

PCE 10-Q 9/30/2011

Section 1: 10-Q (FORM 10-Q)

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

FORM 10-Q

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

For the quarterly period ended September 30, 2011

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: 1-9900

PACIFIC OFFICE PROPERTIES TRUST, INC.
(Exact name of registrant as specified in its charter)

Maryland
(State or other jurisdiction of incorporation or organization)

86-0602478
(I.R.S. Employer Identification No.)

10188 Telesis Court, Suite 222
San Diego, CA 92121
(Address of principal executive offices) (Zip Code)

(Registrant's telephone number, including area code): (858) 882-9500

(Former name, former address and former fiscal year, if changed since last report)

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 R No £

Indicate by check mark 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 R No £

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

Large accelerated filer £ Accelerated filer £ Non-accelerated filer £ (Do not check if a smaller reporting company) Smaller Reporting Company R

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes £ No R

APPLICABLE ONLY TO CORPORATE ISSUERS:

As of November 14, 2011 there were issued and outstanding 3,941,142 shares of common stock listed on the NYSE Amex, par value \$0.0001 per share ("Listed Common Stock"); 100 shares of Class B Common Stock, par value \$0.0001 per share; and 2,410,839 shares of Senior Common Stock, par value \$0.0001 per share.

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements (unaudited).

**Pacific Office Properties Trust, Inc.
Consolidated Balance Sheets
(in thousands, except share and per share data)**

	September 30, 2011	December 31, 2010
	(unaudited)	
ASSETS		
Investments in real estate, net	\$ 283,539	\$ 353,137
Cash and cash equivalents	4,777	9,112
Restricted cash	4,545	9,851
Rents and other receivables, net	2,169	2,302
Deferred rents	4,803	6,332
Intangible assets, net	14,125	24,801
Acquired above-market leases, net	223	358
Other assets, net	3,628	5,141
Goodwill	48,549	48,549
Investments in unconsolidated joint ventures	6,406	8,802
Total assets	<u>\$ 372,764</u>	<u>\$ 468,385</u>
LIABILITIES AND EQUITY (DEFICIT)		
Mortgage and other loans, net	\$ 356,208	\$ 420,126
Unsecured notes payable to related parties	21,104	21,104
Accounts payable and other liabilities	28,646	31,816
Acquired below-market leases, net	5,365	7,918
Total liabilities	<u>411,323</u>	<u>480,964</u>
Commitments and contingencies (Note 10)		
Equity:		
Preferred Stock, \$0.0001 par value per share, 100,000,000 shares authorized, one share of Proportionate Voting Preferred Stock issued and outstanding at September 30, 2011 and December 31, 2010	—	—
Senior Common Stock, \$0.0001 par value per share (liquidation preference \$10 per share, \$24,108 and \$24,179 for September 30, 2011 and December 31, 2010 respectively) 40,000,000 shares authorized, 2,410,839 and 2,417,867 shares issued and outstanding at September 30, 2011 and December 31, 2010	21,459	21,525
Listed Common Stock, \$0.0001 par value per share, 599,999,900 shares authorized, 3,941,142 and 3,903,050 shares issued and outstanding at September 30, 2011 and December 31, 2010, respectively	185	185
Class B Common Stock, \$0.0001 par value per share, 100 shares authorized, issued and outstanding at September 30, 2011 and December 31, 2010	—	—
Additional paid-in capital	110	50
Cumulative deficit	(156,175)	(150,524)
Total stockholders' equity (deficit)	<u>(134,421)</u>	<u>(128,764)</u>
Non-controlling interests:		
Preferred unitholders in the Operating Partnership	127,268	127,268
Common unitholders in the Operating Partnership	(31,406)	(11,083)
Total equity (deficit)	<u>(38,559)</u>	<u>(12,579)</u>
Total liabilities and equity (deficit)	<u>\$ 372,764</u>	<u>\$ 468,385</u>

See accompanying notes to consolidated financial statements.

Pacific Office Properties Trust, Inc.
Consolidated Statements of Operations
(in thousands, except share and per share data)
(unaudited)

	For the three months ended	
	September 30,	
	2011	2010
Revenue:		
Rental	\$ 7,233	\$ 10,876
Tenant reimbursements	5,166	5,324
Property management and other services	1,300	—
Parking	1,633	2,025
Other	121	91
Total revenue	15,453	18,316
Expenses:		
Rental property operating	7,914	10,168
General and administrative	2,395	687
Depreciation and amortization	3,717	5,649
Interest	6,306	9,133
Acquisition costs	12	630
Total expenses	20,344	26,267
Loss before equity in net earnings (loss) of unconsolidated joint ventures	(4,891)	(7,951)
Equity in net earnings (loss) of unconsolidated joint ventures	(1,121)	140
Net loss	(6,012)	(7,811)
Net (income) loss attributable to non-controlling interests:		
Preferred unitholders in the Operating Partnership	(568)	(568)
Common unitholders in the Operating Partnership	5,480	6,617
	4,912	6,049
Dividends on Senior Common Stock	(437)	(49)
Net loss attributable to common stockholders	\$ (1,537)	\$ (1,811)
Net loss per common share - basic and diluted	\$ (0.39)	\$ (0.46)
Weighted average number of common shares outstanding - basic and diluted	3,941,242	3,903,150

See accompanying notes to consolidated financial statements.

Pacific Office Properties Trust, Inc.
Consolidated Statements of Operations
(in thousands, except share and per share data)
(unaudited)

	For the nine months ended	
	September 30,	
	2011	2010
Revenue:		
Rental	\$ 25,837	\$ 31,621
Tenant reimbursements	15,397	16,742
Property management and other services	3,533	—
Parking	5,429	6,093
Other	1,013	267
Total revenue	<u>51,209</u>	<u>54,723</u>
Expenses:		
Rental property operating	25,852	29,885
General and administrative	8,029	2,091
Depreciation and amortization	12,801	17,178
Interest	20,035	22,580
Abandoned offering costs	420	—
Acquisition costs	279	630
Impairment on long-lived assets	14,784	—
Total expenses	<u>82,200</u>	<u>72,364</u>
Loss before gain on forgiveness of debt, equity in net earnings (loss) of unconsolidated joint ventures and non-operating income	(30,991)	(17,641)
Gain on forgiveness of debt	10,045	—
Equity in net earnings (loss) of unconsolidated joint ventures	(2,515)	184
Non-operating income	507	—
Net loss	<u>(22,954)</u>	<u>(17,457)</u>
Net (income) loss attributable to non-controlling interests:		
Preferred unitholders in the Operating Partnership	(1,704)	(1,704)
Common unitholders in the Operating Partnership	20,322	15,113
	<u>18,618</u>	<u>13,409</u>
Dividends on Senior Common Stock	(1,312)	(53)
Net loss attributable to common stockholders	<u>\$ (5,648)</u>	<u>\$ (4,101)</u>
Net loss per common share - basic and diluted	<u>\$ (1.44)</u>	<u>\$ (1.06)</u>
Weighted average number of common shares outstanding - basic and diluted	<u>3,918,080</u>	<u>3,869,991</u>

See accompanying notes to consolidated financial statements.

Pacific Office Properties Trust, Inc.
Consolidated Statements of Cash Flows
(in thousands and unaudited)

	For the nine months ended	
	September 30,	
	2011	2010
Operating activities		
Net loss	\$ (22,954)	\$ (17,457)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	12,801	17,178
Abandoned tenant improvement project	111	—
Impairment on long-lived assets	14,784	—
Gain on forgiveness of debt	(10,045)	—
Gain on internalization of the Advisor	(507)	—
Deferred rent	126	(984)
Deferred ground rents	1,559	1,567
Interest amortization	2,117	1,044
Share based compensation	60	150
Above- and below-market lease amortization, net	(876)	(1,495)
Equity in net earnings (loss) of unconsolidated joint ventures	2,515	(184)
Net operating distributions received from unconsolidated joint ventures	—	179
Bad debt expense	277	362
Changes in operating assets and liabilities:		
Restricted cash used for operating activities	4,531	(233)
Rents and other receivables	(142)	(348)
Other assets	928	(1,677)
Accounts payable and other liabilities	(2,027)	5,299
Net cash provided by operating activities	3,258	3,401
Investing activities		
Improvement of real estate	(3,437)	(5,865)
Deposit for acquisition of real estate	—	(5,000)
Investment in unconsolidated joint ventures	(2,876)	—
Acquisition of Advisor, net of cash received	293	—
Capital distributions from unconsolidated joint ventures	1,963	1,472
Capital contributions to unconsolidated joint ventures	(125)	—
Payment of leasing commissions	(663)	(1,249)
Interim financing provided to unconsolidated joint venture	(600)	—
Decrease in restricted cash used for capital expenditures	1,371	349
Net cash used in investing activities	(4,074)	(10,293)
Financing activities		
Repayment of mortgage notes payable	(299)	(352)
Proceeds from mortgage notes payable	—	238
Borrowings from revolving credit facility	553	13,100
Proceeds from sale of Senior Common Stock, net	—	5,905
Senior Common Stock repurchase	(66)	—
Financing costs	(1,558)	—
Offering costs	—	(1,935)
Security deposits	(84)	(97)
Senior Common Stock dividends	(1,295)	(24)
Listed Common Stock dividends	(47)	(593)
Redemption of OP units	—	(500)
Distributions to non-controlling interests - Preferred unitholders	(568)	(1,704)
Distributions to non-controlling interests - Common unitholders	(155)	(2,145)

Net cash (used in) provided by financing activities	<u>\$ (3,519)</u>	<u>\$ 11,893</u>
Increase in cash and cash equivalents	(4,335)	5,001
Cash and cash equivalents at beginning of period	<u>9,112</u>	<u>2,354</u>
Cash and cash equivalents at end of period	<u>\$ 4,777</u>	<u>\$ 7,355</u>
Supplemental cash flow information		
Interest paid	<u>\$ 15,801</u>	<u>\$ 18,217</u>
Supplemental Disclosure of Non-Cash Investing and Financing Activities		
Accrued dividends and distributions	<u>\$ 1,704</u>	<u>\$ —</u>
Accrued capital expenditures	<u>\$ (895)</u>	<u>\$ 1,103</u>

See accompanying notes to consolidated financial statements.

Pacific Office Properties Trust, Inc.
Notes to Consolidated Financial Statements
(unaudited)

1. Organization and Ownership

Pacific Office Properties -

The terms “Pacific Office Properties,” “us,” “we,” and “our” as used in this Quarterly Report on Form 10-Q refer to Pacific Office Properties Trust, Inc. (the “Company”) and its subsidiaries and joint ventures. Through our controlling interest in Pacific Office Properties, L.P. (the “Operating Partnership”), of which we are the sole general partner, and the subsidiaries of the Operating Partnership, we own and operate primarily institutional-quality office properties principally in selected long-term growth markets in southern California and Hawaii. We operate in a manner that permits us to satisfy the requirements for taxation as a real estate investment trust (“REIT”) under the Internal Revenue Code of 1986 (the “Code”).

During 2010, we were externally advised by Pacific Office Management, Inc., a Delaware corporation (the “Advisor” or “Pacific Office Management”), an entity that was owned and controlled by Jay H. Shidler, our Chairman of the Board, and certain of our executive officers and related parties of The Shidler Group, which is a business name utilized by a number of affiliates of Mr. Shidler. The Advisor was responsible for our day-to-day operation and management. Effective as of February 1, 2011, we acquired all of the outstanding stock of our Advisor for an aggregate purchase price of \$25,000 and internalized management.

Through our Operating Partnership, as of September 30, 2011, we owned six office properties comprising approximately 1.5 million rentable square feet and interests (ranging from 5.0% to approximately 32.2%) in 19 joint venture properties, of which we have managing ownership interests in 15, comprising approximately 3.5 million rentable square feet (the “Property Portfolio”). As of September 30, 2011, our Property Portfolio included office buildings in Honolulu, San Diego, Orange County, certain submarkets of Los Angeles and Phoenix. Our property statistics as of September 30, 2011, were as follows:

	Number of Properties	Buildings	Property Portfolio Sq. Ft.
Wholly-owned properties	6	7	1,512,137
Unconsolidated joint ventures properties	19	41	3,454,283
Total	25	48	4,966,420

2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited consolidated financial statements and related disclosures included herein have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”). Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted in accordance with such rules and regulations. In the opinion of management, the consolidated financial statements include all adjustments, consisting of only normal recurring adjustments, necessary to present fairly the financial information in accordance with GAAP.

The financial statements of the Company for all periods presented herein have not been audited by an independent registered public accounting firm. Further, the interim results of operations for the aforementioned periods are not necessarily indicative of the results of operations that might be expected for a given fiscal year.

The accompanying consolidated financial statements should be read in conjunction with the financial statements and notes thereto included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2010.

Principles of Consolidation

The accompanying consolidated financial statements include the account balances and transactions of consolidated subsidiaries, which are wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

Pacific Office Properties Trust, Inc.
Notes to Consolidated Financial Statements

Use of Estimates in Financial Statements

The preparation of financial statements in conformity with GAAP requires management to make 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 reported periods. Actual results could differ from those estimates.

Liquidity

Our business is capital intensive and our ability to maintain our operations depends on our cash flow from operations and our ability to raise additional capital on acceptable terms. Our primary focus is to preserve and generate cash.

We expect to meet our short-term liquidity and capital requirements primarily through existing cash on hand, net cash provided by operating activities, the contribution of existing wholly-owned assets to joint ventures or asset dispositions. We expect to meet our long-term capital requirements through net cash provided by operating activities, borrowings under our revolving credit facility (if available), refinancing of existing debt or through other available investment and financing activities, including the contribution of existing wholly-owned assets to joint ventures (partial sell-down of equity interests in wholly-owned assets) or asset dispositions. In February 2011, we terminated our registered continuous public offering of Senior Common Stock, so this offering is no longer a source of capital for us. In March 2011, we engaged Eastdil Secured to assist in the potential recapitalization of the Hawaii-based portfolio, which could include the contribution of existing wholly-owned assets to joint ventures or asset dispositions. In the second quarter of 2011, we contributed two wholly-owned properties, our Pacific Business News Building and City Square properties, to newly-formed joint ventures with Angelo Gordon & Co.

The following are our actual and potential sources of liquidity in 2011, which we currently believe will be sufficient to fund our 2011 liquidity needs for the remainder of the year:

- Unrestricted and restricted cash on hand;
- Net cash flow generated from operations;
- Contribution of existing wholly-owned assets to joint ventures;
- Asset dispositions; and/or
- Proceeds from additional secured or unsecured debt financings.

These sources are essential to our short-term liquidity and financial position, and we cannot assure you that we will be able to successfully access them (particularly in the current economic environment). If we are unable to generate adequate cash from these sources, we will have liquidity-related problems and may be exposed to significant risks.

We are focused on ensuring our properties are operating as efficiently as possible. We have taken steps to identify opportunities to reduce discretionary operating costs wherever possible and at the same time maintaining the quality of our buildings and the integrity of our management services.

We internalized our management by acquiring our Advisor effective as of February 1, 2011. We now employ our executive officers and other employees through our former Advisor, Pacific Office Management, which is now our subsidiary. By employing personnel, we are now subject to potential liabilities commonly faced by employers, such as workers' disability and compensation claims, potential labor disputes and other employee-related liabilities and grievances. We are also responsible for all costs previously incurred by the Advisor in the management of our Company, but we are relieved of the \$0.8 million annual advisory fee. Because the Advisor operates at a loss, we continue to focus on reducing corporate overhead expenses.

Capital expenditures fluctuate in any given period, subject to the nature, extent and timing of improvements required to maintain our properties. Leasing costs also fluctuate in any given period, depending upon such factors as the type of property, the term of the lease, the type of lease and overall market conditions. Our costs for capital expenditures and leasing fall into two categories: (1) amounts that we are contractually obligated to spend and (2) discretionary amounts. As of September 30, 2011, we expect to spend approximately \$2.9 million in committed capital expenditures and leasing costs. We are currently focused on preserving cash and intend to limit the amount of discretionary funds allocated to capital expenditures and leasing costs in the near term. This may result in a decrease in average rental rates and the number of new leases we execute, which would adversely affect our cash flow generated from operations.

Pacific Office Properties Trust, Inc.
Notes to Consolidated Financial Statements

As of September 30, 2011, our total consolidated debt (which includes our mortgage and other loans with a carrying value of \$356.2 million and our unsecured promissory notes with a carrying value of \$21.1 million) was approximately \$377.3 million, with a weighted average interest rate of 5.92% (utilizing default interest rates for the Sorrento Technology Center loan), and a weighted average remaining term of 4.41 years.

We have \$11.6 million in aggregate principal indebtedness secured by our Sorrento Technology Center property that is in default as of September 30, 2011. On June 6, 2011, we received a notice of default from the lender of this loan asserting our failure to pay all amounts when due thereunder. We are currently in negotiations with the lender to modify the terms of the loan.

While we may be able to anticipate and plan for certain liquidity needs, there may be unexpected increases in uses of cash that are beyond our control and which would affect our financial condition and results of operations. For example, we may be required to comply with new laws or regulations that cause us to incur unanticipated capital expenditures for our properties, thereby increasing our liquidity needs. Even if there are no material changes to our anticipated liquidity requirements, our sources of liquidity may be fewer than, and the funds available from such sources may be less than, anticipated or needed. Although we believe we have sufficient funds to operate in the normal course through at least December 31, 2011, should unexpected events arise, we may need to initiate cost saving and other initiatives to allow us to continue to operate through at least December 31, 2011. These cost savings and other initiatives could negatively impact our operations in future years.

Investments in Real Estate

We account for acquisitions of real estate utilizing the purchase method and, accordingly, the results of operations of acquired properties are included in our results of operations from the respective dates of acquisition.

Investments in real estate properties are stated at cost, less accumulated depreciation and amortization. A portion of certain assets comprising the properties contributed at the time of our formation transactions (the "Contributed Properties") are stated at their historical net cost basis in an amount attributable to the ownership interests in the Contributed Properties owned by Jay H. Shidler. Additions to land, buildings and improvements, furniture, fixtures and equipment and construction in progress are recorded at cost.

Transaction costs related to acquisitions are expensed. Costs associated with developing space for its intended use are capitalized and amortized over their estimated useful lives, commencing at the earlier of the lease execution date or the lease commencement date.

Estimates of future cash flows and other valuation techniques are used to allocate the acquisition cost of acquired properties among land, buildings and improvements, and identifiable intangible assets and liabilities such as amounts related to in-place at-market leases, acquired above- and below-market leases, and acquired above- and below-market ground leases.

The fair values of real estate assets acquired are determined on an "as-if-vacant" basis. The "as-if-vacant" fair value is allocated to land, and where applicable, buildings, tenant improvements and equipment based on comparable sales and other relevant information obtained in connection with the acquisition of the property.

Fair value is assigned to above-market and below-market leases based on the difference between (a) the contractual amounts to be paid by the tenant based on the existing lease and (b) management's estimate of current market lease rates for the corresponding in-place leases, over the remaining terms of the in-place leases. Capitalized above- and below-market lease amounts are reflected in "Acquired above-market leases, net" and "Acquired below-market leases, net," respectively, in the consolidated balance sheets. Capitalized above-market lease amounts are amortized as a decrease to rental revenue over the remaining initial non-cancellable lease terms plus the terms of any below-market fixed rate renewal options that are considered bargain renewal options. Capitalized below-market lease amounts are amortized as an increase in rental revenue over the remaining initial non-cancellable lease terms plus the terms of any below-market fixed rate renewal options that are considered bargain renewal options. If a tenant vacates its space prior to the contractual termination of the lease and no rental payments are being made on the lease, any unamortized balance, net of the security deposit, of the related intangible is written off.

Fair value is also assigned to tenant relationships. Capitalized tenant relationship amounts are included in intangible assets on the balance sheets and are amortized to depreciation and amortization in the accompanying consolidated statements of operations. Amounts are amortized over the remaining terms of the respective leases even if a tenant vacates prior to the contractual termination of the lease. An adjustment to tenant relationship amounts occurs should the property experience an impairment loss.

Pacific Office Properties Trust, Inc.
Notes to Consolidated Financial Statements

The aggregate value of other acquired intangible assets consists of acquired in-place leases. The fair value allocated to acquired in-place leases consists of a variety of components including, but not necessarily limited to: (a) the value associated with avoiding the cost of originating the acquired in-place lease (i.e. the market cost to execute a lease, including leasing commissions and legal fees, if any); (b) the value associated with lost revenue related to tenant reimbursable operating costs estimated to be incurred during the assumed lease-up period (i.e. real estate taxes, insurance and other operating expenses); (c) the value associated with lost rental revenue from existing leases during the assumed lease-up period; and (d) the value associated with any other inducements to secure a tenant lease. The value assigned to acquired in-place leases is amortized over the remaining lives of the related leases.

We record the excess of the cost of an acquired entity over the net of the amounts assigned to assets acquired (including identified intangible assets) and liabilities assumed as goodwill. Goodwill is not amortized but is tested for impairment at a level of reporting referred to as a reporting unit on an annual basis, during the fourth quarter of each calendar year, or more frequently, if events or changes in circumstances indicate that the asset might be impaired. An impairment loss for an asset group is allocated to the long-lived assets of the group on a pro-rata basis using the relative carrying amounts of those assets, except that the loss allocated to an individual long-lived asset shall not reduce the carrying amount of that asset below its fair value. A description of our testing policy is set forth in "Impairment of Long-Lived Assets".

Impairment of Long-Lived Assets

In accordance with the provisions of the Impairment or Disposal of Long-Lived Assets Subsections of Financial Accounting Standards Board ("FASB") Accounting Standards Codification 360, *Property, Plant and Equipment*, we assess the potential for impairment of our long-lived assets, including real estate properties, whenever events occur or a change in circumstances indicate that the recorded carrying value might not be fully recoverable. Indicators of potential impairment include significant decreases in occupancy levels and/or rental rates or a change in strategy that results in a decreased holding period. We determine whether impairment in value has occurred by comparing the estimated future cash flows, undiscounted and excluding interest, expected from the use and eventual disposition of the asset to its carrying value. If the undiscounted cash flows do not exceed the carrying value, the real estate or intangible carrying value is reduced to fair value and impairment loss is recognized. Assets to be disposed of are reported at the lower of the carrying amount or fair value, less costs to sell. In May of 2011, we defaulted on our loan secured by the Sorrento Technology Center property. As a result of our default, our intent and ability to hold the asset long-term was adversely impacted. Based on this event, we concluded the carrying value of the asset may not be fully recoverable and recorded a non-cash asset impairment charge of \$3.3 million which is reflected in the nine month operating results ended September 30, 2011. In addition, as previously mentioned, we contributed our Pacific Business News Building and City Square properties into joint ventures with a third party based on fair values below the current carrying values. As a result, we recorded additional non-cash asset impairment charges of \$5.1 million and \$6.4 million, respectively. No impairment was identified for the three months ended September 30, 2011 and no impairment was identified for the three and nine months ended September 30, 2010.

Investments in Unconsolidated Joint Ventures

Our investments in joint ventures are accounted for under the equity method of accounting because we exercise significant influence over, but do not control, our joint ventures. Our joint venture partners have substantive participating rights, including approval of and participation in setting operating budgets. Accordingly, we have determined that the equity method of accounting is appropriate for our investments in joint ventures.

Investments in unconsolidated joint ventures are initially recorded at cost and are subsequently adjusted for our proportionate equity in the net income or net loss of the joint ventures, contributions made to, or distributions received from, the joint ventures and other adjustments. We record distributions of operating profit from our investments in unconsolidated joint ventures as part of cash flows from operating activities and distributions related to a capital transaction, such as a refinancing transaction or sale, as investing activities in the consolidated statements of cash flows. A description of our impairment policy is set forth within this Note 2.

The difference between the initial cost of the investment in our joint ventures included in our consolidated balance sheet and the underlying equity in net assets of the respective joint ventures ("JV Basis Differential") is amortized as an adjustment to equity in net income or net loss of the joint ventures in our consolidated statement of operations over the estimated useful lives of the underlying assets of the respective joint ventures.

We evaluate all investments in accordance with the guidance of FASB Accounting Standards Update 2009-17, *Consolidations (Topic 810): Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities*, which was effective

Pacific Office Properties Trust, Inc.
Notes to Consolidated Financial Statements

January 1, 2010 and which requires ongoing assessments of the investments to determine whether or not they are variable interest entities (“VIEs”) and if they are VIEs, whether or not we are determined to be the primary beneficiary. We would consolidate a VIE if it is determined that we are the primary beneficiary. We use qualitative analyses to determine whether we are the primary beneficiary of a VIE. Consideration of various factors could include, but is not limited to, the purpose and design of the VIE, risks that the VIE was designed to create and pass through, the form of our ownership interest, our representation of the entity’s governing body, the size and seniority of our investment, our ability to participate in policy making decisions, and the rights of the other investors to participate in the decision making process and to replace us as manager and/or liquidate the venture, if applicable. We currently do not hold any investments in VIEs.

Impairment of Investments in Unconsolidated Joint Ventures

Our investment in unconsolidated joint ventures is subject to a periodic impairment review and is considered to be impaired when a decline in fair value, which is less than the carrying value of an investment, is judged to be other-than-temporary. An investment in an unconsolidated joint venture that we identify as having an indicator of impairment is subject to further analysis to determine if the investment is other than temporarily impaired, in which case we write down the investment to its estimated fair value. During a periodic impairment review, we noted uncertainty surrounding debt that matured in May 2011 secured by our US Bank property and as a result, we recorded a non-cash impairment charge of approximately \$1.4 million during the three months ended June 30, 2011 to write off our investment in the unconsolidated joint venture that owns our US Bank property. In addition, during the third quarter of 2011, we noted uncertainty surrounding debt that is scheduled to mature in the first quarter of 2012 secured by our Black Canyon property and the properties that constitute our SoCal Portfolio (“SoCal Portfolio”), and as a result, we recorded non-cash impairment charges of approximately \$0.06 million and \$1.1 million, respectively, during the three months ended September 30, 2011 to write down our investments in the unconsolidated joint ventures that own these properties. Our equity interests in the Black Canyon and SoCal Portfolio joint ventures are 17.5% and 10%, respectively. These non-cash impairment charges are included in “equity from earnings of unconsolidated joint ventures” on the consolidated statement of operations. At September 30, 2011, our remaining investments in the Black Canyon and SoCal Portfolio joint ventures were \$0.04 million and \$0.79 million, respectively. The SoCal Portfolio includes 15 office and flex buildings totaling approximately 1,000,000 rentable square feet situated on seven properties (Via Frontera Business Park, Poway Flex, Carlsbad Corporate Center, Savi Tech Center, Yorba Linda Business Park, South Coast Executive Center and Gateway Corporate Center) in Los Angeles, Orange and San Diego counties in Southern California. We did not recognize an impairment loss on our investment in unconsolidated joint ventures during the three or nine months ended September 30, 2010.

Goodwill

We record the excess cost of an acquired entity over the net of the amounts assigned to assets acquired (including identified intangible assets) and liabilities assumed as goodwill. Goodwill is not amortized but is tested for impairment on an annual basis during the fourth quarter of each calendar year, or more frequently if circumstances indicate that a possible impairment has occurred. The assessment of impairment involves a two-step process whereby an initial assessment for potential impairment is performed, followed by a measurement of the amount of impairment, if any. Impairment testing is performed using the fair value approach, which requires the use of estimates and judgment, at the “reporting unit” level. A reporting unit is the operating segment, or a business that is one level below the operating segment if discrete financial information is prepared and regularly reviewed by management at that level. All of our consolidated properties in Hawaii are considered one reporting unit due to similar geographic and economic characteristics. Our goodwill of \$48.5 million was allocated to the Hawaii reporting unit at the time of our formation transactions in 2008. The reporting unit’s fair value is calculated as the discounted future cash flows based on management’s best estimate of the applicable capitalization and discount rates. If the carrying value of a reporting unit exceeds its fair value, the second step of the goodwill impairment test is performed to measure the amount of impairment loss, if any. An impairment is recognized as a charge against income equal to the excess of the carrying value of goodwill over its implied value on the date of the impairment. Factors that may cause an impairment in goodwill include, but may not be limited to, a sustained decline in our stock price and the occurrence, or sustained existence, of adverse economic conditions or decreased cash flow from our properties.

Revenue Recognition

The following four criteria must be met before we recognize revenue and gains:

- persuasive evidence of an arrangement exists;
- the delivery has occurred or services rendered;
- the fee is fixed and determinable; and
- collectibility is reasonably assured.

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All of our tenant leases are classified as operating leases. For all leases with scheduled rent increases or other adjustments, minimum rental income is recognized on a straight-line basis over the terms of the related leases. Straight-line rent receivable represents rental revenue recognized on a straight-line basis in excess of billed rents and this amount is included in "Deferred rents" on the accompanying consolidated balance sheets. The straight-line rent adjustment included in rental revenues was an increase of \$0.05 million and \$0.35 million for the three months ended September 30, 2011 and 2010, respectively. The straight line rent adjustment included in rental revenues was a decrease of (\$0.13) million and an increase of \$0.98 million for the nine months ended September 30, 2011 and 2010, respectively. Reimbursements from tenants for real estate taxes, excise taxes and other recoverable operating expenses are recognized as revenues in the period the applicable costs are incurred.

We have leased space to certain tenants under non-cancelable operating leases, which provide for percentage rents based upon tenant revenues. Percentage rental income is recorded in rental revenues in the consolidated statements of operations.

Rental revenue from parking operations and month-to-month leases or leases with no scheduled rent increases or other adjustments is recognized on a monthly basis when earned.

Lease termination fees, net of the write-off of associated intangible assets and liabilities and straight-line rent balances which are included in other revenues of the accompanying consolidated statements of operations, are recognized when the related leases are canceled and we have no continuing obligation to provide services to such former tenants.

Other revenue on the accompanying consolidated statements of operations generally includes income incidental to our operations and is recognized when earned.

Tenant Receivables

Tenant receivables are recorded and carried at the amount billable per the applicable lease agreement, less any allowance for doubtful accounts. An allowance for doubtful accounts is made when collection of the full amounts is no longer considered probable. Tenant receivables are included in "Rents and other receivables, net," in the accompanying consolidated balance sheets. If a tenant fails to make contractual payments beyond any allowance, we may recognize bad debt expense in future periods equal to the amount of unpaid rent and deferred rent. We take into consideration factors including historical termination, default activity and current economic conditions to evaluate the level of reserve necessary. We had an allowance for doubtful accounts of \$0.5 million and \$0.9 million as of September 30, 2011 and December 31, 2010, respectively.

Notes Receivable

Notes receivable are recorded and carried at the amount stipulated per the loan agreement. In May 2011, we agreed to provide short-term financing in the total amount of \$1.5 million to one of our unconsolidated joint ventures. We funded \$0.6 million of this amount during the second quarter of 2011. No amounts were advanced during the third quarter of 2011. This loan bore interest at the annual rate of 12%, compounded annually, and was scheduled to mature in November 2011. At September 30, 2011, the joint venture was under contract to sell one of the properties included in the portfolio and informed us that it intended to repay us with the proceeds of the sale. The note receivable and related interest of 12% per annum are included in rents and other receivables, net in the accompanying consolidated balance sheets. The sale of the property under contract was consummated in October 2011 and the loan and accrued interest were repaid in full. See further discussion under Note 17, Subsequent Events.

Cash and Cash Equivalents

We consider all short-term cash investments with maturities of three months or less when purchased to be cash equivalents. Restricted cash is excluded from cash and cash equivalents for the purpose of preparing our consolidated statements of cash flows.

We maintain cash balances in various financial institutions. At times, the amounts of cash held in financial institutions may exceed the maximum amount insured by the Federal Deposit Insurance Corporation. We do not believe that we are exposed to any significant credit risk on our cash and cash equivalents.

Restricted Cash

Restricted cash includes escrow accounts for real property taxes, insurance, capital expenditures, tenant improvements and leasing costs held by lenders. As of December 31, 2010, we also had \$1.5 million reserved to fund a letter of credit held by a

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lender for a loan in default. Upon the May 2011 closing of the City Square joint venture with a third party and the joint venture's repayment of the City Square mezzanine note at a discount, the funds used for the letter of credit were returned to us.

Mortgage and Other Loans

Mortgage and other loans assumed upon acquisition of related real estate properties are stated at estimated fair value upon their respective dates of assumption, net of unamortized discounts or premiums to their outstanding contractual balances.

Amortization of discount and the accretion of premiums on mortgage and other loans assumed upon acquisition of related real estate properties are recognized from the date of assumption through their contractual maturity date using the straight line method, which approximates the effective interest method.

Deferred Loan Fees

Deferred loan fees include fees and costs incurred in conjunction with long-term financings and are amortized over the terms of the related debt using a method that approximates the interest method. Deferred loan fees are included in other assets, net in the accompanying consolidated balance sheets. Amortization of deferred loan fees is included in interest in the accompanying consolidated statements of operations.

Repairs, Maintenance and Major Improvements

The costs of ordinary repairs and maintenance are included when incurred in rental property operating expenses in the accompanying consolidated statements of operations. Major improvements that extend the life of an asset are capitalized and depreciated over the remaining useful life of the asset. Various lenders have required us to maintain reserve accounts for the funding of future repairs and capital expenditures, and the balances of these accounts are classified as restricted cash on the accompanying consolidated balance sheets.

Leasing Commissions

Leasing commissions are capitalized and amortized on a straight line basis over the life of the related lease. The payment of leasing commissions is included in cash used in investing activities on the accompanying consolidated statement of cash flows because we believe that paying leasing commissions for good tenants is a prudent investment in increasing the value of our income-producing assets.

Depreciation and Amortization

Depreciation and amortization are computed using the straight-line method for financial reporting purposes. Buildings and improvements are depreciated over their estimated useful lives which range from five to 42 years. Tenant improvement costs recorded as capital assets are depreciated over the shorter of (i) the tenant's remaining lease term or (ii) the life of the improvement. Furniture, fixtures and equipment are depreciated over three to seven years. Properties that are acquired that are subject to ground leases are depreciated over the lesser of the useful life or the remaining life of the related leases as of the date of assumption of the lease.

Equity Offering Costs

Costs from potential equity offerings are reflected in other assets, net in the accompanying consolidated balance sheets and are reclassified as a reduction in additional paid-in capital if and when the offering is successfully completed. Costs include legal, accounting, marketing and other professional fees associated with the offering. If an equity offering is abandoned or delayed for more than 90 days, the costs recorded on the balance sheet are expensed. During the nine months ended September 30, 2011, we expensed \$0.4 million of costs related to an unsuccessful public offering of Listed Common Stock.

Stock-Based Compensation

All share-based payments to employees, including directors, are recognized in the consolidated statement of operations based on their fair values. We recognize share-based compensation in accordance with FASB Accounting Standards Codification (ASC) 718, *Compensation—Stock Compensation*. In accordance with FASB ASC 718, we determine the fair value of the share-based compensation grants on the respective grant dates, and recognize to expense the fair value of the grants over the employees' or

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directors' requisite service periods, which are generally the vesting periods. If the grants vest immediately, we expense the fair value of the grant in full on the grant date. The fair value of the share-based payment awards are generally based on the Company's Listed Common Stock price on the date of grant. See Note 14 for a more detailed discussion.

Non-Controlling Interests

We account for non-controlling interests in accordance with FASB ASC 810, *Consolidation*. In accordance with FASB ASC 810, we report non-controlling interests in subsidiaries within equity in the consolidated financial statements, but separate from the parent stockholders' equity. Net income attributable to non-controlling interests is presented as a reduction from net income in calculating net income available to common stockholders on the statement of operations. Acquisitions or dispositions of non-controlling interests that do not result in a change of control are accounted for as equity transactions. In addition, FASB ASC 810 requires that a parent company recognize a gain or loss in net income when a subsidiary is deconsolidated upon a change in control. In accordance with FASB ASC 480-10, *Distinguishing Liabilities from Equity*, non-controlling interests that are determined to be redeemable are carried at their redemption value as of the balance sheet date and reported as temporary equity. We periodically evaluate individual non-controlling interests for the ability to continue to recognize the non-controlling interest as permanent equity in the consolidated balance sheets. Any non-controlling interest that fails to qualify as permanent equity will be reclassified as temporary equity and adjusted to the greater of (a) the carrying amount, or (b) its redemption value as of the end of the period in which the determination is made, the resulting adjustment is recorded in the consolidated statement of operations.

Preferred Units

The Class A convertible preferred units of the Operating Partnership ("Preferred Units") have fixed rights to distributions at an annual rate of 2% of their liquidation preference of \$25 per Preferred Unit. Accordingly, income or loss of the Operating Partnership is allocated among the general partner interest and limited partner common interests after taking into consideration distribution rights allocable to the Preferred Units.

Earnings (Loss) per Share

We present both basic and diluted earnings (loss) per share ("EPS"). Basic EPS is computed by dividing net income (loss) available to common stockholders by the weighted average number of listed common shares outstanding during each period.

Diluted EPS is computed by dividing net income (loss) available to common stockholders for the period by the weighted average number of listed common shares that would have been outstanding for the period, assuming the issuance of listed common shares for all potentially dilutive listed common shares outstanding during such period.

Segments

We own and operate office properties in the western United States. We have concentrated on two long-term growth submarkets, Honolulu and the western United States mainland (in particular, southern California and the greater Phoenix metropolitan area). We consider each of our properties to be an operating segment. We aggregate the operating segments into two geographic segments on the basis of how the properties are managed and how our chief operating decision maker allocates resources and their similar economic characteristics. See Note 15 for additional details.

Income Taxes

We have elected to be taxed as a REIT under the Code. To qualify as a REIT, we must meet a number of organizational and operational requirements, including a requirement that we currently distribute at least 90% of our REIT taxable income to our stockholders. Also, at least 95% of gross income in any year must be derived from qualifying sources. We intend to adhere to these requirements and maintain our REIT status. As a REIT, we generally will not be subject to corporate level federal income tax on taxable income that we distribute currently to our stockholders. However, we may be subject to certain state and local taxes on our income and property, and to federal income and excise taxes on our undistributed taxable income, if any. Management believes that we have distributed and will continue to distribute a sufficient majority of our taxable income, if any, in the form of dividends and distributions to our stockholders and unit holders. Accordingly, we have not recognized any provision for income taxes.

Pursuant to the Code, we may elect to treat certain of our corporate subsidiaries as taxable REIT subsidiaries ("TRS"). In general, a TRS may perform non-customary services for our tenants, hold assets that we cannot hold directly and generally engage

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in any real estate or non-real estate related business. A TRS is treated as a corporation and is subject to federal income tax and applicable state income and franchise taxes at regular corporate rates. As of December 31, 2010, none of our subsidiaries had elected to be treated as a TRS. However, effective as of February 1, 2011, we internalized our management by acquiring all of the outstanding stock of our Advisor for an aggregate purchase price of \$25,000 payable in cash. We intend to elect to treat this entity, Pacific Office Management, as a TRS for income tax purposes.

Recent Accounting Pronouncements

In September 2011, the FASB issued ASU No. 2011-08, Intangibles - Goodwill and Other (Topic 350), which is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Under the amendments in ASU No. 2011-08, an entity, through an assessment of qualitative factors, is not required to calculate the estimated fair value of a reporting unit, in connection with the two-step goodwill impairment test, unless the entity determines that it is more likely than not that its fair value is less than its carrying amount. ASU No. 2011-08 will apply to our disclosures in Note 2 related to our annual goodwill impairment test.

3. Investments in Real Estate, net

Our investments in real estate, net, at September 30, 2011 (unaudited), and at December 31, 2010, are summarized as follows (in thousands):

	September 30, 2011	December 31, 2010
Land and land improvements	\$ 48,877	\$ 69,040
Building and building improvements	249,065	294,829
Tenant improvements	29,376	35,681
Construction in progress	870	2,757
Furniture, fixtures and equipment	1,354	1,391
Investments in real estate	329,542	403,698
Less: accumulated depreciation	(46,003)	(50,561)
Investments in real estate, net	<u>\$ 283,539</u>	<u>\$ 353,137</u>

4. Intangible Assets and Acquired Above- and Below-Market Lease Liabilities

Our identifiable intangible assets and acquired above- and below-market leases, net at September 30, 2011 (unaudited), and at December 31, 2010, are summarized as follows (in thousands):

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	September 30, 2011	December 31, 2010
Acquired leasing commissions		
Gross amount	\$ 7,316	9,596
Accumulated amortization	(4,186)	(5,528)
Net balance	3,130	4,068
Acquired leases in place		
Gross amount	10,573	15,823
Accumulated amortization	(8,661)	(12,103)
Net balance	1,912	3,720
Acquired tenant relationship costs		
Gross amount	12,844	18,312
Accumulated amortization	(5,855)	(6,899)
Net balance	6,989	11,413
Acquired other intangibles		
Gross amount	3,152	7,139
Accumulated amortization	(1,058)	(1,539)
Net balance	2,094	5,600
Intangible assets, net	\$ 14,125	\$ 24,801
Acquired above-market leases		
Gross amount	\$ 2,018	\$ 2,167
Accumulated amortization	(1,795)	(1,809)
Acquired above-market leases, net	\$ 223	\$ 358
Acquired below-market leases		
Gross amount	\$ 9,133	\$ 15,245
Accumulated amortization	(3,768)	(7,327)
Acquired below-market leases, net	\$ 5,365	\$ 7,918

5. Investments in Unconsolidated Joint Ventures

At September 30, 2011, we owned interests in nine joint ventures (including managing ownership interests in six of those nine, holding 19 office properties, comprised of 41 office buildings and approximately 3.5 million rentable square feet. Our ownership interest percentages in these joint ventures range from 5.0% to 32.2%. In exchange for our equity investment in these joint ventures, we are entitled to fees, preferential allocations of earnings and cash flows from each respective joint venture.

At September 30, 2011 and December 31, 2010, the JV Basis Differential was approximately (\$0.1 million) and \$1.0 million, respectively, and is included in investments in unconsolidated joint ventures in our consolidated balance sheet. During the nine months ended September 30, 2011, we recognized approximately \$1.2 million of amortization expense attributable to the JV Basis Differential (primarily related to the write-off of the JV Basis Differential in the US Bank, Black Canyon and SoCal Portfolio Investments), which is included in equity in net earnings (loss) of unconsolidated joint ventures in our consolidated statement of operations.

During the second quarter of 2011, we identified impairment indicators that are other than temporary, and as such, we do not believe we will be able to recover our 7.5% equity interest in the unconsolidated joint venture that owns our US Bank property. We determined that there was uncertainty surrounding debt secured by our US Bank property due to its maturity in May 2011. Accordingly, we recorded a non-cash impairment charge of approximately \$1.4 million during the three months ended June 30, 2011. In addition, during the third quarter of 2011 we noted uncertainty

surrounding debt that is scheduled to mature in the first

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quarter of 2012 secured by our Black Canyon property and the properties that constitute our SoCal Portfolio, and as a result, we recorded non-cash impairment charges of approximately \$0.06 million and \$1.1 million, respectively, during the three months ended September 30, 2011 to write down our investments in the unconsolidated joint ventures that own these properties. Our equity interests in the Black Canyon and SoCal Portfolio joint ventures are 17.5% and 10%, respectively. At September 30, 2011, our remaining investments in the Black Canyon and SoCal Portfolio joint ventures were \$0.04 million and \$0.79 million, respectively. The SoCal Portfolio includes 15 office and flex buildings totaling approximately 1,000,000 rentable square feet situated on seven properties (Via Frontera Business Park, Poway Flex, Carlsbad Corporate Center, Savi Tech Center, Yorba Linda Business Park, South Coast Executive Center and Gateway Corporate Center) in Los Angeles, Orange and San Diego counties in Southern California. These non-cash impairment charges are presented in “equity in net earnings of unconsolidated joint ventures” on our consolidated statement of operations and represents the difference between the estimated fair value of our investment in these unconsolidated joint venture and their carrying values. Our estimates of the fair values of our investments in these unconsolidated joint ventures were determined using widely accepted valuation techniques, including discounted cash flow analysis on expected cash flows as well as other subjective assumptions that are subject to economic and market uncertainties.

Contribution of Wholly-Owned Assets into Unconsolidated Joint Ventures

On April 13, 2011, we contributed our Pacific Business News Building property to a newly-formed joint venture with Angelo Gordon & Co. (“Angelo Gordon”). The joint venture paid off a previously discounted loan of \$8.7million, secured by the property, which had matured in April 2010.

On May 2, 2011, we contributed our City Square property to a newly-formed joint venture with Angelo Gordon. The joint venture paid off a previously discounted mezzanine loan of \$19.5 million and assumed the senior loan of \$27.5 million, encumbering the City Square property, each of which had matured in September 2010. The lender also extended the maturity date of the senior loan to June 15, 2011. The joint venture refinanced the aforementioned senior loan with a new loan that matures in January 2014.

Acquisition of a Joint Venture Investment

On August 30, 2011, we, along with our joint venture partner Angelo Gordon, acquired the Valencia Corporate Center property, located in Santa Clarita, California. The property was acquired by the joint venture that also owns our Pacific Business News building property. The Company's investment in this joint venture increased by \$0.5 million.

We account for our investments in joint ventures under the equity method of accounting.

The following tables summarize financial information for our unconsolidated joint ventures (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2011	2010	2011	2010
Revenues:				
Rental	\$ 14,003	\$ 11,528	\$ 37,257	\$ 34,431
Other	3,449	2,385	9,229	7,211
Total revenues	17,452	13,913	46,486	41,642
Expenses:				
Rental operating	8,553	5,409	21,408	16,966
Depreciation and amortization	6,539	5,443	18,413	17,301
Interest	7,058	5,955	18,796	17,994
Acquisition costs	357	—	1,396	—
Total expenses	22,507	16,807	60,013	52,261
Net loss	\$ (5,055)	\$ (2,894)	\$ (13,527)	\$ (10,619)
Equity in net earnings (loss) of unconsolidated joint ventures (a)	\$ (1,121)	\$ 140	\$ (2,515)	\$ 184

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	September 30, 2011	December 31, 2010
Investment in real estate, net	\$ 443,256	\$ 381,738
Other assets	88,106	65,064
Total assets	\$ 531,362	\$ 446,802
Mortgage and other loans	\$ 401,952	\$ 365,573
Other liabilities	25,542	20,073
Total liabilities	\$ 427,494	\$ 385,646
Investment in unconsolidated joint ventures	\$ 6,406	\$ 8,802

- (a) The total earnings of all the respective joint ventures of the Company, for all periods presented, are in a loss position. However, the equity in net earnings of the joint ventures attributable to the Company is positive for the three and nine month periods ended September 30, 2010. This occurred because the Company's effective ownership in the various joint ventures ranges from 5.0% to approximately 32.2% and therefore only a portion of the losses of the joint ventures was attributable to the Company. In addition, the Company earns a priority return which, for the three and nine month periods ended September 30, 2010, exceeded the attributable losses, resulting in net earnings attributable to the Company for these periods. Our equity in net earnings of unconsolidated joint ventures is negative for the three and nine month periods ended September 30, 2011 primarily because of the non-cash impairment charges recorded in connection with the write-off of our investment in the unconsolidated joint venture that owns our US Bank property and the write down of our investments in the unconsolidated joint ventures that own our Black Canyon property and the properties that constitute our SoCal Portfolio.

6. Other Assets, net

Other assets, net consist of the following (in thousands):

	September 30, 2011	December 31, 2010
Deferred loan fees, net of accumulated amortization of \$1.5 million and \$1.7 million at September 30, 2011 and December 31, 2010, respectively	\$ 1,338	\$ 1,846
Prepaid expenses	2,290	1,305
Acquisition deposits	—	1,990
Total other assets, net	\$ 3,628	\$ 5,141

7. Accounts Payable and Other Liabilities

Accounts payable and other liabilities consist of the following (in thousands):

	September 30, 2011	December 31, 2010
Accounts payable	\$ 437	\$ 1,150
Interest payable	7,041	6,675
Deferred revenue	1,439	1,690
Security deposits	1,952	2,618
Deferred straight-line ground rent	10,246	8,708
Accrued expenses	6,928	10,334
Asset retirement obligations	603	641
Total accounts payable and other liabilities	\$ 28,646	\$ 31,816

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8. Mortgage and Other Loans

A summary of our mortgage and other loans, net of discount or premium, at September 30, 2011 and December 31, 2010 is as follows (in thousands):

<u>Property</u>	<u>Outstanding Principal Balance, Net at</u>		<u>Interest Rate</u>	<u>Maturity Date</u>
	<u>September 30, 2011</u>	<u>December 31, 2010</u>		
Clifford Center	\$ 3,001	\$ 3,226	4.375 ^(a) %	8/15/2014 ^(a)
First Insurance Center	37,603	37,533	5.74 %	1/1/2016
First Insurance Center	13,852	13,826	5.40 %	1/6/2016
Sorrento Technology Center	11,469	11,521	5.75 ^(b) %	1/11/2016 ^(b)
Pan Am Building	59,973	59,969	6.17 %	8/11/2016
Waterfront Plaza	100,000	100,000	6.37 %	9/11/2016
Waterfront Plaza	11,000	11,000	6.37 %	9/11/2016
Davies Pacific Center	94,310	94,209	5.86 %	11/11/2016
Pacific Business News Building ^(c)	—	11,601	6.98 %	(c)
City Square ^(d)	—	27,500	5.58 %	(d)
City Square ^(e)	—	25,294	LIBOR + 2.35%	(e)
Subtotal	331,208	395,679		
Revolving line of credit ^(f)	25,000	24,447	1.15 %	12/31/2013
Total	<u>\$ 356,208</u>	<u>\$ 420,126</u>		

- (a) The terms of the Clifford Center loan were amended in August 2011 extending the maturity date to August 15, 2014, changing the interest rate to float simultaneously with the lender's prime rate and adjusting the principal portion of the monthly payment to \$31.6 thousand.
- (b) We ceased making the required debt service payments on this loan in the second quarter of 2011, and on June 6, 2011, we received a notice of default accelerating the maturity date of the loan. As a result, interest is being incurred at the stated rate plus the default rate of 5% as stipulated in the loan agreement. We are currently in negotiations with the lender to modify the terms of this loan.
- (c) The loan secured by the Pacific Business News Building property had matured and we had a forbearance agreement in place as of December 31, 2010. In April 2011, we contributed this property into a joint venture with a third party and the joint venture repaid the loan at a discount.
- (d) The senior loan secured by the City Square property had matured and we had a forbearance agreement in place as of December 31, 2010. In May 2011, we contributed this property into a joint venture with a third party that assumed the loan in full and subsequently refinanced it with a new loan that matures in January 2014.
- (e) The mezzanine loan secured by a pledge of the ownership interests in the entities owning the City Square property had matured and we had a forbearance agreement in place as of December 31, 2010. In May 2011, we contributed this property into a joint venture with a third party and the joint venture repaid the loan at a discount.
- (f) The revolving line of credit matures on December 31, 2013. Amounts borrowed under the revolving line of credit bear interest at a fluctuating annual rate equal to the effective rate of interest paid by the lender on time certificates of deposit, plus 1.00%. See "Revolving Line of Credit" below.

The lenders' collateral for notes payable, with the exception of the Clifford Center note payable, is the property and, in some instances, cash reserve accounts, ownership interests in the underlying entity owning the real property, leasehold interests in certain ground leases, rights under certain service agreements, and letters of credit posted by certain related parties of the Company. The lenders' collateral for the Clifford Center note payable is the leasehold property as well as guarantees from affiliates of the Company. The Operating Partnership has agreed to indemnify these affiliates (Mr. Shidler and James C. Reynolds) to the extent of their guaranty liability. In management's judgment, it would be a remote possibility for us to incur any material liability under

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these indemnities that would have a material adverse effect on our financial condition, results of operations or cash flows.

The existing and scheduled maturities for our mortgages and other loans for the periods succeeding September 30, 2011 are as follows (in thousands and includes scheduled principal paydowns):

2011 ⁽¹⁾	\$ 11,689
2012	379
2013	25,379
2014	2,148
2015	—
Thereafter	318,000
Total ⁽²⁾	<u>\$ 357,595</u>

- (1) Includes the loan secured by Sorrento Technology Center, which was declared immediately due and payable by the lender on June 6, 2011 as we have ceased making the required debt service payments.
- (2) This balance is the gross amount and does not include the discount of \$1,387 thousand which is included in the outstanding balance of \$356,208 thousand as shown in mortgage and other loans, net, in the accompanying balance sheet.

Revolving Line of Credit

On September 2, 2009, we entered into a Credit Agreement (the “FHB Credit Facility”) with First Hawaiian Bank (the “Lender”). The FHB Credit Facility initially provided us with a revolving line of credit in the principal sum of \$10 million. On December 31, 2009, we amended the FHB Credit Facility to increase the maximum principal amount available for borrowing under the revolving line of credit to \$15 million. On May 25, 2010, we entered into an amendment with the Lender to increase the maximum principal amount available for borrowing thereunder from \$15 million to \$25 million and to extend the maturity date from September 2, 2011 to December 31, 2013. Amounts borrowed under the FHB Credit Facility bear interest at a fluctuating annual rate equal to the effective rate of interest paid by the Lender on time certificates of deposit, plus 1.00%. We are permitted to use the proceeds of the line of credit for working capital and general corporate purposes, consistent with our real estate operations and for such other purposes as the Lender may approve. As of September 30, 2011 and December 31, 2010, we had outstanding borrowings of \$25.0 million and \$24.4 million, respectively, under the FHB Credit Facility.

As security for the FHB Credit Facility, as amended, Shidler Equities, L.P., a Hawaii limited partnership controlled by Mr. Shidler (“Shidler LP”), has pledged to the Lender a certificate of deposit in the principal amount of \$25.0 million. As a condition to this pledge, the Operating Partnership and Shidler LP entered into an indemnification agreement pursuant to which the Operating Partnership agreed to indemnify Shidler LP from any losses, damages, costs and expenses incurred by Shidler LP in connection with the pledge. In addition, to the extent that all or any portion of the certificate of deposit is withdrawn by the Lender and applied to the payment of principal, interest and/or charges under the FHB Credit Facility, the Operating Partnership agreed to pay to Shidler LP interest on the withdrawn amount at a rate of 7.0% per annum from the date of the withdrawal until the date of repayment in full by the Operating Partnership to Shidler LP. Pursuant to this indemnification agreement, as amended, the Operating Partnership also agreed to pay to Shidler LP an annual fee of 2.0% of the entire \$25.0 million principal amount of the certificate of deposit.

The FHB Credit Facility contains various customary covenants, including covenants relating to disclosure of financial and other information to the Lender, maintenance and performance of our material contracts, our maintenance of adequate insurance, payment of the Lender’s fees and expenses, and other customary terms and conditions.

9. Unsecured Notes Payable to Related Parties

At September 30, 2011 and December 31, 2010, we had promissory notes payable by the Operating Partnership to certain affiliates in the aggregate principal amount of \$21.1 million, at both dates, which were originally issued as consideration to the affiliates, to fund certain capital improvements upon the completion of our formation transactions and upon the exercise of options granted to us by POP Venture, LLC (“Venture”) and its affiliates as part of our formation transactions in 2008. The promissory notes accrue interest at a rate of 7%, per annum, with interest payable quarterly, subject to the Operating Partnership’s right to defer the payment of interest for any or all periods up until the date of maturity. The promissory notes mature on various dates commencing on March 19, 2013 through August 31, 2013, but the Operating Partnership may elect to extend maturity for one additional year. Maturity accelerates upon the occurrence of a) an underwritten public offering of at least \$75 million of our common stock; b) the sale of substantially all the assets of the Company; or c) the merger of the Company with another entity.

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The promissory notes are unsecured obligations of the Operating Partnership.

For the period from March 20, 2008 through September 30, 2011, interest payments on the unsecured notes payable to related parties have been deferred with the exception of \$0.3 million which was related to the notes exchanged for shares of common stock in 2009. At September 30, 2011 and December 31, 2010, \$5.6 million and \$4.3 million, respectively, of accrued interest attributable to unsecured notes payable to related parties is included in accounts payable and other liabilities in the accompanying consolidated balance sheets.

10. Commitments and Contingencies

Minimum Future Ground Rents

We hold long-term ground leasehold interests in our Clifford Center and Waterfront Plaza properties.

The Clifford Center property ground lease expires May 31, 2035. The annual rental obligation is a combination of a base rent amount plus 3% of base rental income from tenants. On June 1, 2016 and 2026, the annual rental obligation will reset to an amount equal to the greater of (i) 6% of the fair market value of the land, and (ii) the ground rent payable for the prior period.

The Waterfront Plaza ground lease expires December 31, 2060. The annual rental obligation has fixed increases at 5-year intervals until it resets on January 1, 2036, 2041, 2046, 2051, and 2056 to an amount equal to the greater of (i) 8.0% of the fair market value of the land and (ii) the ground rent payable for the prior period.

Contingencies

From time to time, we may be subject to various legal proceedings and claims that arise in the ordinary course of business. These matters are generally covered by insurance, subject to deductibles and other customary limitations on recoveries. We believe that the ultimate settlement of these actions will not have a material adverse effect on our consolidated financial position and results of operations or cash flows.

Concentration of Credit Risk

Our operating properties are located in Honolulu, San Diego, Los Angeles, Orange County and Phoenix. The ability of the tenants to honor the terms of their respective leases is dependent upon the economic, regulatory and social factors affecting the markets in which the tenants operate. No single tenant accounts for 10% or more of our total annualized base rents. We perform ongoing credit evaluations of our tenants for potential credit losses.

Financial instruments that subject us to credit risk consist primarily of cash, accounts receivable, deferred rents receivable and an interest rate contract. We maintain our cash and cash equivalents and restricted cash on deposit with what management believes are relatively stable financial institutions. Accounts at each institution are insured by the Federal Deposit Insurance Corporation up to the maximum amount; and, to date, we have not experienced any losses on our invested cash. Restricted cash held by lenders is held by those lenders in accounts maintained at major financial institutions.

Conditional Asset Retirement Obligations

We record a liability for a conditional asset retirement obligation, defined as a legal obligation to perform an asset retirement activity in which the timing and/or method of settlement is conditional on a future event that may or may not be within a company's control, when the fair value of the obligation can be reasonably estimated. Depending on the age of the construction, certain properties in our portfolio may contain non-friable asbestos. If these properties undergo major renovations or are demolished, certain environmental regulations are in place, which specify the manner in which the asbestos, if present, must be handled and disposed. Based on our evaluation of the physical condition and attributes of certain of our properties, we recorded conditional asset retirement obligations related to asbestos removal. As of September 30, 2011 and December 31, 2010, the liability in our consolidated balance sheets for conditional asset retirement obligations was \$0.6 million for both periods. The accretion expense for the three and nine months ended September 30, 2011 and 2010 was not significant.

Clifford Center Ground Lease

We are subject to a surrender clause under the Clifford Center property ground lease that provides the lessor with the right to require us, at our own expense, to raze and remove all improvements from the leased land if we have not complied with certain other provisions of the ground lease. These provisions require us to: (1) only make significant improvements or alterations to

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the building under the supervision of a licensed architect and/or structural engineer with lessor's written approval; (2) comply with the Americans with Disabilities Act of 1990; and (3) comply with all federal, state, and local laws regarding the handling and use of hazardous materials. The requirement to remove the improvements is contingent, first, on our failure to comply with the terms of the lease and, second, upon the cost of compliance with the lease exceeding the estimated value of the improvements. To our knowledge, we are in substantial compliance with the Americans with Disabilities Act of 1990, all work is supervised by licensed professionals, and we are not aware of any violations of laws regarding the handling or use of hazardous materials at the Clifford Center property. If we fail to satisfy any of these requirements in the future, the obligation is subject to the lessor's decision to require the improvements to be removed. We intend to satisfy the requirements of the agreement.

Waterfront Plaza Ground Lease

We are subject to a surrender clause under the Waterfront Plaza ground lease that provides the lessor with the right to require us, at our own expense, to raze and remove all improvements from the leased land, contingent on the lessor's decision at the time the ground lease expires on December 31, 2060. Accordingly, as of September 30, 2011 and December 31, 2010, the liability in our consolidated balance sheets for this asset retirement obligation was \$0.3 million for both periods. The accretion expense was not significant for the three and nine months ended September 30, 2011 and 2010, respectively.

Environmental Matters

We follow the policy of monitoring our properties for the presence of hazardous or toxic substances. While there can be no assurance that a material environmental liability does not exist, we are not currently aware of any environmental liability with respect to the properties that would have a material effect on our financial condition, results of operations, and cash flow. Further, we are not aware of any environmental liability or any unasserted claim or assessment with respect to an environmental liability other than our conditional asset retirement obligations that we believe would require additional disclosure or the recording of a loss contingency.

Capital Commitments

We are required by certain leases and loan agreements to complete tenant and building improvements. As of September 30, 2011, this amount is projected to be \$2.9 million during the remainder of 2011 and in 2012. We anticipate that our reserves, as well as other sources of liquidity, including existing cash on hand, our cash flows from operations, financing and investing activities will be sufficient to fund our committed capital expenditures.

The loan secured by our Sorrento Technology Center property requires us to deposit letters of credit totaling \$0.6 million in the event that certain tenants cease occupancy, go dark or give us notice of their intent to vacate the property. Based on our current occupancy expectations for this property, we expect to be funding these letters of credit in the fourth quarter of 2011.

In May 2011, we agreed to provide short-term financing in the total amount of up to \$1.5 million to one of our unconsolidated joint ventures. We funded \$0.6 million of this amount during the second quarter of 2011. No amounts were advanced during the third quarter of 2011. This loan bore interest at the annual rate of 12%, compounded annually, and was scheduled to mature in November 2011. At September 30, 2011, the joint venture was under contract to sell one of the properties included in the portfolio, Palomar Heights Corporate Center, and informed us that it intended to repay us with the proceeds of the sale. The note receivable and related interest of 12% per annum are included in "Rents and other receivables, net" in the accompanying consolidated balance sheets. The sale of Palomar Heights Corporate Center was consummated in October 2011 and the loan and accrued interest were repaid in full. See further discussion under Note 17, Subsequent Events.

Tax Protection Arrangements

A sale of any of the Contributed Properties that would not provide continued tax deferral to Venture is contractually prohibited until March 2018, which is ten years after the closing of the transaction related to such properties. In addition, we have agreed that, during such ten-year period, we will not prepay or defease any mortgage indebtedness of such properties, other than in connection with a concurrent refinancing with non-recourse mortgage debt of an equal or greater amount and subject to certain other restrictions. Furthermore, if any such sale or defeasance is foreseeable, we are required to notify Venture and to cooperate with it in considering strategies to defer or mitigate the recognition of gain under the Code by any of the equity interest holders of the recipient of the Operating Partnership units.

Indemnities

The mortgage debt that we maintain for our consolidated properties and unconsolidated joint venture properties is typically

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property-specific debt that is non-recourse to our Operating Partnership, except for customary recourse carve-outs for borrower misconduct and environmental liabilities. The recourse liability for borrower misconduct and environmental liabilities was guaranteed by Mr. Reynolds or, with respect to one loan, Mr. Shidler, or, in some instances, by our Operating Partnership. Our Operating Partnership has agreed to indemnify Messrs. Reynolds and Shidler to the extent of their guaranty liability. This debt strategy isolates mortgage liabilities in separate, stand-alone entities, allowing us to have only our property-specific equity investment at risk, except to the extent of the recourse carve-outs. In management's judgment, it would be unlikely for us to incur any material liability under these indemnities that would have a material adverse effect on our financial condition, results of operations or cash flows.

11. Equity (Deficit) and Earnings (Loss) per Share

Total Equity

The changes in total equity (deficit) for the period from December 31, 2010 to September 30, 2011 are shown below (in thousands):

	Pacific Office Properties Trust, Inc.	Non-controlling interest - Preferred	Non-controlling interest - Common	Total
Balance at December 31, 2010	\$ (128,764)	\$ 127,268	\$ (11,083)	(12,579)
Net loss	(4,335)	1,705	(20,323)	(22,953)
Senior common stock repurchase	(66)	—	—	(66)
Stock compensation	60	—	—	60
Dividends and distributions	(1,316)	(1,705)	—	(3,021)
Balance at September 30, 2011	<u>\$ (134,421)</u>	<u>\$ 127,268</u>	<u>\$ (31,406)</u>	<u>\$ (38,559)</u>

Stockholders' Equity (Deficit)

Our common stock listed on NYSE Amex (the "Listed Common Stock") and Class B Common Stock are identical in all respects, except that in the event of liquidation the Class B Common Stock will not be entitled to any portion of our net assets, which will be allocated and distributed to the holders of the Listed Common Stock. Shares of our Listed Common Stock and Class B Common Stock vote together as a single class and each share is entitled to one vote on each matter to be voted upon by our stockholders. Dividends on the Listed Common Stock and Class B Common Stock are payable at the discretion of our Board of Directors.

Our Senior Common Stock ranks senior to our Listed Common Stock and Class B Common Stock with respect to dividends and distribution of amounts upon liquidation. It has a \$10.00 per share (plus accrued and unpaid dividends) liquidation preference. Subject to the preferential rights of any future series of preferred shares, holders of Senior Common Stock are entitled to receive, when and as declared by the Company's Board of Directors, cumulative cash dividends in an amount per share equal to a minimum of \$0.725 per share per annum, payable monthly. Should the dividend payable on the Listed Common Stock exceed the rate of \$0.20 per share per annum, the Senior Common Stock dividend would increase by 25% of the amount by which the Listed Common Stock dividend exceeds \$0.20 per share per annum. Holders of Senior Common Stock have the right to vote on all matters presented to stockholders as a single class with holders of the Listed Common Stock, the Class B Common Stock and the Company's outstanding share of Proportionate Voting Preferred Stock (as discussed below). Each share of the Company's Listed Common Stock, the Class B Common Stock and the Senior Common Stock is entitled to one vote on each matter to be voted upon by the Company's stockholders. Shares of Senior Common Stock may be exchanged, at the option of the holder, for shares of Listed Common Stock after the fifth anniversary of the issuance of such shares of Senior Common Stock. The exchange ratio is to be calculated using a value for our Listed Common Stock based on the average of the trailing 30-day closing price of the Listed Common Stock on the date the shares are submitted for exchange, but in no event less than \$1.00 per share, and a value for the Senior Common Stock of \$10.00 per share. As of September 30, 2011 and December 31, 2010, we had a total of 2,410,839 and 2,417,867 shares of Senior Common Stock issued and outstanding for net proceeds of \$21.5 million. We terminated our continuous public offering of Senior Common Stock in February 2011 and do not expect to issue any additional shares of Senior Common Stock.

General Partnership Interest

The Company's general partnership interest in the Operating Partnership is denominated in a number of Common Units equal

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to the number of shares of our Listed Common Stock and Class B Common Stock outstanding. Our general partnership interest includes the right to participate in distributions of the Operating Partnership to holders of Common Units in a percentage equal to the quotient obtained by dividing (a) the number of shares of our Listed Common Stock and Class B Common Stock outstanding by (b) the sum of shares of our Listed Common Stock and Class B Common Stock outstanding plus the number of shares of our Listed Common Stock for which the outstanding Common Units of the Operating Partnership may be redeemed. We also hold a number of Senior Common Units corresponding to the number of shares of Senior Common Stock outstanding, which entitle us to receive distributions from the Operating Partnership in an amount per Senior Common Unit equal to the per share dividend payable to holders of our Senior Common Stock.

Non-controlling Interests

Non-controlling interests include the interests in the Operating Partnership that are not owned by the Company, which amounted to all of the Preferred Units and 78.26% of the Common Units outstanding as of September 30, 2011. On August 4, 2010, our Operating Partnership redeemed 198,263 Common Units with a book value of \$0.6 million for consideration of \$0.9 million. The resulting difference of \$0.3 million was recorded as an adjustment to additional paid-in capital and cumulative deficit in accordance with FASB ASC 810, *Consolidation*. In accordance with FASB ASC 810, the redemption of a non-controlling interest that does not result in a change in control is considered to be an equity transaction with no gain or loss recorded on the redemption. During the year ended December 31, 2010, no Preferred Units were redeemed or issued. As of September 30, 2011, 46,698,532 shares of our Listed Common Stock were reserved for issuance upon redemption of outstanding Common Units and Preferred Units.

Upon initial issuance in March 2008, each Preferred Unit was convertible into 7.1717 Common Units, but no earlier than the later of (i) March 19, 2010, and (ii) the date we consummate an underwritten public offering (of at least \$75 million) of our common stock. Upon conversion of the Preferred Units to Common Units, the Common Units were redeemable by the holders on a one-for-one basis for shares of our Listed Common Stock or cash, as elected by the Company, but no earlier than one year after the date of their conversion from Preferred Units to Common Units. The Preferred Units have fixed rights to annual distributions at an annual rate of 2% of their liquidation preference of \$25 per Preferred Unit and priority over Common Units in the event of a liquidation of the Operating Partnership. At September 30, 2011, the cumulative unpaid distributions attributable to Preferred Units were \$1.7 million. We anticipate continuing to accrue these distributions for the remainder of 2011.

On December 30, 2009, we amended certain provisions of the partnership agreement of the Operating Partnership (the "Partnership Agreement") relating to the redemption rights of the Common Units and Preferred Units. The Common Units issued upon the completion of our formation transactions on March 19, 2008 were reclassified as Class B Common Units, which are redeemable by the holder on a one-for-one basis for shares of Listed Common Stock or a new class of Common Units, designated Class C Common Units, which have no redemption rights, as elected by a majority of our independent directors. All other outstanding Common Units were reclassified as Class A Common Units, which are redeemable by the holders on a one-for-one basis for shares of Listed Common Stock or cash, as elected by a majority of our independent directors. If converted, the Preferred Units will convert into Class B Common Units. Furthermore, the Preferred Unit put option was modified by eliminating the various alternative currencies possible upon exercise of the put and permitting only the issuance of new preferred units in settlement of an exercised put. The modification of the terms of the Preferred Units was more than inconsequential and therefore triggered a revaluation of the Preferred Units to their fair value on the modification date. As a result of the amendments to the Partnership Agreement, the Non-Controlling Interests attributable to the Common Units and Preferred Units were reclassified from mezzanine equity to permanent equity on the consolidated balance sheet. Simultaneously, the excess of market value over carrying value for the Preferred Units was booked as a fair value adjustment of Preferred Units on the consolidated statement of operations.

Common Units of all classes and Preferred Units of the Operating Partnership do not have any right to vote on any matters presented to our stockholders. As part of our formation transactions, we issued to the Advisor one share of Proportionate Voting Preferred Stock. The Proportionate Voting Preferred Stock has no dividend rights and minimal rights to distributions in the event of liquidation, but it entitles its holder to vote on all matters for which the holders of Listed Common Stock are entitled to vote. The Proportionate Voting Preferred Stock entitles its holder to cast a number of votes equal to the total number of shares of Listed Common Stock issuable upon redemption for shares of the Common Units and Preferred Units issued in connection with the completion of our formation transactions on March 19, 2008. This number will decrease to the extent that these Operating Partnership units are redeemed for shares of Listed Common Stock in the future. The number will not increase in the event of future unit issuances by the Operating Partnership. As of September 30, 2011, that share of Proportionate Voting Preferred Stock represented 87.9% of our voting power. In connection with the internalization of our management, our Advisor sold the share of Proportionate Voting Preferred Stock to Pacific Office Holding, Inc., a corporation owned by Mr. Shidler and certain of our executive officers and other affiliates, for nominal consideration. Pacific Office Holding, Inc. has agreed to cast its Proportionate Voting Preferred Stock votes on any matter in direct proportion to votes that are cast by limited partners of our Operating Partnership.

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holding the Common Units and Preferred Units issued in the formation transactions.

As of September 30, 2011, Venture owned 46,173,693 shares of our Listed Common Stock assuming that all Operating Partnership units were fully redeemed for shares on such date, notwithstanding the restrictions on redemption noted above. Assuming the immediate redemption of all the Operating Partnership units held by Venture, Venture and its related parties control approximately 91.5% of the total voting power in the Company.

Loss per Share

We present both basic and diluted earnings per share (“EPS”). Basic EPS is computed by dividing net loss available to common stockholders by the weighted average number of shares of Listed Common Stock and Class B Common Stock outstanding during each period. Diluted EPS is computed by dividing net loss available to common stockholders for the period by the number of shares of Listed Common Stock and Class B Common Stock that would have been outstanding assuming the issuance of shares of Listed Common Stock for all potentially dilutive shares of Listed Common Stock outstanding during each period. Net income or loss in the Operating Partnership is allocated in accordance with the Partnership Agreement among our general partner and limited partner Common Unit holders in accordance with their weighted average ownership percentages in the Operating Partnership of 21.74% and 78.26%, respectively, after taking into consideration the priority distributions allocated to the limited partner preferred unit holders in the Operating Partnership. The following is the basic and diluted loss per share/unit (in thousands, except share and per share amounts):

	For the three months ended September 30,		For the nine months ended September 30,	
	2011	2010	2011	2010
Net loss attributable to common stockholders - basic and diluted ⁽¹⁾	\$ (1,537)	\$ (1,811)	\$ (5,648)	\$ (4,101)
Weighted average number of common shares	3,941,242	3,903,150	3,918,080	3,869,991
Potentially dilutive common shares ⁽²⁾	—	—	—	—
Weighted average number of common shares outstanding — basic and diluted	3,941,242	3,903,150	3,918,080	3,869,991
Net loss per common share — basic and diluted	\$ (0.39)	\$ (0.46)	\$ (1.44)	\$ (1.06)

(1) For the three and nine months ended September 30, 2011 and 2010, net loss attributable to common stockholders includes \$0.6 million and \$1.7 million of priority allocation to Preferred Unit holders each, respectively, which is included in non-controlling interests in the consolidated statements of operations. The Company continues to accrue the distributions during the current year period, but does not anticipate paying the distributions in 2011. See below for additional detail.

(2) 14,101,004 shares of Listed Common Stock which may be issued upon redemption of Common Units, 32,597,528 shares of Listed Common Stock which may be issued upon redemption of Preferred Units, and 2,411,826 shares of Senior Common Stock, for the three months ended September 30, 2011 were excluded from the calculation of diluted earnings per share because they were anti-dilutive due to our net loss position;

14,101,004 shares of Listed Common Stock which may be issued upon redemption of Common Units, 32,597,528 shares of Listed Common Stock which may be issued upon redemption of Preferred Units, and 2,414,736 shares of Senior Common Stock, for the nine months ended September 30, 2011 were excluded from the calculation of diluted earnings per share because they were anti-dilutive due to our net loss position;

Approximately 47,615 non-vested restricted stock units, 32,597,528 shares of Listed Common Stock which may be issued upon redemption of Preferred Units, and 275,483 shares of Senior Common Stock, for the three months ended September 30, 2010, were excluded from the calculation of diluted earnings per share because they were anti-dilutive due to our net loss position; and

Approximately 47,615 non-vested restricted stock units, 32,597,528 shares of Listed Common Stock which may be issued upon redemption of Preferred Units, and 99,309 shares of Senior Common Stock, for the nine months ended September 30, 2010, were excluded from the calculation of diluted earnings per share because they were anti-dilutive due to our net loss position.

Refer to “Non-Controlling Interests” and “Stockholders’ Equity (Deficit)” in this footnote for the redemption and

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conversion terms and conditions of the Preferred Units and Senior Common Stock.

Dividends and Distributions

For the fourth quarter of 2010, our board of directors authorized a cash distribution of \$0.011 per Common Unit and a cash dividend of \$0.011 per share of our Listed Common Stock and Class B Common Stock, which was paid on January 17, 2011 to holders of record as of December 31, 2010. In addition, we paid 2% distributions, or \$1.25 per unit, to the holder of the Preferred Units for the quarter ended December 31, 2010 on January 17, 2011. We relied upon borrowings under our revolving line of credit to pay a portion of these dividends and distributions.

Our board of directors has authorized daily dividends on the Senior Common Stock, payable to holders of record of the Senior Common Stock as of the close of business on each day of the period commencing April 22, 2010 through December 31, 2011, in an amount equal to an annualized rate of 7.25%. Dividends declared for each month have been or will be paid on or about the 15th day of the following month.

Amounts accumulated for distribution to stockholders and Operating Partnership unit holders are invested primarily in interest-bearing accounts which are consistent with our intention to maintain our qualification as a REIT. At September 30, 2011, the cumulative unpaid distributions attributable to Preferred Units were \$1.7 million, which we do not anticipate to pay in 2011.

Dividends declared on the Listed Common Stock, Class B Common Stock and Senior Common Stock are included in retained deficit in the accompanying consolidated balance sheets. Distributions on Common Units and Preferred Units are included in non-controlling interests in the accompanying consolidated balance sheets.

12. Acquisition and Disposition Activity

Internalization of the Advisor

Throughout 2010 and January 2011, we were externally advised by our Advisor, an entity that was owned and controlled by Mr. Shidler and certain of our executive officers and related parties. Pursuant to our Advisory Agreement, our Advisor was entitled to an annual corporate management fee of one tenth of one percent (0.1%) of the gross cost basis of our total property portfolio (less accumulated depreciation and amortization), but in no event less than \$1.5 million per annum. Although we were responsible for all direct expenses incurred by us for certain services for which we were the primary service obligee, our Advisor bore the cost and was not reimbursed by us for any expenses incurred by it in the course of performing operational advisory services for us, which expenses included, but were not limited to, salaries and wages, office rent, equipment costs, travel costs, insurance costs, telecommunications and supplies. The corporate management fee was subject to reduction of up to \$750,000 based upon the amounts of the direct costs that we bore. Additionally, our Advisor and its affiliates were entitled to receive property management fees of 2.5% to 4.5% of the rental cash receipts collected by the properties, leasing fees consistent with the prevailing market as well as property transaction fees in an amount equal to 1% of the contract price of any acquired or disposed property; however, such property management fees, leasing fees, and property transaction fees were required to be consistent with prevailing market rates for similar services provided on an arms-length basis in the area in which the subject property is located.

The Advisor was also entitled to certain fees related to any placement of debt or equity that we undertook, including (i) 0.50% of the total amount of co-investment equity capital procured, (ii) 0.50% of the total gross offering proceeds including, but not limited to, the issuance or placement of equity securities and the issuance of Operating Partnership units, and (iii) 0.50% of the principal amount of any new indebtedness related to properties that we wholly own, and on properties owned in a joint venture with co-investment partners or entity-level financings, as well as on amounts available on our credit facilities and on the principal amount of indebtedness we may issue.

Effective as of February 1, 2011 we internalized our management by terminating the Advisory Agreement and acquiring all of the outstanding stock of our Advisor for an aggregate purchase price of \$25,000. The Advisor waived the internalization fee equal to \$1.0 million, plus certain accrued and unreimbursed expenses.

Prior to the internalization, we paid amounts to our Advisor relating to property management, leasing, property transactions and debt placement. The fees paid are summarized in the table below for the indicated periods (in thousands):

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	For the nine months ended September 30, 2011	For the three months ended September 30, 2010	For the nine months ended September 30, 2010
Property management fees			
to affiliates of Advisor ⁽¹⁾	\$ 223	\$ 715	\$ 2,276
Corporate management fees to Advisor	63	188	563
Leasing commissions ⁽²⁾	—	1	254
Construction management fees and other	3	6	42
Total	<u>\$ 289</u>	<u>\$ 910</u>	<u>\$ 3,135</u>

- Property management fees are calculated as a percentage of the rental cash receipts collected by the properties under management (ranging from 2.5% to 4.5%), plus the payroll costs of on-site employees.
- Leasing commissions are capitalized as deferred leasing costs and are amortized over the life of the related lease.

Prior to internalization, our Advisor leased space from us at certain of our wholly-owned properties for building management and corporate offices. The rents from these leases totaled \$0.2 million for the three months ended September 30, 2010, \$0.5 million for the nine months ended September 30, 2010 and \$0.1 million for the one month ended January 31, 2011.

The purchase price of \$25,000 for our Advisor was less than the fair value of the assets acquired and liabilities assumed resulting in a bargain purchase which is recognized as a gain on the acquisition date. The gain resulted in part because previously unpaid amounts due from the wholly-owned properties were eliminated upon consolidation. The \$0.5 million gain is reflected as non-operating income in the consolidated income statement for the nine months ended September 30, 2011. The gain calculation and purchase accounting were finalized during the second quarter of 2011, resulting in an adjustment to non-operating income of \$17 thousand during the three months ended June 30, 2011. No further adjustment was recorded during the quarter ended September 30, 2011.

Since February 1, 2011, we recognized the following revenues, primarily from management contracts with our joint ventures, and expenses due to the internalization of the Advisor (in thousands).

Revenues:	
Property management and other services	\$ 3,533
Rental and other	265
Total revenues	<u>\$ 3,798</u>
Expenses:	
General and administrative and other	\$ 6,145
Total expenses	<u>\$ 6,145</u>

Contribution of Wholly-Owned Assets into Unconsolidated Joint Ventures

On April 13, 2011, we contributed our Pacific Business News Building property to a newly-formed joint venture with Angelo Gordon & Co. (“Angelo Gordon”). The joint venture paid off at a discount the loan secured by the property, which had matured in April 2010.

On May 2, 2011, we contributed our City Square property to a newly-formed joint venture with Angelo Gordon. The joint venture paid off at a discount the mezzanine loan and assumed the senior loan encumbering the City Square property, each of which had matured in September 2010. The lender also extended the maturity date of the senior loan to June 15, 2011. The joint venture refinanced the senior loan with a new loan that matures in January 2014.

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Below is the pro forma information that reflects the specified line items of our consolidated financial statements assuming that the purchase of our Advisor and the contribution of City Square and Pacific Business News Building had been completed as of January 1, 2010 (in thousands, except per share amounts).

	For the three months ended September 30,		For the nine months ended September 30,	
	2011	2010	2011	2010
Pro forma revenues	\$ 15,451	\$ 15,180	\$ 46,687	\$ 45,353
Pro forma net loss attributable to common stockholders	\$ (1,535)	\$ (1,300)	\$ (5,255)	\$ (3,816)
Pro forma loss per common share	\$ (0.39)	\$ (0.33)	\$ (1.34)	\$ (0.99)

Acquisition of a Joint Venture Investment

On August 30, 2011, we, along with our joint venture partner Angelo Gordon, acquired the Valencia Corporate Center property, located in Santa Clarita, California. The property was acquired by the joint venture that also owns our Pacific Business News building property. The Company's investment in this joint venture increased by \$0.5 million.

13. Related Party Transactions

On September 2, 2009, as security for the FHB Credit Facility, Shidler LP pledged to the Lender (the "Shidler LP Pledge") a certificate of deposit in the principal amount of \$10.0 million (the "Certificate of Deposit"). As a condition to the Shidler LP Pledge, our Operating Partnership and Shidler LP entered into an Indemnification Agreement, effective as of September 2, 2009 (the "Indemnification Agreement"), pursuant to which we agreed to indemnify Shidler LP from any losses, damages, costs and expenses incurred by Shidler LP in connection with the Shidler LP Pledge. In addition, to the extent that all or any portion of the Certificate of Deposit is withdrawn by the Lender and applied to the payment of principal, interest and/or charges under the FHB Credit Facility, we agreed to pay to Shidler LP interest on the withdrawn amount at a rate of 7.0% per annum from the date of the withdrawal until the date of repayment in full to Shidler LP. Pursuant to the Indemnification Agreement, we also agreed to pay to Shidler LP an annual fee of 2.0% of the entire principal amount of the Certificate of Deposit. As of December 30, 2009, the amount of the security was increased to \$15.0 million and subsequently further increased to \$25.0 million on May 25, 2010. During the three months ended September 30, 2011 and 2010, we paid \$0.1 million for both periods to Shidler LP for the annual fee. During the nine months ended September 30, 2011 and 2010, we paid \$0.4 million and \$0.3 million, respectively, to Shidler LP for the annual fee. See Note 8 for more discussion on the FHB Credit Facility.

On May 17, 2010, the Operating Partnership entered into an amendment to its indemnity agreement dated as of March 19, 2008 with James C. Reynolds. Pursuant to the original agreement, the Operating Partnership agreed to indemnify Mr. Reynolds with respect to all of his obligations under certain guaranties provided by Mr. Reynolds to lenders of indebtedness encumbering the Contributed Properties. Pursuant to the amendment, the Operating Partnership agreed to indemnify Mr. Reynolds with respect to guaranties provided by him with respect to indebtedness encumbering certain additional properties acquired after the completion of our formation transactions. Mr. Reynolds is the beneficial owner of approximately 12% of our Listed Common Stock, and was a director and stockholder of our Advisor prior to our acquisition of our Advisor.

At September 30, 2011 and December 31, 2010, \$5.6 million and \$4.3 million of accrued interest attributable to unsecured notes payable to related parties, respectively, is included in accounts payable and other liabilities in the accompanying consolidated balance sheets. See Note 9 for a detailed discussion on these notes payable.

At September 30, 2011, we have \$0.4 million of amounts receivable from related parties included in rents and other receivables on our consolidated balance sheets, which primarily consist of unpaid property management fees and lease commission fees from our joint ventures. These amounts are a direct result of the internalization of the Advisor. See Note 12 for additional discussion of transactions with our Advisor.

14. Share-Based Payments

On May 21, 2008, the Board of Directors of the Company adopted the 2008 Directors' Stock Plan, as amended and restated (the "2008 Directors' Plan"), subject to stockholder approval. The Company reserved 150,000 shares of the Company's Listed Common Stock under the 2008 Directors' Plan for the issuance of stock options, restricted stock awards, stock appreciation rights

Pacific Office Properties Trust, Inc.
Notes to Consolidated Financial Statements

and performance awards. The 2008 Directors' Plan was approved by our stockholders at our annual meeting of stockholders on May 12, 2009.

On June 19, 2009, the Company issued restricted stock units representing 52,630 shares under the 2008 Directors' Plan, which awards vested on the first anniversary of the grant date. The grant date fair value of each restricted stock unit was \$3.80, which was the Company's closing stock price on June 19, 2009.

On June 16, 2010, the Company issued restricted stock units representing 47,615 shares under the 2008 Directors' Plan, 38,092 of which awards vested on the first anniversary of the grant date. The grant date fair value of each restricted stock unit was \$4.20, which was the Company's closing stock price on June 16, 2010. On March 4, 2011, Thomas R. Hislop resigned from the Company's Board of Directors. Upon resignation, he forfeited 9,523 shares of unvested restricted stock units that were granted in 2010. Accordingly, the Company reversed the stock compensation expense recognized related to these forfeited shares.

The Company did not issue any restricted stock units in 2011. As of September 30, 2011, all of our share-based payments to directors have vested. In connection with these grants, the Company recorded \$0 and \$50,000, respectively, of stock-based compensation expense for the three months ended September 30, 2011 and 2010. The Company recorded \$60,000 and \$150,000 of stock-based compensation expense for the nine months ended September 30, 2011 and 2010, respectively. These amounts are included in general and administrative expenses in the accompanying consolidated statement of operations.

15. Segment Reporting

We own and operate primarily institutional-quality office properties principally in selected long-term growth markets in southern California and Hawaii. We aggregate our operations by geographic region into two reportable segments (Honolulu and the Western United States mainland) based on the similar economic characteristics of the properties located in each of these regions. The products at all our properties include primarily rental of office space and other tenant services, including parking and storage space rental. We also have certain corporate level income and expenses related to our credit facility and legal, accounting, finance and management activities, which are not considered separate operating segments.

The following tables summarize the statements of operations by region of our wholly-owned consolidated properties for the three and nine months ended September 30, 2011 and 2010 (in thousands):

	For the three months ended September 30, 2011			
	Honolulu	Western U.S.	Corporate	Total
Revenue:				
Rental	\$ 7,080	\$ 133	\$ 20	\$ 7,233
Tenant reimbursements	5,123	43	—	5,166
Property management and other services	—	—	1,300	1,300
Parking	1,633	—	—	1,633
Other	60	11	50	121
Total revenue	13,896	187	1,370	15,453
Expenses:				
Rental property operating	7,839	75	—	7,914
General and administrative	—	—	2,395	2,395
Depreciation and amortization	3,620	97	—	3,717
Interest	5,108	502	696	6,306
Acquisition costs	—	—	12	12
Total expenses	16,567	674	3,103	20,344
Loss before equity in net loss of unconsolidated joint ventures	\$ (2,671)	\$ (487)	\$ (1,733)	(4,891)
Equity in net loss of unconsolidated joint ventures				(1,121)
Net loss attributable to non-controlling interests				4,912
Dividends on Senior Common Stock				(437)
Net loss attributable to common stockholders				\$ (1,537)

Pacific Office Properties Trust, Inc.
Notes to Consolidated Financial Statements

	For the nine months ended September 30, 2011			Total
	Honolulu	Western U.S.	Corporate	
Revenue:				
Rental	\$ 21,734	\$ 4,048	\$ 55	\$ 25,837
Tenant reimbursements	15,054	343	—	15,397
Property management and other services	—	—	3,533	3,533
Parking	5,106	323	—	5,429
Other	689	56	268	1,013
Total revenue	42,583	4,770	3,856	51,209
Expenses:				
Rental property operating	23,315	2,537	—	25,852
General and administrative	—	—	8,029	8,029
Depreciation and amortization	10,996	1,805	—	12,801
Interest	15,581	2,405	2,049	20,035
Abandoned offering costs	—	—	420	420
Acquisition costs	—	—	279	279
Impairment on long-lived assets	5,049	9,735	—	14,784
Total expenses	54,941	16,482	10,777	82,200
Loss before gain on forgiveness of debt, equity in net loss of unconsolidated joint ventures and non-operating income	<u>\$ (12,358)</u>	<u>\$ (11,712)</u>	<u>\$ (6,921)</u>	(30,991)
Gain on forgiveness of debt				10,045
Equity in net loss of unconsolidated joint ventures				(2,515)
Non-operating income				507
Net loss attributable to non-controlling interests				18,618
Dividends on Senior Common Stock				(1,312)
Net loss attributable to common stockholders				<u>\$ (5,648)</u>

Pacific Office Properties Trust, Inc.
Notes to Consolidated Financial Statements

	For the three months ended September 30, 2010			Total
	Honolulu	Western U.S.	Corporate	
Revenue:				
Rental	\$ 7,776	\$ 3,096	\$ 4	\$ 10,876
Tenant reimbursements	5,046	278	—	5,324
Parking	1,782	243	—	2,025
Other	32	8	51	91
Total revenue	14,636	3,625	55	18,316
Expenses:				
Rental property operating	8,161	2,007	—	10,168
General and administrative	—	—	687	687
Depreciation and amortization	3,929	1,720	—	5,649
Interest	5,996	2,469	668	9,133
Acquisition costs	—	—	630	630
Total expenses	18,086	6,196	1,985	26,267
Loss before equity in net earnings of unconsolidated joint ventures	\$ (3,450)	\$ (2,571)	\$ (1,930)	(7,951)
Equity in net earnings of unconsolidated joint ventures				140
Net loss attributable to non-controlling interests				6,049
Dividends on Senior Common Stock				(49)
Net loss attributable to common stockholders				\$ (1,811)

	For the nine months ended September 30, 2010			Total
	Honolulu	Western U.S.	Corporate	
Revenue:				
Rental	\$ 22,253	\$ 9,357	\$ 11	\$ 31,621
Tenant reimbursements	15,887	855	—	16,742
Parking	5,367	726	—	6,093
Other	95	22	150	267
Total revenue	43,602	10,960	161	54,723
Expenses:				
Rental property operating	24,368	5,517	—	29,885
General and administrative	—	—	2,091	2,091
Depreciation and amortization	11,837	5,341	—	17,178
Interest	16,629	4,121	1,830	22,580
Acquisition costs	—	—	630	630
Total expenses	52,834	14,979	4,551	72,364
Loss before equity in net earnings of unconsolidated joint ventures	\$ (9,232)	\$ (4,019)	\$ (4,390)	(17,641)
Equity in net earnings of unconsolidated joint ventures				184
Net loss attributable to non-controlling interests				13,409
Dividends on Senior Common Stock				(53)
Net loss attributable to common stockholders				\$ (4,101)

Pacific Office Properties Trust, Inc.
Notes to Consolidated Financial Statements

The following table summarizes total assets, goodwill and capital expenditures, by region, of our wholly-owned consolidated properties as of September 30, 2011 and December 31, 2010 (in thousands):

	Honolulu	Western U.S.	Corporate	Total
Total assets:				
September 30, 2011	\$ 352,313	\$ 9,872	\$ 10,579	\$ 372,764
December 31, 2010	\$ 375,645	\$ 73,351	\$ 19,389	\$ 468,385
Total goodwill:				
September 30, 2011	\$ 48,549	\$ —	\$ —	\$ 48,549
December 31, 2010	\$ 48,549	\$ —	\$ —	\$ 48,549
Capital expenditures				
For the three month period ended:				
September 30, 2011	\$ 1,223	\$ —	\$ —	\$ 1,223
September 30, 2010	\$ 1,402	\$ 69	\$ —	\$ 1,471
For the nine month period ended:				
September 30, 2011	\$ 2,652	\$ 37	\$ —	\$ 2,689
September 30, 2010	\$ 6,843	\$ 126	\$ —	\$ 6,969

16. Fair Value of Financial Instruments

We are required to disclose fair value information about all financial instruments, whether or not recognized in the balance sheet, for which it is practicable to estimate fair value. We measure and disclose the estimated fair value of financial assets and liabilities utilizing a fair value hierarchy that distinguishes between data obtained from sources independent of the reporting entity and the reporting entity's own assumptions about market participant assumptions. This hierarchy consists of three broad levels as follows: 1) using quoted prices in active markets for identical assets or liabilities, 2) "significant other observable inputs" and 3) "significant unobservable inputs." "Significant other observable inputs" can include quoted prices for similar assets or liabilities in active markets, as well as inputs that are observable for the asset or liability, such as interest rates, foreign exchange rates and yield curves that are observable at commonly quoted intervals. "Significant unobservable inputs" are typically based on an entity's own assumptions, since there is little, if any, related market activity. In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety. Our assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the asset or liability. The fair market value of debt is determined using the trading price of public debt or a discounted cash flow technique that incorporates a market interest yield curve with adjustments for duration, optionality and risk profile, including the Company's non-performance risk. Considerable judgment is necessary to interpret market data and develop estimated fair value. The use of different market assumptions or estimation methods may have a material effect on the estimated fair value amounts.

The carrying amounts for cash and cash equivalents, restricted cash, rents and other receivables, accounts payable and other liabilities approximate fair value because of the short-term nature of these instruments. We calculate the fair value of our mortgage and other loans, and unsecured notes payable by using "significant other observable inputs" such as available market information and discounted cash flows analyses based on borrowing rates we believe we could obtain with similar terms and maturities. Because the valuations of our financial instruments are based on these types of estimates, the actual fair value of our financial instruments may differ materially if our estimates do not prove to be accurate. Additionally, the use of different market assumptions or estimation methods may have a material effect on the estimated fair value amounts. The carrying value of the FHB Credit Facility approximates its fair value.

At September 30, 2011, the carrying value (excluding accrued interest) and estimated fair value of the mortgage and other loans were \$356.2 million and \$355.7 million, respectively. At December 31, 2010, the carrying value (excluding accrued interest) and estimated fair value of the mortgage and other loans (excluding the Pacific Business News Building and City Square loans in default at that date with a total carrying value of \$64.4 million for which we could not practically determine the fair value) were \$355.7 million and \$342.2 million, respectively.

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Notes to Consolidated Financial Statements

17. Subsequent Events

On October 14, 2011 one of our unconsolidated joint ventures completed the sale of one of its properties, Palomar Heights Corporate Center, to an unrelated third party. Net proceeds of the transaction, after repayment of mortgage indebtedness, were used to pay down other joint venture debt with the balance retained for working capital purposes. We are not expecting to receive a return of a portion of our equity investment from the transaction.

On October 17, 2011, we received a payment of \$0.6 million representing payment in full of principal and accrued interest on advances we made in the second quarter of 2011 under a short-term financing arrangement with the aforementioned unconsolidated joint venture. The advances bore interest at the annual rate of 12%, compounded annually, and were scheduled to mature in November 2011. At September 30, 2011, the note receivable and related interest were included in Rents and other receivables, net in the accompanying consolidated balance sheets.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with the consolidated financial statements and the related notes thereto that appear in Item 1 of this Quarterly Report on Form 10-Q.

Note Regarding Forward-Looking Statements -

Our disclosure and analysis in this Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), which include information relating to future events, future financial performance, strategies, expectations, risks and uncertainties. From time to time, we also provide forward-looking statements in other materials we release to the public as well as oral forward-looking statements. These forward-looking statements include, without limitation, statements regarding: projections, predictions, expectations, estimates or forecasts as to our business, financial and operational results and future economic performance; statements regarding strategic transactions such as mergers or acquisitions or a possible dissolution of the Company; and statements of management's goals and objectives and other similar expressions. Such statements give our current expectations or forecasts of future events; they do not relate strictly to historical or current facts. Words such as "believe," "assume," "may," "will," "should," "could," "would," "predict," "potential," "continue," "plan," "anticipate," "estimate," "expect," "intend," "objective," "seek," "strive" and similar expressions, as well as statements in future tense, identify forward-looking statements.

Certain matters discussed in this Quarterly Report on Form 10-Q are forward-looking statements. The risks and uncertainties inherent in such statements may cause actual future events or results to differ materially and adversely from those described in the forward-looking statements.

We cannot guarantee that any forward-looking statement will be realized. Achievement of future results is subject to risks, uncertainties and potentially inaccurate assumptions. Should known or unknown risks or uncertainties materialize, or should underlying assumptions prove inaccurate, actual results could differ materially from past results and those anticipated, estimated or projected. These factors include the risks and uncertainties described in "Risk Factors" in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2010 and in Item 1A, "Risk Factors," in this Quarterly Report on Form 10-Q. You should bear this in mind as you consider forward-looking statements.

We undertake no obligation to publicly update forward-looking statements, whether as a result of new information, future events or otherwise. You are advised, however, to consult any further disclosures we make on related subjects in our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K filed with the SEC.

Overview –

We are a self-administered and self-managed REIT that owns and operates primarily institutional-quality office properties principally in selected long-term growth markets in southern California and Hawaii. As of September 30, 2011, we owned six office properties comprising approximately 1.5 million rentable square feet. At that date, we also owned interests (ranging from 5% to approximately 32.2%) in 19 joint venture properties, of which we have managing ownership interests in 15, comprising approximately 3.5 million rentable square feet.

During 2010 and January 2011, we were externally advised by Pacific Office Management, Inc., referred to as our Advisor, an entity that was owned and controlled by Jay H. Shidler, our Chairman of the Board, and certain of our executive officers and related parties of The Shidler Group, which is a business name utilized by a number of affiliates of Mr. Shidler. The Advisor was responsible for the day-to-day operation and management of the Company. Effective as of February 1, 2011, we acquired all of the outstanding stock of our Advisor for an aggregate purchase price of \$25,000 and internalized management.

We were formed in 2008 as a continuation of The Shidler Group's successful 30-year history of operations in the western United States and Hawaii. Our formation was accomplished through a reverse merger into a publicly traded REIT, Arizona Land Income Corporation, whose common stock was listed and traded on the American Stock Exchange. Concurrent with the merger, we changed our name to Pacific Office Properties Trust, Inc. and reincorporated in the State of Maryland.

We maintain a website at www.pacificofficeproperties.com. Information on this website shall not constitute part of this Form 10-Q. Copies of our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to such reports are available without charge on our website. In addition, our Corporate Governance Guidelines, Code of Business Conduct and Ethics, Audit Committee Charter, Compensation Committee Charter and Nominating and Corporate Governance Committee Charter are all available without charge on our website or upon request to us. We also post

Pacific Office Properties Trust, Inc.

or otherwise make available on our website from time to time other information that may be of interest to our investors.

Property Portfolio –

As of September 30, 2011, we owned 25 office properties, including the interests in our joint venture properties, comprising approximately 5.0 million rentable square feet in 48 buildings. The following table presents an overview of our Property Portfolio, based on information as of September 30, 2011:

PROPERTY	NO. OF BUILDINGS	RENTABLE SQ. FT.	PERCENTAGE OWNERSHIP	ANNUALIZED RENT ⁽¹⁾
Wholly-Owned Properties				
Waterfront Plaza				
500 Ala Moana Blvd. Honolulu, HI 96813	1	554,695	100.0%	\$ 18,967,238
Davies Pacific Center				
841 Bishop Street Honolulu, HI 96813	1	375,021	100.0%	9,439,379
Pan Am Building				
1600 Kapiolani Blvd. Honolulu, HI 96814	1	225,876	100.0%	6,939,331
First Insurance Center				
1100 Ward Avenue Honolulu, HI 96814	1	215,527	100.0%	7,450,427
Clifford Center				
810 Richards Street Honolulu, HI 96813	1	77,655	100.0%	1,811,457
Sorrento Technology Center				
10140 Barnes Canyon Rd. 10180 Barnes Canyon Rd. San Diego, CA 92121	2	63,363	100.0%	676,381
Total Wholly-Owned Properties	7	1,512,137		\$ 45,284,213

Pacific Office Properties Trust, Inc.

PROPERTY	NO. OF BUILDINGS	RENTABLE SQ. FT.	PERCENTAGE OWNERSHIP	ANNUALIZED RENT ⁽¹⁾⁽²⁾
Joint Venture Properties				
Savi Tech Center				
22705 Savi Ranch Pkwy.	4	371,098	10.0%	\$ 7,047,987
22715 Savi Ranch Pkwy.				
22725 Savi Ranch Pkwy.				
22745 Savi Ranch Pkwy.				
Yorba Linda, CA 92887				
Yorba Linda Bus. Park				
22833 La Palma Ave.	5	164,121	10.0%	1,500,147
22343 La Palma Ave.				
22345 La Palma Ave.				
22347 La Palma Ave.				
22349 La Palma Ave.				
Yorba Linda, CA 92887				
Torrey Hills Corp. Center				
11250 El Camino Real	1	23,478	32.2%	111,153
San Diego, CA 92130				
Palomar Heights Plaza				
5860 Owens Avenue	3	45,538	32.2%	704,892
5868 Owens Avenue				
5876 Owens Avenue				
Carlsbad, CA 92008				
Palomar Heights Corp. Center ⁽³⁾				
5857 Owens Avenue	1	67,862	32.2%	1,426,518
Carlsbad, CA 92008				
Scripps Ranch Bus. Park				
9775 Business Park Ave.	2	48,146	32.2%	912,965
10021 Willow Creek Rd.				
San Diego, CA 92131				
Via Frontera Bus. Park				
10965 Via Frontera Dr.	2	75,651	10.0%	727,481
10993 Via Frontera Dr.				
San Diego, CA 92127				
Poway Flex				
13550 Stowe Drive	1	111,258	10.0%	1,501,966
Poway, CA 92064				
Carlsbad Corp. Center.				
1950 Camino Vida Roble	1	120,483	10.0%	2,465,796

Pacific Office Properties Trust, Inc.

PROPERTY	NO. OF BUILDINGS	RENTABLE SQ. FT.	PERCENTAGE OWNERSHIP	ANNUALIZED RENT⁽¹⁾⁽²⁾
South Coast Exec. Center 1503 South Coast Dr. Costa Mesa, CA 92626	1	60,798	10.0%	894,093
Gateway Corp. Center 1370 Valley Vista Dr. Diamond Bar, CA 91765	1	85,048	10.0%	1,745,367
Black Canyon Corp. Ctr. 16404 N. Black Canyon Hwy. Phoenix, AZ 85053	1	218,694	17.5%	3,105,523
Bank of Hawaii Waikiki Center 2155 Kalakaua Avenue Honolulu, HI 96815	1	152,288	17.5%	7,420,064
Seville Plaza 5469 Kearny Villa Rd. 5471 Kearny Villa Rd. 5473 Kearny Villa Rd. San Diego, CA 92123	3	139,335	7.5%	2,142,143
U.S. Bank Center 101 North First Ave. 21 West Van Buren St. Phoenix, AZ 85003	2	372,606	7.5%	6,346,850
Pacific Business News Building 1833 Kalakaua Avenue Honolulu, HI 96815	1	97,467	5.0%	1,914,976
Valencia Corporate Center 28470 Avenue Stanford 28480 Avenue Stanford 28490 Avenue Stanford Santa Clarita, CA 91355	3	194,268	5.0%	4,431,493
City Square 3800 N. Central Ave. 3838 N. Central Ave. 4000 N. Central Ave. Phoenix, AZ 85012	3	750,331	5.0%	10,593,069
Seaview Corporate Center 10180 Telesis Court 10190 Telesis Court 10182 Telesis Court	5	355,813	5.0%	10,220,455

Total Joint Venture Properties	<u>41</u>	<u>3,454,283</u>	<u>\$ 65,212,938</u>
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Pacific Office Properties Trust, Inc.

1. Annualized rent represents the monthly contractual rent under commenced leases as of September 30, 2011. This amount reflects total rent before abatements and includes contractual expense reimbursements, which are estimated by annualizing September 2011 actual expense reimbursement billings. Total abatements committed to as of September 30, 2011 for the 12 months ending September 30, 2012 were approximately \$0.4 million for our wholly-owned properties and \$2.0 million for our joint venture properties.
2. Annualized rent for the joint venture properties is reported with respect to each property in its entirety, rather than the portion of the property represented by our ownership interest. No portion of the joint venture properties' annualized rent is consolidated in our consolidated financial statements because our interests in our joint venture properties are accounted for under the equity method of accounting.
3. Subsequent to September 30, 2011, the joint venture owning this property sold the property to an unrelated third party. Net proceeds of the transaction, after repayment of mortgage indebtedness, were used to pay down other joint venture debt with the balance retained for working capital purposes. We are not expecting to receive a return of a portion of our equity investment from the transaction.

Critical Accounting Policies -

This discussion and analysis of the historical financial condition and results of operations is based upon the accompanying consolidated financial statements which have been prepared in accordance with GAAP. The preparation of these financial statements in conformity with GAAP requires management to make estimates and assumptions in certain circumstances that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses in the reporting period. Actual amounts may differ from these estimates and assumptions. These estimates have been evaluated on an ongoing basis, based upon information currently available and on various assumptions that management believes are reasonable as of the date hereof. In addition, other companies in similar businesses may use different estimation policies and methodologies, which may impact the comparability of the results of operations and financial conditions to those of other companies.

In addition, we identified certain critical accounting policies that affect our more significant estimates and assumptions used in preparing our consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2010. We have not made any material changes to those policies during the period covered by this Quarterly Report on Form 10-Q.

Results of Operations

Our results of operations for the three and nine months ended September 30, 2011 compared to the same periods in 2010 were significantly affected by the contribution of two of our wholly-owned properties, City Square and the Pacific Business News Building, into joint ventures with a third party ("Contribution Properties"). As a result, our results are not comparable from period to period. Therefore, in the tables below, we have also separately presented the results of our "Same Properties Portfolio."

Our Same Properties Portfolio includes the results of our wholly-owned properties as of September 30, 2011 (specifically our five properties located in Honolulu, Hawaii - Waterfront Plaza, First Insurance Center, Davies Pacific Center, Clifford Center and the Pan-Am Building - and our Sorrento Technology Center property in San Diego, California). Our discussion of the results of our Same Properties Portfolio excludes the effects of the internalization of the Advisor.

Overview –

As of September 30, 2011, the Property Portfolio (including our consolidated and joint venture properties) was 81.4% leased to a total of 733 tenants. Approximately 5.0% of our Property Portfolio leased square footage was scheduled to expire during the remainder of 2011 and another 13.7% of our Property Portfolio leased square footage was scheduled to expire during 2012. We receive income primarily from rental revenue (including tenant reimbursements) from our office properties and, to a lesser extent, from our parking revenues. Our office properties are typically leased to tenants with good credit for terms ranging from two to 20 years.

As of September 30, 2011, our consolidated Honolulu portfolio was 88.0% leased, with approximately 165,400 square feet available. Our Honolulu portfolio attributable to our unconsolidated joint ventures was 77.4% leased, with approximately 54,700 square feet available.

Pacific Office Properties Trust, Inc.

As of September 30, 2011, our consolidated San Diego portfolio, which consists of our Sorrento Technology Center property, was 40.2% leased. Our San Diego portfolio attributable to our unconsolidated joint ventures was 82.3% leased, with approximately 175,200 square feet available.

As of September 30, 2011, our Phoenix portfolio attributable to our unconsolidated joint ventures was 71.8% leased, with approximately 370,600 square feet available.

Comparison of the three months ended September 30, 2011 to the three months ended September 30, 2010 (in thousands)

	Same Properties				Total Portfolio			
	2011	2010	\$ Change	% Change	2011	2010	\$ Change	% Change
Revenue:								
Rental	\$ 7,326	\$ 7,847	\$ (521)	(6.6)%	\$ 7,233	\$ 10,876	\$ (3,643)	(33.5)%
Tenant reimbursements	5,167	4,851	316	6.5 %	5,166	5,324	(158)	(3.0)%
Property management and other services	—	—	—	N/A	1,300	—	1,300	100.0 %
Parking	1,633	1,598	35	2.2 %	1,633	2,025	(392)	(19.4)%
Other	113	83	30	36.1 %	121	91	30	33.0 %
Total revenue	14,239	14,379	(140)	(1.0)%	15,453	18,316	(2,863)	(15.6)%
Expenses:								
Rental property operating	8,327	7,765	562	7.2 %	7,914	10,168	(2,254)	(22.2)%
General and administrative	637	687	(50)	(7.3)%	2,395	687	1,708	248.6 %
Depreciation and amortization	3,717	3,913	(196)	(5.0)%	3,717	5,649	(1,932)	(34.2)%
Interest	6,306	5,967	339	5.7 %	6,306	9,133	(2,827)	(31.0)%
Acquisition costs	—	630	(630)	100.0 %	12	630	(618)	(98.1)%
Total expenses	18,987	18,962	25	0.1 %	20,344	26,267	(5,923)	(22.5)%
Loss before equity in net earnings (loss) of unconsolidated joint ventures	(4,748)	(4,583)	(165)	3.6 %	(4,891)	(7,951)	3,060	(38.5)%
Equity in net earnings (loss) of unconsolidated joint ventures	(1,121)	140	(1,261)	(900.7)%	(1,121)	140	(1,261)	(900.7)%
Net loss	\$ (5,869)	\$ (4,443)	\$ (1,426)	32.1 %	\$ (6,012)	\$ (7,811)	\$ 1,799	(23.0)%

Revenues

Rental Revenue. Total rental revenue decreased by \$3.6 million, or 33.5%, primarily due to the elimination of the Contribution Properties. Rental revenue for the Same Properties Portfolio decreased \$0.5 million, or 6.6%, which is primarily due to decreased occupancy at our Waterfront Plaza property (\$0.1 million) and our Davies Pacific Center (\$0.1 million) in Hawaii. In addition, we experienced a reduction in rental revenue at Sorrento Technology Center (\$0.2 million) because a large tenant moved out on December 31, 2010 and we have not yet re-leased the space.

Tenant Reimbursements. Total tenant reimbursements decreased by \$0.2 million, or 3.0%, primarily due to the elimination of the Contribution Properties. Tenant reimbursements for the Same Properties Portfolio increased by \$0.3 million, or 6.5%. The increase in tenant reimbursements for the Same Properties Portfolio was primarily due to an increase in recoverable electric utility expenses and other common area maintenance costs at our First Insurance Center and Waterfront Plaza properties in Hawaii.

Property Management and Other Services. We internalized management by acquiring our Advisor effective as of February 1, 2011. As a result, we began recognizing revenue related to property management and other services from our joint venture properties and other properties owned by related parties. We did not receive this revenue in the prior year period.

Parking Revenue. Total parking revenue decreased by \$0.4 million, or 19.4%, due to the elimination of our Contribution Properties. Parking revenue for the Same Properties Portfolio remained relatively constant for both periods presented.

Other Revenue. Total other revenue remained relatively constant on a Total Portfolio and Same Properties Portfolio basis for both periods presented.

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Expenses

Rental Property Operating Expenses. Total rental property operating expenses decreased by \$2.3 million, or 22.2%, due to the elimination of the Contribution Properties and a reduction in property management fees that are no longer paid to the Advisor as of February 1, 2011 (\$0.4 million was eliminated in consolidation during the quarter). Rental property operating expenses for our Same Properties Portfolio increased by \$0.6 million, or 7.2%, due to higher electricity costs at Waterfront Plaza (\$0.3 million), First Insurance Center (\$0.1 million) and the Pan Am Building (\$0.1 million) as a result of increased electricity rates. Expenses at Waterfront Plaza also included approximately \$0.1 million related to an abandoned building improvement project. There was no similar cost in the prior year period.

General and Administrative Expense. Total general and administrative expense increased by \$1.7 million, or 248.6%, due to the internalization of management effective as of February 1, 2011. We now employ our executive officers and other employees and are also responsible for all costs previously incurred by the Advisor in the management of our Company. On a Same Properties Portfolio basis, the Operating Partnership did not incur \$0.2 million in advisory fees in the current year period that were incurred in the prior year period due to the internalization. This reduction in expense was partially offset by an increase in professional fees associated with corporate initiatives.

Depreciation and Amortization Expense. Total depreciation and amortization expense decreased by \$1.9 million, or 34.2%, primarily due to the elimination of the Contribution Properties, but partially also due to our Same Properties Portfolio. Depreciation and amortization expense for our Same Properties Portfolio decreased by \$0.2 million, or 5.0%, due to lower expense attributable to the Sorrento Technology Center as a result of the real estate impairment charge taken in the second quarter of 2011. In addition, the decrease was partially due to the expiration of useful lives of certain intangible assets acquired pursuant to our formation transactions in 2008. We expect the amortization expense related to intangible assets acquired pursuant to our formation transactions in 2008 to continue to decrease as their useful lives expire. These decreases were partially offset by an increase in depreciation expense at Waterfront Plaza resulting from tenant improvement additions.

Interest Expense. Total interest expense decreased by \$2.8 million, or 31.0%, primarily due to the elimination of the Contribution Properties but partially offset by our Same Properties Portfolio. Interest expense for our Same Properties Portfolio increased by \$0.3 million, or 5.7%, primarily due to default interest incurred on our Sorrento Technology Center loan, with a principal balance of \$11.6 million, since May 2011.

Acquisition Costs. We incurred \$12 thousand in acquisition costs for the three months ended September 30, 2011 primarily in connection with the acquisition of the Valencia Corporate Center. We received a reimbursement of acquisition costs related to Valencia Corporate Center which is included in other revenue. For the three months ended September 30, 2010 we incurred \$0.6 million in acquisition costs primarily in connection the GRE portfolio (\$0.5 million) and a one-building office property located in San Diego, California (\$0.1 million).

Equity in net earnings of unconsolidated joint ventures

Equity in net earnings of unconsolidated joint ventures decreased by \$1.3 million for the three months ended September 30, 2011 compared to the three months ended September 30, 2010. During the quarter ended September 30, 2011, we recorded non-cash impairment charges to write down our investments in unconsolidated joint ventures that own the Black Canyon Corporate Center and the SoCal Portfolio, of \$0.06 million and \$1.1 million, respectively, as a result of uncertainty surrounding debt that is scheduled to mature in the first quarter of 2012 secured by the properties held by these joint ventures.

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Comparison of the nine months ended September 30, 2011 to the nine months ended September 30, 2010 (in thousands)

	Same Properties				Total Portfolio			
	2011	2010	\$ Change	% Change	2011	2010	\$ Change	% Change
Revenue:								
Rental	\$ 22,105	\$ 22,474	\$ (369)	(1.6)%	\$ 25,837	\$ 31,621	\$ (5,784)	(18.3)%
Tenant reimbursements	14,874	15,276	(402)	(2.6)%	15,397	16,742	(1,345)	(8.0)%
Property management and other services	—	—	—	N/A	3,533	—	3,533	100.0 %
Parking	4,917	4,789	128	2.7 %	5,429	6,093	(664)	(10.9)%
Other	751	244	507	207.8 %	1,013	267	746	279.4 %
Total revenue	42,647	42,783	(136)	(0.3)%	51,209	54,723	(3,514)	(6.4)%
Expenses:								
Rental property operating	24,158	23,235	923	4.0 %	25,852	29,885	(4,033)	(13.5)%
General and administrative	1,987	2,091	(104)	(5.0)%	8,029	2,091	5,938	284.0 %
Depreciation and amortization	11,235	11,923	(688)	(5.8)%	12,801	17,178	(4,377)	(25.5)%
Interest	18,179	17,562	617	3.5 %	20,035	22,580	(2,545)	(11.3)%
Abandoned offering costs	420	—	420	100.0 %	420	—	420	100.0 %
Acquisition costs	255	630	(375)	(59.5)%	279	630	(351)	(55.7)%
Impairment of long-lived assets	3,328	—	3,328	100.0 %	14,784	—	14,784	100.0 %
Total expenses	59,562	55,441	4,121	7.4 %	82,200	72,364	9,836	13.6 %
Loss before gain on forgiveness of debt, equity in net earnings (loss) of unconsolidated joint ventures and non-operating income	(16,915)	(12,658)	(4,257)	33.6 %	(30,991)	(17,641)	(13,350)	75.7 %
Gain on forgiveness of debt	—	—	—	N/A	10,045	—	10,045	100.0 %
Equity in net earnings (loss) of unconsolidated joint ventures	(2,515)	184	(2,699)	(1,466.8)%	(2,515)	184	(2,699)	(1,466.8)%
Non-operating income	—	—	—	N/A	507	—	507	100.0 %
Net loss	\$ (19,430)	\$ (12,474)	\$ (6,956)	55.8 %	\$ (22,954)	\$ (17,457)	\$ (5,497)	31.5 %

Revenues

Rental Revenue. Total rental revenue decreased by \$5.8 million, or 18.3%, primarily due to the elimination of the Contribution Properties. Rental revenue for the Same Properties Portfolio decreased \$0.4 million, or 1.6%, which is primarily due to decreased occupancy at Davies Pacific Center (\$0.5 million) and the Pan Am Building (\$0.3 million) offset by increased occupancy at our Waterfront Plaza property (\$1.0 million). In addition, we experienced a reduction in rental revenue at Sorrento Technology Center (\$0.6 million) because a large tenant moved out on December 31, 2010 and we have not yet re-leased the space.

Tenant Reimbursements. Total tenant reimbursements decreased by \$1.3 million, or 8.0% due to the elimination of the Contribution Properties and partially due to decreased tenant reimbursements for our Same Properties Portfolio. Tenant reimbursements for the Same Properties Portfolio decreased by \$0.4 million, or 2.6%, primarily due to decreased occupancy at Clifford Center (\$0.1 million), Davies Pacific Center (\$0.2 million) and Sorrento Technology Center (\$0.2 million) and because the 2010 period included an adjustment for 2009 recoverable revenue (\$0.5 million). We did not have a prior year adjustment in the current year period because our estimated reimbursement revenue was closer to actual amounts. These decreases were offset by an increase in recoverable electric utility expenses and other common area maintenance costs at our First Insurance Center (\$0.2 million) and Waterfront Plaza (\$0.4 million) properties.

Property Management and Other Services. We internalized management by acquiring our Advisor effective as of February 1, 2011. As a result, we began recognizing revenue related to property management and other services from our joint venture properties and other properties owned by related parties. We did not receive this revenue in the prior year period.

Parking Revenue. Total parking revenue decreased by \$0.7 million, or 10.9%, primarily due to the elimination of our Contribution Properties. Parking revenue for the Same Properties Portfolio increased by \$0.1 million, or 2.7%, due to increased

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revenue at Waterfront Plaza, which was a result of increased occupancy.

Other Revenue. Total other revenue increased by \$0.7 million, or 279.4%, due to the internalization of our Advisor and our Same Properties Portfolio. Other revenue for the Same Properties Portfolio increased by \$0.5 million, or 207.8%, primarily due to a termination fee received from a tenant who signed a lease termination agreement at our Davies Pacific Center property during the current year period.

Expenses

Rental Property Operating Expenses. Total rental property operating expenses decreased by \$4.0 million, or 13.5%, due to the elimination of the Contribution Properties and a reduction in property management fees that are no longer paid to the Advisor as of February 1, 2011 (\$1.2 million was eliminated in consolidation during the nine month period). Rental property operating expenses for our Same Properties Portfolio increased by \$0.9 million, or 4.0%, due to higher electricity costs at Waterfront Plaza, First Insurance Center and the Pan Am Building as a result of increased electricity rates and increased occupancy. Expenses at Waterfront Plaza in the current year period also included (\$0.1 million) related to an abandoned building improvement project. There was no similar cost in the prior year period.

General and Administrative Expense. Total general and administrative expense increased by \$5.9 million, or 284.0%, due to the internalization of management effective as of February 1, 2011. We now employ our executive officers and other employees and are also responsible for all costs previously incurred by the Advisor in the management of our Company.

Depreciation and Amortization Expense. Total depreciation and amortization expense decreased by \$4.4 million, or 25.5%, primarily due to the elimination of the Contribution Properties and in part, due to the Same Properties Portfolio. Depreciation and amortization expense for our Same Properties Portfolio decreased by \$0.7 million, or 5.8%, due to lower expense attributable to the Sorrento Technology Center as a result of the real estate impairment charge taken in the second quarter of 2011. In addition, the decrease was also partially due to the expiration of useful lives of certain intangible assets acquired pursuant to our formation transactions in 2008. We expect the amortization expense related to intangible assets acquired pursuant to our formation transactions in 2008 to continue to decrease as their useful lives expire. These decreases were partially offset by an increase in depreciation expense at Waterfront Plaza resulting from tenant improvement additions.

Interest Expense. Total interest expense decreased by \$2.5 million, or 11.3%, primarily due to the elimination of the Contribution Properties. Interest expense for our Same Properties Portfolio increased by \$0.6 million, or 3.5%, primarily due to default interest incurred on our Sorrento Technology Center loan, with a principal balance of \$11.6 million, since May 2011, and additional interest expense on our credit facility due to a higher outstanding balance during the current year period.

Abandoned Offering Costs. We incurred \$0.4 million in abandoned offering costs for the nine months ended September 30, 2011 in connection with an unsuccessful public offering of Listed Common Stock.

Acquisition Costs. We incurred \$0.3 million in acquisition costs for the nine months ended September 30, 2011 primarily in connection with the contribution of our Pacific Business News and City Square properties into joint ventures and a terminated acquisition of the GRE portfolio, a portfolio of 12 office properties comprising approximately 1.9 million rentable square feet located primarily in southern California. For the nine months ended September 30, 2010 we incurred \$0.6 million in acquisition costs primarily in connection the GRE portfolio (\$0.5 million) and a one-building office property located in San Diego, California (\$0.1 million).

Impairment of Long-Lived Assets. We recognized \$14.8 million in impairment of long-lived assets for the nine months ended September 30, 2011, primarily due to the Contribution Properties. We determined that the fair value of the Contribution Properties were higher than the respective book values and as a result, we recorded non-cash asset impairment charges of \$5.1 million and \$6.4 million related to our Pacific Business News Building and City Square properties, respectively. In addition, we determined that the holding period for our Sorrento Technology Center property needed to be shortened due to the uncertainty surrounding the defaulted debt secured by this asset. As a result, we recorded a non-cash asset impairment charge of \$3.3 million.

Gain on forgiveness of debt

We recognized a gain on forgiveness of debt related to the defaulted debt secured by the Contribution Properties. We negotiated discounted payoff amounts for the Pacific Business News Building mortgage loan and the City Square Mezzanine Loan. As part of the agreement, principal and interest amounts totaling \$2.6 million and \$7.4 million, respectively, were forgiven. The joint ventures that each property was contributed into repaid these loans at the negotiated discounted amounts.

Equity in net earnings of unconsolidated joint ventures

Equity in net earnings of unconsolidated joint ventures decreased by \$2.7 million for the nine months ended September 30, 2011 compared to the nine months ended September 30, 2010. During the nine months ended September 30, 2011, the debt secured by our US Bank property matured and as a result of the uncertainty surrounding the defaulted debt, we recorded a non-cash impairment charge of approximately \$1.4 million to write off our investment in the unconsolidated joint venture that owns our US Bank property. In addition, during the nine months ended September 30, 2011, we recorded non-cash impairment charges to write down our investments in the unconsolidated joint ventures that own the Black Canyon Corporate Center and the SoCal Portfolio, of \$0.06 million and \$1.1 million, respectively, as a result of uncertainty surrounding debt that is scheduled to mature in the first quarter of 2012 secured by the properties held by these joint ventures.

Non-operating income

We recognized non-operating income of \$0.5 million during the nine months ended September 30, 2011 resulting from the internalization of our Advisor. The purchase price of \$25,000 for our Advisor was less than the fair value of the assets acquired and liabilities assumed resulting in a bargain purchase which is recognized as a gain on the acquisition date. The gain resulted in part because previously unpaid amounts due from the wholly-owned properties were eliminated upon consolidation. The gain calculation and purchase accounting were finalized during the second quarter of 2011. We did not recognize any comparable income during the nine months ended September 30, 2010.

Liquidity and Capital Resources

Liquidity is a measure of our ability to meet potential cash requirements, including ongoing commitments to repay borrowings, fund and maintain our assets and operations, make distributions to our stockholders and other general business needs. In order to qualify as a REIT, we must distribute to our stockholders, each calendar year, at least 90% of our REIT taxable income. As discussed further below, however, we have not declared and do not currently expect to declare dividends on our Listed Common Stock during fiscal 2011.

Our business is capital intensive and our ability to maintain our operations depends on our cash flow from operations and our ability to raise additional capital on acceptable terms. Our primary focus is to preserve and generate cash.

We expect to meet our short-term liquidity and capital requirements primarily through existing cash on hand, net cash provided by operating activities, the contribution of existing wholly-owned assets to joint ventures or asset dispositions. We expect to meet our long-term capital requirements through net cash provided by operating activities, borrowings under our revolving credit facility (if available), refinancing of existing debt or through other available investment and financing activities, including the contribution of existing wholly-owned assets to joint ventures (partial sell-down of equity interests in wholly-owned assets) or asset dispositions. In February 2011, we terminated our registered continuous public offering of Senior Common Stock, so this offering is no longer a source of capital for us. In March 2011, we engaged Eastdil Secured to assist in the potential recapitalization of the Hawaii-based portfolio, which could include the contribution of existing wholly-owned assets to joint ventures or asset dispositions. In the second quarter of 2011, we contributed two wholly-owned properties, our Pacific Business News Building and City Square properties, to newly-formed joint ventures with Angelo Gordon & Co.

While we may be able to anticipate and plan for certain liquidity needs, there may be unexpected increases in uses of cash that are beyond our control and which would affect our financial condition and results of operations. For example, we may be required to comply with new laws or regulations that cause us to incur unanticipated capital expenditures for our properties, thereby increasing our liquidity needs. Even if there are no material changes to our anticipated liquidity requirements, our sources of liquidity may be fewer than, and the funds available from such sources may be less than, anticipated or needed.

Actual and Potential Sources of Liquidity

Listed below are our actual and potential sources of liquidity in 2011, which we currently believe will be sufficient to fund our 2011 liquidity needs:

- Unrestricted and restricted cash on hand;
- Net cash flow generated from operations;
- Contribution of existing wholly-owned assets to joint ventures;
- Asset dispositions; and/or

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- Proceeds, if available, from additional secured or unsecured debt financings.

These sources are essential to our short-term liquidity and financial position, and we cannot assure you that we will be able to successfully access them (particularly in the current economic environment). If we are unable to generate adequate cash from these sources, we will have liquidity-related problems and may be exposed to significant risks. For a further discussion of such risks, see “Risk Factors” in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2010 and in Item 1A of this Quarterly Report on Form 10-Q.

Unrestricted and restricted cash on hand

As of September 30, 2011, we had \$4.8 million in unrestricted cash and cash equivalents. In addition, we had restricted cash balances of \$4.5 million. A summary of our restricted cash reserves is as follows.

Tax, insurance and other working capital reserves	\$	1,858
Leasing and capital expenditure reserves		866
Ground lease reserves		1,055
Collateral accounts		766
	\$	<u>4,545</u>

The leasing and capital expenditure, tax, insurance and other working capital reserves are held in restricted accounts by our lenders in accordance with the terms of our mortgage loans. These restricted cash accounts are expected to fund (1) anticipated leasing expenditures (primarily commissions and tenant improvement costs) for existing and prospective tenants, (2) non-recurring discretionary capital expenditures, (3) payments for properties subject to ground leases and (4) property taxes and insurance. The collateral accounts are held by our lenders under our other obligations.

Net cash flow generated from operations

Our cash flows from operations depend significantly on market rents and the ability of our tenants to make rental payments. While we believe the diversity and high credit quality of our tenants help mitigate the risk of a significant interruption of our cash flows from operations, the challenging economic conditions that we are currently experiencing, the downward pressure on rental rates and occupancy in our Hawaii and mainland submarkets, the potential for an increase in interest rates, or the possibility for a further downturn in one of our concentration markets could adversely impact our operating cash flows. Competition to attract and retain high credit-quality tenants remains intense due to general economic conditions. At the same time, a significant number of our leases at our properties are scheduled to expire over the next three years, and the capital requirements necessary to maintain our current occupancy levels, including payment of leasing commissions, tenant concessions, and anticipated leasing expenditures, could increase. As such, we will continue to closely monitor our tenant renewals, rental rates, competitive market conditions and our cash flows.

Contribution of existing wholly-owned assets to joint ventures

We are currently partners with third parties in nine joint ventures, including two newly-formed joint ventures into which we contributed our Pacific Business News Building and City Square properties in the second quarter of 2011. In the near term or longer term, we may seek to raise capital by contributing additional wholly-owned assets to a joint venture with a third party. Investments in joint ventures may, under certain circumstances, involve risks not present were a third party not involved. Our ability to successfully identify, negotiate and close joint venture transactions on acceptable terms or at all is highly uncertain in the current economic environment.

Asset dispositions

In the near term or longer term, we may seek to raise additional capital by selling some or all of our existing wholly-owned assets, but our ability to do so on acceptable terms or at all is highly uncertain. Moreover, a sale of any of the properties contributed by POP Venture, LLC, or Venture, in connection with our formation transactions in March 2008 (specifically, our Waterfront Plaza, Davies Pacific Center, Pan Am Building, First Insurance Center, Pacific Business News Building, Clifford Center, Sorrento Technology Center, City Square and Seville Plaza properties) that would not provide continued tax deferral to Venture is contractually prohibited for ten years after the closing of the transactions related to such properties. These restrictions on the sale of such properties may prevent us from selling the properties or may adversely impact the terms available to us upon a disposition. In addition, we have agreed that, during such ten-year period, we will not prepay or defease

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any mortgage indebtedness of such properties, other than in connection with a concurrent refinancing with non-recourse mortgage debt of an equal or greater amount and subject to certain other restrictions. Furthermore, if any such sale or defeasance is foreseeable, we are required to notify Venture and to cooperate with it in considering strategies to defer or mitigate the recognition of gain under the Code. These contractual obligations may limit our future operating flexibility and compel us to take actions or enter into transactions that we otherwise would not undertake. If we fail to comply with any of these requirements, we will be liable for a make-whole cash payment to Venture, the cost of which could be material and could adversely affect our liquidity.

Proceeds from additional secured or unsecured debt financings

As of September 30, 2011, we have \$25.0 million of outstanding borrowings on our unsecured credit facility, which is the maximum amount available for borrowing under this facility. We currently do not have any arrangements for future unsecured financings and believe that it will be challenging to obtain any significant unsecured financings in the near term. In addition, all of our consolidated properties are currently encumbered and thus, we do not anticipate procuring any additional secured debt financings.

Actual and Potential Uses of Liquidity

The following are the projected uses, and some of the potential uses, of our cash for the remainder of 2011. Because of the current uncertainty in the real estate market and the economy as a whole, there may be other uses of our cash that are unexpected (and that are not identified below).

- Property operating and corporate expenses;
- Capital expenditures (including building and tenant improvements and leasing commissions);
- Financing costs and commitments; and/or
- Dividends to stockholders and distributions to limited partners of our Operating Partnership.

Property operating and corporate expenses

We are focused on ensuring our properties are operating as efficiently as possible. We have taken steps to identify opportunities to reduce discretionary operating costs wherever possible and at the same time maintaining the quality of our buildings and the integrity of our management services.

We internalized our management by acquiring our Advisor effective as of February 1, 2011. We now employ our executive officers and other employees through our former Advisor, Pacific Office Management, which is now our subsidiary. By employing personnel, we are now subject to potential liabilities commonly faced by employers, such as workers' disability and compensation claims, potential labor disputes and other employee-related liabilities and grievances. We are also responsible for all costs previously incurred by the Advisor in the management of our Company, but we are relieved of the \$0.8 million annual advisory fee. Because the Advisor operated at a loss, we are heavily focused on successfully integrating the operations of our Advisor and reducing corporate overhead expenses.

Capital expenditures (including building and tenant improvements and leasing commissions)

Capital expenditures fluctuate in any given period, subject to the nature, extent and timing of improvements required to maintain our properties. Leasing costs also fluctuate in any given period, depending upon such factors as the type of property, the term of the lease, the type of lease and overall market conditions. Our costs for capital expenditures and leasing fall into two categories: (1) amounts that we are contractually obligated to spend and (2) discretionary amounts. As of September 30, 2011, we expect to spend approximately \$2.9 million in committed capital expenditures and leasing costs for the remainder of 2011 and 2012. We are currently focused on preserving cash and intend to limit the amount of discretionary funds allocated to capital expenditures and leasing costs in the near term. This may result in a decrease in average rental rates and the number of new leases we execute, which would adversely affect our cash flow generated from operations.

Financing costs and commitments

As of September 30, 2011, our total consolidated debt (which includes our mortgage and other loans with a carrying value of \$356.2 million and our unsecured promissory notes with a carrying value of \$21.1 million) was approximately \$377.3 million, with a weighted average interest rate of 5.92% (utilizing a default interest rate for the Sorrento Technology Center loan) and a weighted average remaining term of 4.41 years. See "—Indebtedness" below for additional information with respect to our consolidated debt.

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On June 6, 2011, we received a notice of default on the loan secured by our Sorrento Technology Center property as we have stopped making the required principal and interest payments. The loan also requires us to deposit letters of credit totaling \$0.6 million in the event that certain tenants cease occupancy, go dark or give us notice of their intent to vacate the property. Based on the current occupancy of this property, we expect to fund these letters of credit in the fourth quarter of 2011. We are currently in negotiations with the lender to modify the terms of this loan.

In May 2011, we agreed to provide short-term financing in the total amount of up to \$1.5 million to one of our unconsolidated joint ventures. We funded \$0.6 million of this amount during the second quarter of 2011. No amounts were advanced during the third quarter of 2011. This loan bore interest at the annual rate of 12%, compounded annually, and was scheduled to mature in November 2011. At September 30, 2011, the joint venture was under contract to sell one of the properties included in the portfolio, Palomar Heights Corporate Center, and informed us that it intended to repay us with the proceeds of the sale. The sale of Palomar Heights Corporate Center was consummated in October 2011 and the loan and accrued interest were repaid in full.

Dividends to stockholders and distributions to limited partners of our Operating Partnership

Because we conduct substantially all of our operations through our Operating Partnership, our ability to pay dividends depends almost entirely on distributions received on our interests in our Operating Partnership, the payment of which depends in turn on our ability to operate profitably and generate cash flow from our operations. Our ability to pay dividends to holders of our Listed Common Stock depends on our Operating Partnership's ability first to satisfy its obligations to its creditors and preferred unitholders (including us with respect to the outstanding Senior Common Units of our Operating Partnership, and then to the holder of the outstanding Preferred Units of our Operating Partnership) and then to make distributions to us with respect to our general partnership interest. Our Operating Partnership may not make distributions to the holders of its outstanding Common Units (including us with respect to our general partnership interest) unless full cumulative distributions have been paid on its outstanding Senior Common Units and Preferred Units, and we may not pay dividends on our Listed Common Stock unless full cumulative dividends have been paid on our outstanding Senior Common Stock.

We did not declare a dividend on our Listed Common Stock for the first three quarters of 2011 and do not currently expect to declare a dividend on our Listed Common Stock for the remainder of fiscal 2011. Furthermore, our Operating Partnership did not pay a distribution with respect to its outstanding Preferred Units or Common Units for the first three quarters of 2011, and does not expect to do so for the remainder of fiscal 2011. As noted above, unless full cumulative distributions have been paid on the outstanding Preferred Units, our Operating Partnership may not pay a distribution on its outstanding Common Units (including us with respect to our general partnership interest), which effectively means that we will be unable to declare dividends on our Listed Common Stock until all cumulative distributions have been paid with respect to the Preferred Units.

In 2010, we paid an aggregate of \$6.1 million in cash dividends and distributions to holders of our Listed Common Stock, Class B Common Stock, Common Units and Preferred Units. Our board of directors authorized a cash distribution of \$0.05 per Common Unit and a cash dividend of \$0.05 per share of our Listed Common Stock and Class B Common Stock for each quarter of fiscal year 2009 and each of the first three quarters of fiscal year 2010. These dividends and distributions were paid on the 15th day of the month following the end of each quarter to holders of record as of the final day of such quarter. For the fourth quarter of 2010, our board of directors authorized a cash distribution of \$0.011 per Common Unit and a cash dividend of \$0.011 per share of our Listed Common Stock and Class B Common Stock, which were paid on January 17, 2011 to holders of record as of December 31, 2010. In addition, we paid 2% distributions, or \$1.25 per unit, to the holder of the Preferred Units for each quarter of fiscal years 2009 and 2010 on or about the 15th day of the month following the end of each such quarter. We relied upon borrowings under our revolving line of credit to pay a portion of these dividends and distributions.

Any dividends or other distributions we pay in the future will depend upon our legal and contractual restrictions, including the provisions of the Senior Common Stock, as well as actual results of operations, economic conditions, debt service requirements and other factors. Our actual results of operations will be affected by a number of factors, including any impact on the revenue we receive from our properties, our operating expenses, interest expense, the ability of our tenants to meet their obligations and unanticipated expenditures. For more information regarding risk factors that could materially adversely affect our actual results of operations, see Item 1A – “Risk Factors” of our Annual Report on Form 10-K for the year ended December 31, 2010 and in Item 1A of this Quarterly Report on Form 10-Q.

Our board of directors has authorized daily dividends on the Senior Common Stock, payable to holders of record of the Senior Common Stock as of the close of business on each day of the period commencing April 22, 2010 through October 31, 2011, in an amount equal to an annualized rate of 7.25%. Dividends declared for each month have been or will be paid on or about the 15th day of the following month. There can be no assurance that we will continue to declare and pay daily dividends

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on our Senior Common Stock.

Amounts accumulated for distribution to stockholders and Operating Partnership unitholders are invested primarily in interest-bearing accounts which are consistent with our intention to maintain our qualification as a REIT. At September 30, 2011, the cumulative unpaid distributions attributable to Preferred Units were \$1.7 million, which we do not anticipate to pay in 2011.

Cash Flows -

Net cash provided by operating activities for the Company for the nine months ended September 30, 2011 was \$3.3 million compared to net cash provided by operating activities of \$3.4 million for the nine months ended September 30, 2010. The decrease in operating cash flows was primarily due to a decrease in accounts payable and other liabilities partially offset by a decrease in restricted cash used for operating activities.

Net cash used in investing activities by the Company for the nine months ended September 30, 2011 was \$4.1 million compared to \$10.3 million for the nine months ended September 30, 2010. The decrease was primarily the result of a decrease in our capital expenditures by approximately \$2.5 million in the current year period compared to the prior year period and the prior year period included a \$5.0 million deposit paid for the unconsummated acquisition of the GRE portfolio. There were no acquisition deposits in the current period. These decreases were offset by an increase of \$2.8 million in our investments in unconsolidated joint ventures in the current year period for our ownership interests in the City Square and Pacific Business News Building (including the Valencia Corporate Center investment) joint ventures. Also, we assumed cash in the amount of \$0.3 million upon the internalization of our Advisor during the nine months ended September 30, 2011, with no similar activity in the prior year period.

Net cash used in financing activities was \$3.5 million for the nine months ended September 30, 2011 compared to net cash provided by financing activities of \$11.9 million during the nine months ended September 30, 2010. The primary reason for the decrease is that we have currently drawn the full \$25.0 million available to us on our revolving credit facility. In the prior year period, we had a \$13.1 million draw on our revolving credit facility during the first nine months of 2010, compared to a draw of \$0.6 million in the current year period. In addition, in the prior year period we had proceeds from the sale of Senior Common Stock of \$5.9 million where there were no proceeds in the current year period. Further, in the current year period we incurred \$1.6 million in financing costs and paid \$1.3 million in Senior Common Stock dividends with almost no similar activity in the prior period. These decreases were partially offset by a reduction in our distributions and dividends paid to the holders of our Listed Common Stock and Class B Common Stock and to the holders of Common Units of our Operating Partnership in the current year period compared to the prior year period as well as a decrease in offering costs in the current year period.

Pacific Office Properties Trust, Inc.

Indebtedness

Mortgage and Other Loans -

The following table sets forth information relating to the material borrowings with respect to our properties and our revolving line of credit as of September 30, 2011. Unless otherwise indicated in the footnotes to the table, each loan requires monthly payments of interest only and balloon payments at maturity, and all numbers, other than percentages, are reported in thousands:

PROPERTY	AMOUNT	INTEREST RATE	MATURITY DATE	BALANCE DUE AT MATURITY DATE	PREPAYMENT/ DEFEASANCE
Clifford Center ⁽¹⁾	\$ 3,001	4.375% ⁽²⁾	8/15/2014	\$ 1,896	⁽³⁾
First Insurance Center	38,000	5.74%	1/1/2016	38,000	⁽⁴⁾
First Insurance Center	14,000	5.40%	1/6/2016	14,000	⁽⁵⁾
Sorrento Technology Center ⁽⁶⁾	11,594	5.75% ^{(6) (7)}	1/11/2016 ^{(6) (7)}	11,594	⁽⁸⁾
Pan Am Building	60,000	6.17%	8/11/2016	60,000	⁽⁹⁾
Waterfront Plaza	100,000	6.37%	9/11/2016	100,000	⁽¹⁰⁾
Waterfront Plaza	11,000	6.37%	9/11/2016	11,000	⁽¹¹⁾
Davies Pacific Center	95,000	5.86%	11/11/2016	95,000	⁽¹²⁾
Subtotal	332,595				
Revolving line of credit ⁽¹³⁾	25,000	1.15%	12/31/2013	25,000	
Outstanding principal balance	357,595				
Less: Unamortized discount, net	(1,387)				
Net	\$ 356,208				

- (1) Requires monthly principal payments of \$31.6 thousand plus interest.
- (2) The interest rate on this loan floats with the lender's published prime rate which was 4.375% as of September 30, 2011.
- (3) Loan is prepayable anytime, with three business days notice, without a prepayment charge.
- (4) Loan is prepayable subject to a prepayment premium in an amount equal to the greater of 3% of outstanding principal amount or yield maintenance. No premium due after October 1, 2015. Loan may also be defeased.
- (5) Loan is not prepayable until October 6, 2015; however, loan may be defeased. No premium is due upon prepayment.
- (6) We ceased making the required monthly debt service payments in the amount of \$69 thousand on this loan in the second quarter of 2011, and on June 6, 2011, we received a notice of default accelerating the maturity date of the loan. As a result, interest is being incurred at the stated rate plus the default rate of 5% as stipulated in the loan agreement. We are currently in negotiations with the lender to modify the terms of this loan. The loan also requires us to deposit letters of credit totaling \$0.6 million in the event that certain tenants cease occupancy, go dark or give us notice of their intent to vacate the property. We expect to fund these letters of credit in the fourth quarter of 2011.
- (7) Although the stated maturity date is January 11, 2036, January 11, 2016 is the anticipated repayment date because the interest rate adjusts as of January 11, 2016 to greater of 7.75% or treasury rate plus 70 basis points, plus 2.0%.
- (8) No prepayment is permitted prior to October 11, 2015. Loan may be defeased.
- (9) Loan is prepayable subject to a prepayment premium equal to greater of 1% of principal balance of loan or yield maintenance. No premium is due after May 11, 2016.
- (10) Loan may be prepaid subject to payment of a yield maintenance-based prepayment premium; no premium is due after June 11, 2016. Loan may also be defeased.
- (11) Loan may be prepaid subject to payment of a yield maintenance-based prepayment premium; no premium is due after June 11, 2016.
- (12) Loan is prepayable, subject to prepayment premium equal to greater of (a) 1% of amount prepaid or (b) yield maintenance. No premium due after August 11, 2016.
- (13) The revolving line of credit matures on December 31, 2013. See "Revolving Line of Credit" below.

As of September 30, 2011, our ratio of total consolidated debt to total market capitalization was approximately 88.2%. Our total market capitalization of \$427.8 million includes our total consolidated debt of \$377.3 million, the market value of our Listed Common Stock and equivalents outstanding of \$26.3 million (based on the closing price of our Listed Common

Pacific Office Properties Trust, Inc.

Stock of \$0.52 per share on the NYSE Amex on September 30, 2011) and the market value of our outstanding Senior Common Stock of \$24.1 million (based on its \$10.00 per share offering price).

Revolving Line of Credit -

On September 2, 2009, we entered into a Credit Agreement, referred to as the FHB Credit Facility, with First Hawaiian Bank, or the Lender. The FHB Credit Facility initially provided us with a revolving line of credit in the principal sum of \$10.0 million. On December 31, 2009, we amended the FHB Credit Facility to increase the maximum principal amount available for borrowing under the revolving line of credit to \$15.0 million. On May 25, 2010, we entered into an amendment with the Lender to increase the maximum principal amount available for borrowing thereunder from \$15.0 million to \$25.0 million and to extend the maturity date from September 2, 2011 to December 31, 2013. Amounts borrowed under the FHB Credit Facility bear interest at a fluctuating annual rate equal to the effective rate of interest paid by the Lender on time certificates of deposit, plus 1.00%. We are permitted to use the proceeds of the line of credit for working capital and general corporate purposes, consistent with our real estate operations and for such other purposes as the Lender may approve. As of September 30, 2011 and December 31, 2010, we had outstanding borrowings of \$25.0 million and \$24.4 million, respectively, under the FHB Credit Facility.

As security for the FHB Credit Facility, as amended, Shidler LP, a Hawaii limited partnership controlled by Mr. Shidler, has pledged to the Lender a certificate of deposit in the principal amount of \$25.0 million. As a condition to this pledge, the Operating Partnership and Shidler LP entered into an indemnification agreement pursuant to which the Operating Partnership agreed to indemnify Shidler LP from any losses, damages, costs and expenses incurred by Shidler LP in connection with the pledge. In addition, to the extent that all or any portion of the certificate of deposit is withdrawn by the Lender and applied to the payment of principal, interest and/or charges under the FHB Credit Facility, the Operating Partnership agreed to pay to Shidler LP interest on the withdrawn amount at a rate of 7.00% per annum from the date of the withdrawal until the date of repayment in full by the Operating Partnership to Shidler LP. Pursuant to this indemnification agreement, as amended, the Operating Partnership also agreed to pay to Shidler LP an annual fee of 2.00% of the entire \$25.0 million principal amount of the certificate of deposit.

The FHB Credit Facility contains various customary covenants, including covenants relating to disclosure of financial and other information to the Lender, maintenance and performance of our material contracts, our maintenance of adequate insurance, payment of the Lender's fees and expenses, and other customary terms and conditions.

Subordinated Promissory Notes -

At September 30, 2011 and December 31, 2010, we had promissory notes payable by the Operating Partnership to certain affiliates in the aggregate principal amount of \$21.1 million, at both dates, which were originally issued as consideration to the affiliates, to fund certain capital improvements upon the completion of our formation transactions and upon the exercise of an option granted to us by Venture and its affiliates as part of our formation transactions. The promissory notes accrue interest at a rate of 7% per annum, with interest payable quarterly, subject to the Operating Partnership's right to defer the payment of interest for any or all periods up until the date of maturity. The promissory notes mature on various dates commencing on March 19, 2013 through August 31, 2013, but the Operating Partnership may elect to extend maturity for one additional year. Maturity accelerates upon the occurrence of a) an underwritten public offering of at least \$75 million of our common stock; b) the sale of substantially all the assets of the Company; or c) the merger of the Company with another entity. The promissory notes are unsecured obligations of the Operating Partnership.

For the period from March 20, 2008 through September 30, 2011, interest payments on the outstanding unsecured notes payable to related parties have been deferred. At September 30, 2011 and December 31, 2010, \$5.6 million and \$4.3 million, respectively, of accrued interest attributable to unsecured notes payable to related parties is included in accounts payable and other liabilities in the accompanying consolidated balance sheets.

Off-Balance Sheet Arrangements -

The mortgage debt that we maintain for our consolidated properties and unconsolidated joint venture properties is typically property-specific debt that is non-recourse to our Operating Partnership, except for customary recourse carve-outs for borrower misconduct and environmental liabilities. The recourse liability for borrower misconduct and environmental liabilities was guaranteed by Mr. Reynolds or, with respect to one loan, Mr. Shidler. Our Operating Partnership has agreed to indemnify Messrs. Reynolds and Shidler to the extent of their guaranty liability. This debt strategy isolates mortgage liabilities in separate, stand-alone entities, allowing us to have only our property-specific equity investment at risk, except to the extent of the recourse carve-outs. In management's judgment, it would be remote for us to incur any material liability under these indemnities

Pacific Office Properties Trust, Inc.

that would have a material adverse effect on our financial condition, results of operations or cash flows.

Inflation –

We are exposed to inflation risk, as income from long-term leases is the primary source of our cash flows from operations. Because the majority of our leases require tenants to pay most operating expenses, including real estate taxes, utilities, insurance, and increases in common area maintenance expenses, we do not believe our exposure to increases in costs and operating expenses resulting from inflation is material. Furthermore, the majority of our existing leases contain contractual annual rental rate increases, which will at least partially offset the effect of inflation on our operating results.

Our Status as a REIT -

We have made an election to be taxed as a REIT under Sections 856 through 860 of the Code and related regulations, and intend to continue to operate so as to remain qualified as a REIT for federal income tax purposes. We generally will not be subject to federal income tax on income that we distribute to our stockholders and Operating Partnership unit holders, provided that we distribute 100% of our REIT taxable income and meet certain other requirements for qualifying as a REIT. If we fail to qualify as a REIT in any taxable year, we will be subject to federal income tax on our taxable income at regular corporate rates and will not be permitted to qualify for treatment as a REIT for federal income tax purposes for four years following the year during which qualification is lost. Such an event could materially affect our income and our ability to pay dividends. We believe we have been organized as, and our past and present operations qualify the Company as, a REIT.

In connection with our formation transactions, we received a representation from our predecessor, Arizona Land Income Corporation, or AZL, that it qualified as a REIT under the provisions of the Code. However, during 2009 we became aware that, prior to the consummation of our formation transactions, AZL historically invested excess cash from time to time in money market funds that, in turn, were invested exclusively or primarily in short-term federal government securities. Additionally, during 2009 we became aware that AZL made two investments in local government obligations. Our predecessor, AZL, with no objection from outside advisors, treated these investments as qualifying assets for purposes of the 75% asset test. However, if these investments were not qualifying assets for purposes of the 75% asset test, then AZL would not have satisfied the REIT asset tests for certain quarters, in part, because they would have exceeded 5% of the gross value of AZL's assets. If these investments resulted in AZL's noncompliance with the REIT asset tests, however, we and our predecessor, AZL, would retain qualification as a REIT pursuant to certain mitigation provisions of the Code, which provide that so long as any noncompliance was due to reasonable cause and not due to willful neglect, and certain other requirements are met, qualification as a REIT may be retained but a penalty tax would be owed. Any potential noncompliance with the asset tests would be due to reasonable cause and not due to willful neglect so long as we exercised ordinary business care and prudence in attempting to satisfy such tests. Based on our review of the circumstances surrounding the investments, we believe that we exercised ordinary business care and prudence in attempting to satisfy the REIT asset tests, including the 5% asset test, and accordingly, that any noncompliance was due to reasonable cause and not due to willful neglect. Additionally, we believe that we have complied with the other requirements of the mitigation provisions of the Code with respect to such potential noncompliance with the asset tests (and have paid the appropriate penalty tax), and, therefore, our qualification, and that of our predecessor, AZL, as a REIT should not be affected. The IRS is not bound by our determination, however, and no assurance can be provided that the IRS will not assert that AZL failed to comply with the REIT asset tests as a result of the money market fund investments and the local government securities investments and that such failures were not due to reasonable cause. If the IRS were to successfully challenge this position, then it could determine that we and AZL failed to qualify as a REIT in one or more of our taxable years.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Not required.

Item 4. Controls and Procedures.

Evaluation of disclosure controls and procedures -

As required by Rule 13a-15(b) of the Exchange Act, in connection with the filing of this Quarterly Report on Form 10-Q, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of September 30, 2011, the end of the period covered by this report.

Changes in Internal Control Over Financial Reporting -

There have been no changes in our internal control over financial reporting that occurred during the quarter covered by this Quarterly Report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II — OTHER INFORMATION

Item 1. Legal Proceedings.

We are not currently a party, as plaintiff or defendant, to any legal proceedings which, individually or in the aggregate, are expected by us to have a material effect on our business, financial condition or results of operation if determined adversely to us.

Item 1A. Risk Factors.

Important factors that could cause our actual results to be materially different from the forward-looking statements include the risks factors previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2010 and our Quarterly Reports on Form 10-Q for the quarters ended March 31, 2011 and June 30, 2011, as well as the risk factors set forth below which update risk factors provided therein. In addition to the other information set forth in this report, you should carefully consider these risk factors, which could materially affect our business, financial condition and results of operations.

We may be unable to refinance, extend or repay our substantial indebtedness at maturity, including indebtedness of our unconsolidated joint venture properties that is matured and unpaid.

We cannot assure you that we will be able to refinance, extend or repay our substantial indebtedness on acceptable terms or at all. The ability to refinance our indebtedness is negatively affected by the current condition of the credit markets, which have significantly reduced the capacity levels of commercial lending, and may also be negatively affected by the real or perceived decline in the value of our properties based on general economic conditions.

We have \$11.6 million in aggregate principal indebtedness secured by our Sorrento Technology Center property that is in default. We are currently in negotiations with the lender to modify the terms of the loan, but there can be no assurance that we will be able to retain our ownership of this property.

In addition, as of September 30, 2011, our unconsolidated joint venture properties had, in the aggregate, approximately \$25.5 million of debt scheduled to mature in 2011 (\$24.7 million has since matured and remains unpaid), and an additional \$233.9 million of debt maturing in 2012. Of the debt scheduled to mature in 2012, \$27.1 million and \$150.0 million of debt is secured by the Black Canyon and SoCal Portfolio properties, respectively. The SoCal Portfolio includes 15 office and flex buildings totaling approximately 1,000,000 rentable square feet situated on seven properties (Via Frontera Business Park, Poway Flex, Carlsbad Corporate Center, Savi Tech Center, Yorba Linda Business Park, South Coast Executive Center and Gateway Corporate Center) in Los Angeles, Orange and San Diego counties in Southern California. If we or our joint venture partners are unable to service this debt, the lenders may foreclose on our joint venture properties or the joint ventures may have to deed properties back to the applicable lenders or otherwise dispose of properties, possibly on disadvantageous terms. If any of our joint ventures deed properties back to the applicable lenders, we would be required to write off our investment in the applicable joint venture, which could have a material adverse effect on our business, financial condition or results of operations. There can be no assurance that joint venture operations or contributions by us and/or our joint venture partners will be sufficient to repay these loans.

Unless we regain compliance with all applicable listing standards of the NYSE Amex, our Listed Common Stock could be suspended or delisted from the exchange, which may decrease the liquidity of our Listed Common Stock, make capital raising efforts more difficult and harm our financial condition and business.

Our Listed Common Stock is listed and traded on the NYSE Amex under the symbol "PCE." If we were to fail to meet any of the continued listing standards of the NYSE Amex, our Listed Common Stock could be suspended or delisted from the exchange. The NYSE Amex will consider the suspension or removal of a listed security when, in the opinion of the NYSE Amex:

- the financial condition and/or operating results of the issuer appear to be unsatisfactory,
- it appears that the extent of public distribution or the aggregate market value of the security has become so reduced as to make further dealings on the NYSE Amex inadvisable,

- the issuer has sold or otherwise disposed of its principal operating assets or has ceased to be an operating company,
- the issuer has failed to comply with its listing agreements with the NYSE Amex, or
- any other event occurs or any condition exists which makes further dealings on the NYSE Amex unwarranted.

On April 19, 2011, we received notice from the NYSE Amex indicating that we were not in compliance with the continued listing standards of the exchange, specifically, (i) Section 1003(a)(i) of the NYSE Amex Company Guide, because at December 31, 2010 we had total equity of less than \$2,000,000 and losses from continuing operations and/or net losses in two out of our three most recent fiscal years, and (ii) Section 1003(a)(ii) of the Company Guide, because at December 31, 2010 we had total equity of less than \$4,000,000 and losses from continuing operations and/or net losses in three out of our four most recent fiscal years.

The notification received from the NYSE Amex has had no current effect on the listing of our shares of Listed Common Stock on the exchange. In May 2011, we submitted a plan to the exchange pursuant to which we intend to establish compliance with the requirements of Sections 1003(a)(i) and (ii) of the Company Guide by October 19, 2012. The plan was accepted by the exchange in July 2011. There can be no assurance, however, we will be able to successfully implement our plan or that we will be able to comply with the exchange's other continued listing standards during the plan period. If the exchange initiates suspension or delisting procedures, we could appeal any such decision to the exchange, but there can be no assurance that any appeals by us to the exchange would be successful. Any suspension or delisting could adversely affect the market price and the liquidity of our Listed Common Stock and negatively impact our financial condition and business.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

During the three months ended September 30, 2011, we repurchased shares of our Senior Common Stock as follows:

	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares That May Yet be Purchased Under the Plans or Programs
July 1, 2011 to July 31, 2011 ⁽¹⁾	3,246	\$ 10.00	—	—
August 1, 2011 to August 31, 2011	—	—	—	—
September 1, 2011 to September 30, 2011	—	—	—	—
Total	3,246	\$ 10.00	—	—

(1) Represents a purchase of all of the shares of our Senior Common Stock held by a single investor upon the death of the investor.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. (Removed and Reserved)

Item 5. Other Information.

None.

Item 6. Exhibits.

<u>Exhibit No.</u>	<u>Description</u>
3.1	Articles of Amendment and Restatement of the Company (previously filed as Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2009 (File No. 001-09900) and incorporated herein by reference).
3.2	Articles Supplementary of the Company dated November 20, 2009 (previously filed as Exhibit 3.2 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2009 (File No. 001-09900) and incorporated herein by reference).
3.3	Articles of Amendment of the Company dated November 20, 2009 (previously filed as Exhibit 3.3 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2009 (File No. 001-09900) and incorporated herein by reference).
3.4	Articles of Amendment of the Company dated January 5, 2010 (previously filed as Exhibit 3.1 to the Company's Current Report on Form 8-K filed January 5, 2010 (File No. 001-09900) and incorporated herein by reference).
3.5	Articles Supplementary of Board of Directors Reclassifying and Designating a series of common stock as Senior Common Stock, dated March 4, 2010 (previously filed as Exhibit 3.2 to the Company's Current Report on Form 8-K filed March 9, 2010 (File No. 001-09900) and incorporated herein by reference).
3.6	Certificate of Correction to Articles Supplementary, dated April 30, 2010 (previously filed as Exhibit 3.6 to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2010 (File No. 001-09900) and incorporated herein by reference).
3.7	Articles of Amendment of the Company dated November 1, 2010 (previously filed as Exhibit 3.7 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2010 (File No. 001-09900) and incorporated herein by reference).
3.8	Amended and Restated Bylaws dated December 20, 2010 (previously filed as Exhibit 3.1 to the Company's Current Report on Form 8-K filed December 27, 2010 (File No. 001-09900) and incorporated herein by reference).
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. (Filed herewith.)
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. (Filed herewith.)
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (Furnished herewith.)
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (Furnished herewith.)
101	Interactive Data File. (Furnished herewith.)

SIGNATURES

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

PACIFIC OFFICE PROPERTIES TRUST, INC.

Date: November 14, 2011

By: /s/ James R. Ingebritsen

James R. Ingebritsen

Chief Executive Officer

By: /s/ Michael C. Burer

Michael C. Burer

Chief Financial Officer

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Section 2: EX-31.1 (CERTIFICATION OF CHIEF EXECUTIVE OFFICER)

Exhibit 31.1

CERTIFICATION

I, James R. Ingebritsen, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Pacific Office Properties Trust, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially

affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 14, 2011

By: /s/ James R. Ingebritsen

James R. Ingebritsen
Chief Executive Officer

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Section 3: EX-31.2 (CERTIFICATION OF CHIEF FINANCIAL OFFICER)

Exhibit 31.2

CERTIFICATION

I, Michael C. Burer, certify that:

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

reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

- (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
- (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 14, 2011

By: /s/ Michael C. Burer

Michael C. Burer
Chief Financial Officer

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Section 4: EX-32.1 (CERTIFICATION OF CHIEF EXECUTIVE OFFICER)

Exhibit 32.1

CERTIFICATION

In connection with the quarterly report of Pacific Office Properties Trust, Inc., a Maryland corporation (the "Company"), on Form 10-Q for the period ended September 30, 2011, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), James R. Ingebritsen, Chief Executive Officer, certifies, to the best of his knowledge, the following pursuant to Section 18, U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002:

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

Date: November 14, 2011

By: /s/ James R. Ingebritsen

James R. Ingebritsen
Chief Executive Officer

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Section 5: EX-32.2 (CERTIFICATION OF CHIEF FINANCIAL OFFICER)

Exhibit 32.2

CERTIFICATION

In connection with the quarterly report of Pacific Office Properties Trust, Inc., a Maryland corporation (the “Company”), on Form 10-Q for the period ended September 30, 2011, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), Michael C. Burer, Chief Financial Officer, certifies, to the best of his knowledge, the following pursuant to Section 18, U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002:

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

Date: November 14, 2011

By: /s/ Michael C. Burer

Michael C. Burer
Chief Financial Officer

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