. Prior to that, Mr. Greninger had been the Senior Vice President of Carr Real Estate Services, Inc., since March 1995. Prior to that time, he had been Vice President of Carr Real Estate Services, Inc. since February 1993. During 1994, Mr. Greninger served as President of the Greater Washington Apartment and Office Building Association. Mr. Greninger has served as a director of both the Institute of Real Estate Management and the Building Owners and Managers Association and a former Chairman of its National Advisory Council. Mr. Greninger holds a Masters in Business Administration from the University of Cincinnati and a Bachelor of Science degree from Ohio State University. Mr. Greninger is a member of management s Operating Committee.

* Kurt A. Heister, 33, joined CarrAmerica in August 2002 as Controller. Prior to joining the Company, he worked for Arthur Andersen LLP for eleven years, most recently as a Senior Manager in their Real Estate and Hospitality practice. Mr. Heister holds a Bachelor of Science degree in Accounting from Pennsylvania State University. Mr. Heister is a member of management s Operating Committee.

* Thomas Levy, 38, has been Senior Vice President Investments since April 2001. He joined CarrAmerica in 1996 as Associate Due Diligence Officer after which he was promoted to Investments Director. He was promoted to Vice President of Special Projects in April 1999 and then promoted to Vice President Investments in April 2000. Prior to joining CarrAmerica, Mr. Levy was an Associate in the Investment Advisory Group at J.E. Roberts Companies for five years. Before joining J.E. Roberts, Mr. Levy was a Senior Consultant with Arthur Andersen & Company. He holds a Master of Business Administration from American University and a Bachelor of Arts in Economics from the University of Wisconsin. Mr. Levy is a member of management s Operating Committee.

* Joel A. Manfredo, 48, became Chief Technology Officer and Managing Director of e-business solutions in November 2000. Prior to joining us, Mr. Manfredo was Vice President and Director of Information Strategies with The Rouse Company from 1988. Mr. Manfredo served as Director of Investment Assets for a subsidiary of McCormick and Company from 1981 to 1988. Mr. Manfredo holds a Masters of Science in Finance and a

Masters of Business Administration from Loyola College, as well as, a Bachelors of Science in Business Administration from Lehigh University. He is a member of management s Operating Committee.

* Robert M. Milkovich, 43, was appointed Managing Director, Carr Real Estate Services, Inc. in 2002. From 1999 to 2002, he was Market Managing Director. Prior to that time Mr. Milkovich served as Vice President, Market Managing Director for Phoenix, Arizona since January 1998. Mr. Milkovich has over 14 years of experience in real estate leasing. Mr. Milkovich s most recent experience includes five years as the Assistant Vice President of leasing for Carr Real Estate Services, Inc. Mr. Milkovich holds a Bachelor of Science in Business Administration from the University of Maryland. Mr. Milkovich is a member of management s Operating Committee.

* Malcolm O Donnell, 49, joined us as Vice President and Managing Director for our Southern California region in October 2000. He was previously employed as Principal of Alpine Holding and Keller Equity Group, Inc. overseeing development projects. From March 1997 to December 1997, Mr. O Donnell was Vice President of Acquisitions for Beacon Properties. Mr. O Donnell holds a Bachelor of Science degree from the University of Southern California. He is a member of management s Operating Committee.

* Gerald J. O Malley, 59, has been Market Managing Director Chicago since July 1999. Prior to that time Mr. O Malley served as Vice President, Market Managing Director for Chicago since July 1996. Mr. O Malley has over 32 years of experience in real estate marketing. Mr. O Malley s most recent experience includes 10 years as founder and President of G. J. O Malley & Company, a real estate office leasing company. Mr. O Malley holds a Bachelors of Business Administration degree from Loyola University. Mr. O Malley is a member of management s Operating Committee.

* Jeffrey S. Pace, 40, has been Market Managing Director Austin since July 1999. Prior to that time Mr. Pace served as Vice President, Market Managing Director for Austin, Texas since May 1997. Mr. Pace has over 14 years of experience in real estate marketing. Mr. Pace s most recent experience was with Trammell Crow Company, where he served as Marketing Director. Prior to that time, Mr. Pace held the position of Marketing Representative in the Dallas and Austin markets for Carlisle Property Company, Stockton, Luedmann, French & West and Trammell Crow Company from 1985 to 1997. Mr. Pace holds a Masters of Business Administration from the University of Texas at Arlington and a Bachelor of Science from the University of Texas at Austin. Mr. Pace is a member of management s Operating Committee.

* Christopher Peatross, 37, joined us as Market Managing Director San Francisco in May 2002. Before joining us, Mr. Peatross served as Senior Vice President for DivcoWest Properties. Before DivcoWest, Mr. Peatross was with Catellus Development Corporation for three years, Hunter Properties for two years and Spieker Properties for six years. Mr. Peatross holds a Bachelor of Science Degree in Quantitative Economics from Stanford University.

* William H. Vanderstraaten, 42, has been Market Managing Director Dallas since July 1999. Prior to that time Mr. Vanderstraaten served as Vice President, Market Managing Director for Dallas since April 1997. Mr. Vanderstraaten has over 16 years of experience in real estate development and leasing fields. Mr. Vanderstraaten s most recent experience prior to working for the Company includes eight years as Vice President New Development for Harwood Pacific Corporation in Dallas, Texas, where his primary responsibilities were directing large scale development projects and coordinating leasing efforts for portfolios. Mr. Vanderstraaten holds a Bachelor of Science degree in Business Administration from Southern Methodist University. Mr. Vanderstraaten is a member of management s Operating Committee.

* Stephen Walsh, 45, has been Senior Vice President of Capital Markets since April 2001. Prior to this appointment, Mr. Walsh served as Acting Manager for Capital Markets. Before joining CarrAmerica, Mr. Walsh was Vice President, Investor Relations for the Mills Corporation. Additionally, he served as Vice President in the Structured Debt Group at Bank of America, N.A. Mr. Walsh received his Master of Business Administration from George Washington University and his Bachelor s degree from the State University of New York. Mr. Walsh is a member of management s Operating Committee.

* Karen L. Widmayer, 44, has served as Senior Vice President of Corporate Communications since August 1999. Prior to that time Ms. Widmayer served as Vice President of Corporate Communications since 1997. Ms. Widmayer is an 18-year veteran of CarrAmerica and our predecessor company. Ms. Widmayer is responsible

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for our strategic marketing and branding including media relations, advertising, community relations, employee communications, corporate and project marketing as well as our web site and intranet site. Ms. Widmayer performed Masters work in Economics at the University of Tennessee. Ms. Widmayer holds a Bachelor of Arts degree in Business Management from Virginia Intermont College. Ms. Widmayer is a member of management s Operating Committee.

* James S. Williams, 46, has been a Managing Director since April 1999 and President of CarrAmerica Development, Inc. since May 1999. Prior to that time Mr. Williams was Senior Vice President of CarrAmerica Development, Inc. since October 1996. Mr. Williams rejoined us after two years as Vice President of Operations of Chadwick International. Prior to that, from 1983 to 1994, he served in a variety of capacities for The Oliver Carr Company including Senior Vice President of Development. Mr. Williams is a guest lecturer at George Washington University. He holds a Bachelor of Science degree in Business Administration from West Virginia University. Mr. Williams is a member of the Board of Directors and a member of the Executive Committee of the District of Columbia Building Industry Association. He is a member of the Investment Committee of CarrAmerica Development, Inc. and a member of management s Investment and Operating Committees.

Risk Factors

In addition to the other information in this document, you should consider carefully the following risk factors in evaluating an investment in our securities. Any of these risks or the occurrence of any one or more of the uncertainties described below could have a material adverse effect on our financial condition and the performance of our business.

Our Performance is Subject to Risks Associated with Real Estate Investment

We are a real estate company that derives most of its income from the ownership and operation of office buildings. There are a number of factors that may adversely affect the income that our properties generate, including the following:

* Economic Downturns. Downturns in the national economy, or in regions or localities where our properties are located, generally will negatively impact the demand for office space and rental rates.

* Oversupply of Office Space. An oversupply of space in markets where we own office properties would typically cause rental rates and occupancies to decline, making it more difficult for us to lease space at attractive rental rates.

* Competitive Properties. If our properties are not as attractive to tenants (in terms of rent, services or location) as other properties that are competitive with ours, we will lose tenants to those properties or could have to reduce our rental rates to compensate for that disparity.

* Renovation Costs. In order to maintain the quality of our office buildings and successfully compete against other properties, we periodically have to spend money to repair and renovate our properties.

* Tenant Risk. Our performance, liquidity and financial condition depend on our ability to collect rent from our tenants. While no tenant in our portfolio accounted for more than 5% of our base rental revenue for the year ended December 31, 2002, our financial position may be adversely affected by financial difficulties experienced by a major tenant, or by a number of smaller tenants, including bankruptcies, insolvencies or general downturns in business.

* Reletting Costs and Uncertainties. As leases expire, we try to either relet the space to an existing tenant or attract a new tenant to occupy the space. In either case, we likely will incur significant costs in the process. In addition, if market rents have declined since the time the expiring lease was entered into, the terms of any new lease signed likely will not be as favorable to us as the terms of the expiring lease, thereby reducing the income earned from that space.

* Regulatory Costs. There are a number of government regulations, including zoning, tax and accessibility laws that apply to the ownership and operation of office buildings. Compliance with

existing and newly adopted regulations may require us to spend a significant amount of money on our properties.

* Fixed Nature of Costs. Most of the costs associated with owning and operating an office building are not necessarily reduced when circumstances such as market factors and competition cause a reduction in income from the property.

* Environmental Problems. Federal, state and local laws and regulations relating to the protection of the environment may require a current or previous owner or operator of real property to investigate and clean up hazardous or toxic substances or petroleum product releases at the property. The clean up can be costly. The presence of or failure to clean up contamination may adversely affect our ability to sell or lease a property or to borrow using a property as collateral.

* Competition. A number of other major real estate investors with significant capital compete with us. These competitors include publicly traded REITs, private REITs, investment banking firms and private institutional investment funds.

* Insurance. Although we believe our properties are adequately covered by insurance, we cannot predict at this time if we will be able to obtain full coverage at a reasonable cost in the future. The costs associated with our June 30, 2002 property and casualty insurance renewals were higher than anticipated. All lines of coverage were affected by higher premiums, in part because insurance companies have experienced a loss of income on their investments, underwriting results have been poor and also as a result of the events of September 11, 2001.

New Developments and Acquisitions May Fail to Perform As Expected

We remain active in developing and acquiring office properties. New office property developments are 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 will increase, and there may be costs incurred for projects that are not completed. In deciding whether to acquire or develop a particular property, we made certain assumptions regarding the expected future performance of that property. If a number of these new properties do not perform as expected, our financial performance will be adversely affected.

We Do Not Have Exclusive Control Over Our Joint Venture Investments

We have invested in projects or properties as a co-venturer or partner in the development of new properties. These investments involve risks not present in a wholly-owned project. Risks related to these investments could include:

* Absence of control over the development, financing, leasing, management and other aspects of the project;

* Possibility that our co-venturer or partner might:

    * become bankrupt;

    * have interests or goals that are inconsistent with ours;

  * take action contrary to our instructions, requests or interests (including those related to our qualification as a REIT for tax purposes); or

  * otherwise impede our objectives; and

* Possibility that we, together with our partners, may be required to fund losses of the investee.

In addition, most of our joint venture agreements contain buy/sell clauses that could require us to buy or sell our interest at a time we do not deem favorable for financial or other reasons including the availability of cash at such time and the impact of tax consequences resulting from any sale.

Our Use of Debt Subjects Us to Various Financing Risks

We regularly borrow money to finance our operations, particularly the acquisition and development of properties. We generally incur unsecured debt, although in many cases we will incur mortgage debt that is secured by one or more of our office buildings. In the future, our financial condition could be materially and adversely affected by our use of debt financing, in part due to the following risks:

* No Limitation on Debt Incurrence. Our organizational documents do not limit the amount of debt we can incur. Our degree of leverage could have important consequences, including making it more difficult for us to obtain additional financing in the future for business needs, as well as making us more vulnerable to an economic downturn.

* Possible Inability to Meet Scheduled Debt Payments; Potential Foreclosure. If our properties do not perform as expected, the cash flow from our properties may not be enough to make required principal and interest payments. If a property is mortgaged to secure payment of indebtedness and we are unable to meet mortgage payments, the holder of the mortgage or lender could foreclose on the property, resulting in loss of income and asset value. An unsecured lender could also attempt to foreclose on some of our assets in order to receive payment.

* Inability to Refinance Debt. In most cases, very little of the principal amount that we borrow is repaid prior to the maturity of the loan. We generally expect to refinance that debt when it matures, although in some cases we may pay off the loan. If principal amounts due at maturity cannot be refinanced, extended or paid with proceeds of other capital transactions, such as new equity capital, our cash flow could be insufficient to repay all maturing debt. Prevailing interest rates or other factors at the time of a refinancing (such as possible reluctance of lenders to make commercial real estate loans) may result in higher interest rates and increased interest expense.

* Financial Covenants Could Adversely Affect Our Financial Condition. Our credit facilities and the indentures under which our senior unsecured indebtedness are issued contain financial and operating covenants, including coverage ratios and other limitations on our ability to incur secured and unsecured indebtedness, sell all or substantially all of our assets and engage in mergers, consolidations and certain acquisitions. These covenants may restrict our ability to engage in transactions that would otherwise be in our best interests. In addition, failure to meet any of the financial covenants could cause an event of default under and/or accelerate some or all of our indebtedness, which would have a material adverse effect on our financial condition. Failure to meet our financial covenants could result from, among other things, changes in our results of operations or even general economic changes.

* Variable Interest Rates Could Increase the Cost of Borrowing. As of December 31, 2002, approximately 25.7% of our total financing was subject to variable interest rates, including our line of credit and debt related to interest rate swap agreements. Because we have not hedged significantly against interest fluctuations, significant increases in interest rates could dramatically increase our costs of borrowing. Additionally, interest rates on certain types of our debt are based on the credit rating of our debt by independent agencies, and would be substantially increased in the event that the credit ratings are downgraded.

* Derivatives. We may use derivative financial instruments at times to limit market risk. Interest rate protection agreements may be used to convert variable rate debt to a fixed rate basis, to convert fixed rate debt to a variable rate basis or to hedge anticipated financing transactions. We use derivative financial instruments only for hedging purposes, and not for speculation or trading purposes. Derivatives expose us to risk if our counter-party does not perform or if interest rates fluctuate.

Our Business Structure Has Certain Risks Associated With It

* **Certain Officers and Directors May Have Interests that Conflict with the Interests of Stockholders.** Certain of our officers and members of our board of directors own limited partnership units in Carr Realty, L.P., a partnership that holds some of our properties. These individuals may have personal interests that conflict with the interests of our stockholders with respect to business decisions affecting us and Carr Realty, L.P., such as interests in the timing and pricing of property sales or refinancings in order to obtain favorable tax treatment. We, as the sole general partner of Carr Realty, L.P., have the exclusive authority to determine whether and on what terms Carr Realty, L.P. will sell or refinance an individual property, but the effect of certain transactions on these

unitholders may influence our decisions affecting these properties.

* **We May Not Be Able to Sell Properties When Appropriate**.

Real estate property investments generally cannot be sold quickly. Agreements that we have entered into with respect to certain properties limit our ability to dispose of these properties. Also, the tax laws applicable to REITs restrict our ability to dispose of certain properties. Therefore, we may be unable to vary our portfolio promptly in response to market conditions, which may adversely affect our financial position. In addition, we are subject to income taxes on the sale of properties by our development company, CarrAmerica Development, Inc.

* **Lack of Voting Control Over Carr Real Estate Services, Inc.**

While most of our income is generated from the ownership and operation of our office buildings, we own an 8.1% voting and a 95.8% nonvoting interest in Carr Real Estate Services, Inc. Carr Real Estate Services, Inc. conducts management and leasing operations for third parties and for office buildings in which we own less than a 100% interest. As of December 31, 2002, we owned approximately 95% of the economic interest in Carr Real Estate Services, Inc. The majority of voting common stock of Carr Real Estate Services, Inc. is owned by The Oliver Carr Company. As a result, we have no right to elect the directors of Carr Real Estate Services, Inc., and our ability to influence its operations is limited. Carr Real Estate Services, Inc. may engage in business activities that are not in our best interests.

* **We Depend On External Capital**.

To qualify as a REIT, we generally must distribute to our stockholders each year at least 90% of our net taxable income excluding net capital gains and in order to eliminate federal income tax, we must distribute 100% of our net taxable income, including capital gains. Because of this distribution requirement, we likely will not be able to fund all future capital needs, including capital for property development and acquisitions, with income from operations. We therefore will have to rely on third-party sources of capital, which may or may not be available on favorable terms, if at all. Our access to third-party sources of capital depends on a number of things, including the market s perception of our growth potential and our current and potential future earnings.

Certain Factors May Inhibit Changes in Control of the Company

* **Charter and By-law Provisions**. Certain provisions of our charter and by-laws may delay or prevent a change in control of the Company or other transactions that could provide our common stockholders with a premium over the then-prevailing market price of our common stock or that might otherwise be in the best interests of our stockholders. These currently include a staggered board of directors and the ability of our board of directors to authorize the issuance of preferred stock without stockholder approval, although our board of directors intends to recommend that our stockholders vote to amend our charter to eliminate the staggered nature of our board of directors. Also, any future series of preferred stock may have voting provisions that could delay or prevent a change in control or other transaction that might involve a premium price or otherwise be in the best interests of our common stockholders.

* **Ownership Limit**. In order to assist us in maintaining our qualification as a REIT and for other strategic reasons, our charter contains certain provisions generally limiting the ownership of shares of capital stock by any single stockholder to 9.8% of our outstanding common stock and/or 9.8% of any class or series of preferred stock. The federal tax laws include complex stock ownership and attribution rules that apply in determining whether a stockholder exceeds the ownership limits. These rules may cause a stockholder to be treated as owning stock that is actually owned by others, including family members and entities in which the stockholder has an ownership interest. Our board of directors may waive this restriction with respect to certain stockholders if it is satisfied that ownership in excess of these ownership limits would not jeopardize our status as a REIT and the board otherwise decides that a waiver would be in our interests. Capital stock acquired or transferred in breach of the ownership limit will be automatically transferred to a trust for the benefit of a designated charitable beneficiary.

* **Maryland Law Provisions**. Certain provisions of Maryland law which are applicable to us because we are a Maryland corporation prohibit business combinations with any person that beneficially owns ten percent or more of our outstanding voting shares (an interested stockholder) or with an affiliate of the interested stockholder. These prohibitions last for five years after the most recent date on which the person became an interested stockholder. After the five-year period, a business combination with an interested stockholder must

be approved by two super-majority stockholder votes unless, among other conditions, our common stockholders receive a minimum price for their shares and the consideration is received in cash or in the same form as previously paid by the interested stockholder for its common shares. Our board of directors has opted out of these business combination provisions. Consequently, the five-year prohibition and the super-majority vote requirements will not apply to a business combination involving us. Our board of directors may, however, repeal this election in most cases and cause us to become subject to these provisions in the future. Being subject to the provisions could delay or prevent a change in control or other transactions that might involve a premium price or otherwise be in the best interests of our stockholders.

The Market Value of Our Securities Can Be Adversely Affected by Many Factors

As with any public company, a number of factors may adversely influence the public market price of our common stock, many of which are beyond our control. These factors include:

* Level of institutional interest in us;
* Perception of REITs generally and REITs with portfolios similar to ours, in particular, by market professionals;
* Attractiveness of securities of REITs in comparison to other companies;
* Our financial condition and performance;
* The market s perception of our growth potential and potential future cash dividends;
* Government action or regulation, including President Bush s proposal to eliminate taxes on dividends for individuals, which, if enacted, is not expected to apply to dividends paid by REITs;
* Increases in market interest rates, which may lead investors to demand a higher annual yield from our distributions in relation to the price paid for our stock; and
* Relatively low trading volume of shares of REITs in general, which tends to exacerbate a market trend with respect to our stock.

Sales of a substantial number of shares of our stock, or the perception that such sales could occur, also could adversely affect prevailing market prices for our stock. In addition to the possibility that we may sell shares of our stock in a public offering at any time, we also may issue shares of common stock upon redemption of units of interest held by third parties in affiliated partnerships that we control, as well as upon exercise of stock options that we grant to our employees and others. All of these shares will be available for sale in the public markets from time to time.

Our Status As a REIT

We believe that we qualify for taxation as a REIT for federal income tax purposes, and we plan to operate so that we can continue to meet the requirements for taxation as a REIT. If we qualify as a REIT, we generally will not be subject to federal income tax on our income that we distribute currently to our shareholders. Many of the REIT requirements, however, are highly technical and complex. The determination that we are a REIT requires an analysis of various factual matters and circumstances that may not be totally within our control. For example, to qualify as a REIT, at least 95% of our gross income must come from specific passive sources, like rent, that are itemized in the REIT tax laws. In determining that we have satisfied this requirement, we have concluded that certain services, such as cafeteria services that we have provided to tenants through an independent contractor in certain of our properties under arrangements where we bear part or all of the expenses of such services, are considered customary in the geographic area where such properties are located. There can be no assurance that the IRS or a court would agree with such conclusion or other positions we have taken interpreting the REIT requirements. We also are required to distribute to our stockholders at least 90% of our REIT taxable income (excluding capital gains). The fact that we hold some of our assets through partnerships and their subsidiaries further complicates the application of the REIT requirements. Even a technical or inadvertent mistake could jeopardize our REIT status. Furthermore, Congress and the IRS might make changes to the tax laws and regulations, and the courts might issue new rulings, that make it more difficult, or impossible, for us to remain qualified as a REIT.

If we fail to qualify as a REIT for federal income tax purposes, we would be subject to federal income tax at regular corporate rates. Also, unless the IRS granted us relief under certain statutory provisions, we would remain disqualified as a REIT for four years following the year we first failed to qualify. If we failed to qualify as a REIT, we would have to pay significant income taxes. This likely would have a significant adverse affect on the value of our securities. In addition, we would no longer be required to pay any dividends to stockholders.

Even if we qualify as a REIT for federal income tax purposes, we are required to pay certain federal, state and local taxes on our income and property. For example, if we have net income from prohibited transactions, that income will be subject to a 100% tax. In general, prohibited transactions are sales or other dispositions of property held primarily for sale to customers in the ordinary course of business. The determination as to whether a particular sale is a prohibited transaction depends on the facts and circumstances related to that sale. While we have recently undertaken a number of asset sales, we do not believe that those sales should be considered prohibited transactions, but there can be no assurance that the IRS would not contend otherwise. In addition, any net taxable income earned directly by some of our affiliates, including Carr Real Estate Services, Inc. and CarrAmerica Development, Inc., is subject to federal and state corporate income tax. In this regard, several provisions of the laws applicable to REITs and their subsidiaries ensure that a taxable REIT subsidiary will be subject to an appropriate level of federal income taxation. For example, a taxable REIT subsidiary is limited in its ability to deduct interest payments made to an affiliated REIT. In addition, the REIT has to pay a 100% penalty tax on some payments that it receives or on some deductions taken by the taxable REIT subsidiaries if the economic arrangements between the REIT, the REIT s tenants, and the taxable REIT subsidiary are not comparable to similar arrangements between unrelated parties. Several entities in which we own interests, including Carr Real Estate Services, Inc. and CarrAmerica Development, Inc., have elected to be taxable REIT subsidiaries. Finally, some state and local jurisdictions may tax some of our income even though as a REIT we are not subject to federal income tax on that income. To the extent that we and our affiliates are required to pay federal, state and local taxes, we will have less cash available for distributions to our shareholders.

Legislative or Regulatory Tax Changes May Adversely Affect Us or Our Shareholders

The federal income tax laws governing REITs and other corporations or the administrative interpretations of those laws may be amended at any time. Any new laws or interpretations may take effect retroactively and could adversely affect us or our shareholders. On January 7, 2003, the Bush Administration released a proposal intended to eliminate one level of the double taxation that is currently imposed on corporate income for regular C corporations by excluding corporate dividends from an individual s taxable income to the extent that corporate income tax has been paid on the earnings from which the dividends are paid. REITs currently are tax-advantaged relative to regular C corporations because they are not subject to corporate-level federal income tax on income they distribute to shareholders, but shareholders do include REIT dividends in taxable income. The tax treatment of REITs generally would not be affected by the Bush Administration s proposal in its current form, except that a REIT that receives dividends from a C corporation that have been subject to corporate income tax could distribute or retain those amounts without a second tax being imposed on the REIT or its shareholders. The Bush Administration s proposal, if enacted, could cause individual investors to view stocks of regular C corporations as more attractive relative to stocks of REITs than is the case currently because part or all of the dividends on the stocks of the regular C corporation would be exempt from tax for the individual. It is not possible to predict whether in fact this change in relative perceived value will occur or if it occurs, what the impact will be on the value of our stock. In any event, there can be no assurance regarding whether the Bush Administration s proposal ultimately will be enacted or the form in which it might in fact be enacted.

Item 2. PROPERTIES

General

As of December 31, 2002, we owned interests (consisting of whole or partial ownership interests) in 296 operating office buildings located in 12 markets across the United States. As of December 31, 2002, we owned fee simple title or leasehold interests in 258 operating office buildings, controlling partial interests in two operating office buildings and non-controlling partial interests of 15% to 50% in 36 operating office buildings. In addition, as of December 31, 2002, we owned two office buildings and one residential property under development. Except as we disclose in Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources , we have no immediate plans to renovate our operating properties other than for routine capital improvements.

The following table sets forth information about each operating property in which we own an interest as of December 31, 2002.

Property	# of Buildings	Net Rentable Area in Sq. Feet[1]	Percent Leased[2]	Total Annualized Base Rent[3] (in thousands)	Average Base Rent /Leased Sq. Feet[4]	Significant Tenants[5]
Consolidated Properties						
EASTERN REGION						
Downtown Washington, D.C.:						
International Square	3	1,014,914	96.2%	$ 33,721	$ 34.54	International Monetary Fund (49%)
900 19th Street	1	101,215	98.1%	3,512	35.36	America s Community Bankers (30%), Stone & Webster Management (13%), Korn/Ferry International (12%), Lucent Technologies (11%)
2550 M Street	1	192,393	100.0%	6,338	32.94	Patton Boggs L.L.P. (99%)
1730 Pennsylvania Avenue[6]	1	229,292	98.7%	8,288	36.64	Federal Deposit Insurance Co. (47%), King & Spalding (39%)
1255 23rd Street[7]	1	306,395	96.4%	8,794	29.79	Chronicle of Higher Education (30%), William M. Mercer, Inc. (20%), J&H/March & McLennan (14%)
1747 Pennsylvania Avenue[7]	1	151,925	94.8%	4,875	33.87	Legg Mason Wood Walker, Inc. (19%)
1775 Pennsylvania Avenue	1	143,857	98.6%	4,133	29.12	Citicorp Savings of Washington (81%)
Suburban Washington, D.C.:						
One Rock Spring Plaza[6]	1	205,721	100.0%	5,934	28.85	Caterair International (22%), Sybase, Inc. (19%)
Sunrise Corporate Center	3	260,253	100.0%	6,473	24.87	Software AG of North America (81%)
Reston Crossing East & West	2	327,788	100.0%	6,556	20.00	Nextel Communications, Inc. (100%)
Trans Potomac V Plaza	1	96,960	94.8%	2,362	25.70	Effinity Financial Corp. (13%), Hawthorn Group, L.C. (13%), Larson & Taylor (11%), Onyx Group (11%), Casals & Associates., Inc. (11%)
Canal Center	4	492,001	90.8%	12,445	27.86	Close Up Foundation (12%)
Atlanta, GA:						
Glenridge	1	63,494	98.4%	1,271	20.36	Metropolitan Life Insurance (13%), Brooks, McGinnis & Co. (12%), Spectrum Realty Advisors (12%), Communications Trends (11%)
Century Springs West	1	95,206	71.7%	1,358	19.90	No tenant occupies 10%
Holcomb Place	1	72,827	100.0%	1,365	18.73	Intercept Inc. (64%), Progeni Corporation (13%), Key Construction Services (12%)
Midori	1	99,691	51.3%	978	19.11	UPS (21%), Oakmont Mortgage (12%)
Parkwood	1	150,270	97.1%	2,811	19.26	Onesource (20%), Numerex Corp. (17%)
Lakewood	1	80,768	32.4%	376	14.40	Arch Wood Protection (25%)
The Summit	1	179,085	100.0%	3,234	18.06	Unisys (86%), CSC Continuum (14%)
Spalding Ridge	1	127,833	92.8%	2,412	20.34	Honey Baked Ham (52%), Federal Deposit Insurance Co. (10%)
2400 Lake Park Drive	1	103,460	76.2%	1,426	18.10	United Healthcare Services (28%), Management Consultants Group (19%)
680 Engineering Drive	1	62,154	71.4%	387	8.76	EMS Technologies (26%), Pointclear, LLC (24%), Intelligent Media Corp. (11%)
Embassy Row	3	465,835	85.6%	6,837	17.15	Ceridian Corp. (29%), Hanover Insurance Co. (17%)
Embassy 100, 500	2	190,470	100.0%	4,224	22.18	Art Institute of Atlanta (60%), Career Education Corp. (40%)
Waterford Centre	1	83,170	50.4%	831	19.83	Wood & Co. (23%)
Eastern Region Subtotal	36	5,296,977	92.2%			

PACIFIC REGION						
Southern California: Orange County/Los Angeles:						
Scenic Business Park	4	138,076	87.0%	2,139	17.81	Talbert Medical Group (19%), Miles, Wright, Finely & Zak (19%), Terayon Communication System (17%), Coast Community College (13%), So. Ca. Blood & Tissue Service (12%)
Harbor Corporate Park	4	151,234	79.6%	2,403	19.96	Anzdl, Inc. (25%), Trizetto Group, Inc. (11%)
Plaza PacifiCare	1	104,377	100.0%	1,063	10.19	Pacificare Health Systems, Inc. (100%)
Katella Corporate Center	1	80,609	100.0%	1,514	18.78	No tenants occupies 10%
Warner Center	12	343,486	82.2%	6,730	23.85	General Services Administration (20%)

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South Coast Executive Center	2	161,787	61.0%	2,529	25.65	No tenants occupies 10%
Warner Premier	1	61,210	87.3%	1,216	22.74	Protective Life Insurance (34%), Charles Schwab (12%), Steven B. Simon (11%)
Von Karman	1	104,138	84.1%	2,236	25.53	Vision Solutions (41%), Fidelity National Title Ins. (26%), Taco Bell Corp. (18%)
2600 W. Olive	1	144,831	100.0%	3,730	25.75	Walt Disney Company (80%), Emmis Radio Corp. (16%)
Bay Technology Center	2	107,481	84.6%	1,358	14.93	Finance America (57%), Stratacare, Inc. (21%)
Pacific Corporate Plaza 1, 2, 3	3	125,268	96.5%	2,489	20.59	Gallagher Bassett Svcs., Inc. (20%), Covenant Care California (16%), Lan International (16%), Aqueduct, Inc. (16%), Marie Callender Pie Shops (14%)
Alton Deere Plaza	6	182,183	74.9%	2,429	17.79	Nextlink California (18%), XO California (12%), Foster Wheeler Environmental (11%)
Westlake Spectrum	2	108,084	78.7%	1,543	18.14	Pinkerton's Inc. (67%), Insweb Corp. (12%)
Southern California: San Diego:						
Del Mar Corporate Plaza	2	123,142	100.0%	3,491	28.35	Stellcom, Inc. (79%), JMI, Inc. (20%)
Wateridge Pavilion	1	62,194	89.4%	1,062	19.09	Bsquare (25%), Wateridge Insurance Service (18%), TCS Mortgage, Inc. (14%)
Towne Center Technology Park 1, 2, 3	3	182,120	100.0%	3,250	17.85	Gateway, Inc. (100%)
Lightspan	1	64,800	100.0%	1,278	19.73	Lightspan Partnership, Inc. (100%)
La Jolla Spectrum 1 & 2	2	156,653	100.0%	5,846	37.32	Torrey Mesa Research Institute (51%), Scripps Research Institute (49%)
Palomar Oaks Technology Park	6	170,357	81.4%	1,995	14.38	Unifet, Inc. (23%), TPR Group, Inc. (13%)
Jaycor	1	105,358	100.0%	1,953	18.54	Gateway, Inc. (100%)
Highlands Corporate Center	5	205,191	92.8%	6,210	32.62	Brobeck, Phleger & Harrison (14%), Vycera Communications, Inc. (12%)
11119 Torrey Pines Road	1	76,701	100.0%	1,480	19.29	Chase Manhattan Mortgage (100%)
Carroll Vista I & II	3	107,579	100.0%	2,076	19.30	Chugai Biopharmaceutical (70%), Cardiodynamics International (17%), Peregrine Semiconductors (13%)
Northern California: San Francisco Bay Area:						
CarrAmerica Corporate Center	7	1,004,679	100.0%	23,569	23.46	AT&T (52%), Peoplesoft (18%), Pacific Bell Mobile Services (17%), Safeway Inc. (13%)

Valley Business Park I	2	67,784	83.2%	964	17.10	Premier Devices, Inc. (35%), Informative Inc. (17%), Acer Labs, Inc. USA (15%)
Bayshore Centre 2	1	94,874	100.0%	1,992	21.00	Redback Networks (100%)
Rincon Centre	3	201,178	88.4%	3,479	19.56	Toshiba America Electronic (31%), Propel Software (21%), Future Electronics Corp. (19%), GDA Technologies, Inc. (11%)
Valley Centre II	4	212,082	100.0%	3,156	14.88	Boston Scientific (100%)
Valley Office Centre	2	68,798	86.8%	2,138	35.80	Bank of America (21%), Quadrep, Inc. (13%)
Valley Centre	2	102,291	100.0%	1,875	18.33	Seagate Technology (40%), Numerical Technologies (38%), Vivace Networks (22%)
Valley Business Park II	6	166,928	88.9%	3,086	20.80	Pericom Semiconductor (40%)
Rio Robles	7	368,178	76.6%	4,595	16.30	Fujitsu Microelectronics (41%), KLA Instruments (27%)
First Street Technology Center	1	67,582	100.0%	1,014	15.00	Comdisco, Inc. (100%)
Baytech Business Park	4	300,000	100.0%	4,890	16.30	Schlumberger Technologies (58%), Caspian Networks (25%), Rapid 5 Networks, Inc. (13%)
3571 North First Street	1	116,000	100.0%	3,202	27.60	Sun Microsystems (100%)
San Mateo Center I	1	72,137	28.6%	371	17.97	ePORATES (29%)
Oakmead West Land A-G	7	425,981	100.0%	9,968	23.40	Applied Materials (100%)
San Mateo II & III	2	141,440	80.7%	3,483	30.53	Women.com Networks (18%)
Hacienda West	2	206,657	90.8%	5,830	31.06	Paychex (13%), Sun Microsystems (13%)

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Sunnyvale Technology Center	5	165,520	100.0%	3,541	21.39	Lattice Semiconductor (51%), BMC Software (25%), Nokia Internet Communications (12%), Metelics Corp. (12%)
Clarify Corporate Center 1, 2, 3, 4	4	258,048	100.0%	7,256	28.12	Nortel Networks, Inc. (100%)
Valley Technology Center 1, 2, 3, 4, 5, 6 & 7	7	460,590	100.0%	11,349	24.64	Lattice Semiconductor (29%), TSMC North America (24%), Fore Systems (18%), Navisite, Inc. (14%)
Golden Gateway Commons	3	275,041	93.5%	9,300	36.15	Norcal Mutual Insurance (28%), Sharper Image Corp. (21%), ABM Industries, Inc. (11%)
Techmart Commerce Center	1	266,520	88.9%	9,419	39.74	Network Conference Co., Inc. (13%)
Fremont Technology Park 1, 2, 3	3	139,304	100.0%	2,648	19.01	Applied Fiber Optics (39%), Flash Electronics (32%), Bandwidth Unlimited (29%)
Mountain View Gateway Center	2	236,400	100.0%	5,327	22.53	KPMG LLP, (57%), Netscape Communications (43%)
Stanford Research Park[6]	2	89,595	100.0%	4,095	45.71	McKinsey & Co. Inc. (44%), Merrill Lynch (36%)
Portland, OR:						
Sunset Corporate Park	3	132,531	60.0%	1,039	13.08	Volkswagon of America (34%)
Rock Creek Corp Center	3	142,662	100.0%	3,166	22.19	Corillian Corp. (86%), University of Phoenix (14%)
Seattle, WA:						
Redmond East	10	396,497	90.5%	5,325	14.84	Avaya, Inc. (21%), Cardiac Pacemakers Inc. (20%), Genetic Systems (14%),

						Riverdeep Group (12%)
Redmond Hilltop B & C	2	90,880	100.0%	1,515	16.67	Concur Technologies (90%), Citrix Systems (10%)
Canyon Park	6	316,667	99.1%	5,152	16.41	Icos Corp. (28%), Targeted Genetics Corp. (24%), FedEx (14%)
Willow Creek	1	96,179	100.0%	1,138	11.83	Data I/O Corp. (100%)
Willow Creek Corp. Center 1, 2, 3, 4, 5, 6	6	329,009				