CRESCENT REAL ESTATE EQUITIES CO
Form 10-K
March 16, 2007

**Table of Contents**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**
**Washington, D.C. 20549**
**FORM 10-K**

(Mark One)

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

**For the fiscal year ended December 31, 2006**

**OR**

o **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 1-13038**

**CRESCENT REAL ESTATE EQUITIES COMPANY**

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| TEXAS | 52-1862813 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification Number) |
| 777 Main Street, Suite 2100, Fort Worth, Texas | 76102 |
| (Address of principal executive offices) | (Zip code) |

Registrant s telephone number, including area code (817) 321-2100

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

| Title of each class: | Name of Each Exchange on Which Registered: |
|---|---|
| Common Shares of Beneficial Interest par value $0.01 per share | New York Stock Exchange |
| Series A Convertible Cumulative Preferred Shares of Beneficial Interest par value $0.01 per share | New York Stock Exchange |
| Series B Cumulative Redeemable Preferred Shares of Beneficial Interest par value $0.01 per share | New York Stock Exchange |

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

YES þ NO o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

YES o NO þ

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 twelve (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 ninety (90) days.

YES þ NO o

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

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

Large accelerated filer þ Accelerated filer o Non-accelerated filer o

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

YES o NO þ

As of June 30, 2006, the aggregate market value of the 94,283,113 common shares held by non-affiliates of the registrant was approximately $1.8 billion.

| | |
|---|---|
| Number of Common Shares outstanding as of March 5, 2007: | 102,807,311 |
| Number of Series A Preferred Shares outstanding as of March 5, 2007: | 14,200,000 |
| Number of Series B Preferred Shares outstanding as of March 5, 2007: | 3,400,000 |

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the Proxy Statement to be filed with the Securities and Exchange Commission for Registrant s 2007 Annual Meeting of Shareholders are incorporated by reference into Part III.

# TABLE OF CONTENTS

Table of Contents

# PART I

## Item 1. Business

*References to we, us or our refer to Crescent Real Estate Equities Company and, unless the context otherwise requires, Crescent Real Estate Equities Limited Partnership, which we refer to as our Operating Partnership, and our other direct and indirect subsidiaries. We conduct our business and operations through the Operating Partnership, our other subsidiaries and our joint ventures. References to Crescent refer to Crescent Real Estate Equities Company. The sole general partner of the Operating Partnership is Crescent Real Estate Equities, Ltd., a wholly-owned subsidiary of Crescent Real Estate Equities Company, which we refer to as the General Partner.*

*Certain statements contained herein constitute forward-looking statements as such term is defined in Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Forward-looking statements are not guarantees of performance. Our future results, financial condition and business may differ materially from those expressed in these forward-looking statements. You can find many of these statements by looking for words such as plans, intends, estimates, anticipates, expects, believes or similar expressions in this Form 10-K. These forward-looking statements are subject to numerous assumptions, risks and uncertainties. Many of the factors that will determine these items are beyond our ability to control or predict. For further discussion of these factors, see Item 1A. Risk Factors in this Form 10-K.*

*For these statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. You are cautioned not to place undue reliance on our forward-looking statements, which speak only as of the date of this Form 10-K or the date of any document incorporated by reference. All subsequent written and oral forward-looking statements attributable to us or any person acting on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section. We do not undertake any obligation to release publicly any revisions to our forward-looking statements to reflect events or circumstances after the date of this Form 10-K.*

### General

We operate as a real estate investment trust, or REIT, for federal income tax purposes and provide management, leasing and development services for some of our properties.

At December 31, 2006, our assets and operations consisted of four investment segments:

- Office Segment;
- Resort Residential Development Segment;
- Resort/Hotel Segment; and
- Temperature-Controlled Logistics Segment.

Within these segments, we owned in whole or in part the following operating real estate assets, which we refer to as the Properties, as of December 31, 2006:

- **Office Segment** consisted of 71 office properties, which we refer to as the Office Properties, located in 26 metropolitan submarkets in eight states, with an aggregate of approximately 27.6 million net rentable square feet. Fifty-four of the Office Properties are wholly-owned and 17 are owned through joint ventures, one of which is consolidated in our financial statements contained in Item 8, Financial Statements and Supplementary Data, and 16 of which are unconsolidated.

- **Resort Residential Development Segment** consisted of our ownership of common stock representing interests of 98% to 100% in four Resort Residential Development Corporations and two limited partnerships, which are consolidated. These Resort Residential Development Corporations, through partnership arrangements, owned, in whole or in part, 30 active and planned upscale resort residential development properties, which we refer to as the Resort Residential Development Properties.

Table of Contents

**Resort/Hotel Segment** consisted of five luxury and destination fitness resorts and spas with a total of 949 rooms/guest nights and three upscale business-class hotel properties with a total of 1,376 rooms, which we refer to as the Resort/Hotel Properties. Five of the Resort/Hotel Properties are wholly-owned, one is owned through a joint venture that is consolidated and two are owned through joint ventures that are unconsolidated.

**Temperature-Controlled Logistics Segment** consisted of our 31.7% interest in AmeriCold Realty Trust, or AmeriCold, a REIT. As of December 31, 2006, AmeriCold operated 104 facilities, of which 91 were wholly-owned or leased, one was partially-owned and 12 were managed for outside owners. The 92 owned or leased and partially-owned facilities, which we refer to as the Temperature-Controlled Logistics Properties, had an aggregate of approximately 497.8 million cubic feet (19.0 million square feet) of warehouse space. AmeriCold also owned one quarry and the related land.

See Note 3, Segment Reporting, included in Item 8, Financial Statements and Supplementary Data, for a table showing selected financial information for each of these investment segments for the three years ended December 31, 2006, 2005 and 2004, and total assets, consolidated property level financing, consolidated other liabilities and minority interests for each of these investment segments at December 31, 2006 and 2005.

See Note 1, Organization and Basis of Presentation, included in Item 8, Financial Statements and Supplementary Data, for a table that lists our principal subsidiaries and the properties that they own.

See Note 10, Investments in Unconsolidated Companies, included in Item 8, Financial Statements and Supplementary Data, for a table that lists our ownership in significant unconsolidated joint ventures and investments as of December 31, 2006.

## Business Objectives and Strategies Overview

We are a REIT with assets and operations divided into four investment segments: Office, Resort Residential Development, Resort/Hotel and Temperature-Controlled Logistics. Our strategy has two key elements as outlined below.

First, we selectively invest in premier office properties in markets that offer attractive returns on invested capital. We may align ourselves with institutional partners to enhance our return on equity when compared to the returns we receive as a 100% owner. Where possible, we negotiate performance-based incentives on our joint ventures that allow for additional equity to be earned if return targets are exceeded. For example, we earned promoted interests on the sales of the Three Westlake and Four Westlake joint venture Office Properties in 2006. We currently hold 43% of our office portfolio in joint ventures.

We selectively develop new office properties where the opportunity exists for attractive returns. In August 2006, we completed, with JMI Realty, a 232,330 square-foot, three-building complex in San Diego, California and sold our interest in the property in December 2006 for a $10.4 million gain. We are also developing a 239,000 square-foot office building as an addition to the Hughes Center complex in Las Vegas, Nevada. We are co-developing with Hines a 267,000 square-foot office building in Irvine, California, and with Champion Partners, a 144,380 square-foot, two-building office complex in Austin, Texas.

Second, we invest in real estate businesses that offer returns equal to or superior to what we are able to achieve in our office investments. We develop and sell residential properties in resort locations primarily through Crescent Resort Development, Inc., with Harry Frampton and his East West Partners development team, with the most significant project in terms of future cash flow being our investment in Tahoe Mountain Resorts in California. This development encompasses more than 2,500 total lots and units, of which 532 have been sold, 73 are currently in inventory and over 1,950 are scheduled for development over the next 14 years, and is expected to generate in excess of $5.0 billion in sales. We view our resort residential developments as a business and believe that, beyond the net present value of existing projects, there is value in our strategic relationships with the development teams and our collective ability to identify and develop new projects. In addition, we sometimes serve as the primary developer, such as The Ritz-Carlton Phases I and II. Also, we provide mezzanine financing to other office, hotel and residential investors where we see attractive returns relative to owning the equity. We currently have approximately $124.3 million of mezzanine notes.

Table of Contents

In 2005, we also completed the recapitalization of our Canyon Ranch® investment. In addition to its wellness facilities in Tucson, Arizona and Lenox, Massachusetts and its Spa Club operation at the Venetian Resort in Las Vegas, Nevada, Canyon Ranch partners with developers to establish Canyon Ranch Living communities at which the focal point is a large, comprehensive wellness facility and earns fees for the licensing of the brand name to these communities, providing design and technical services, and the ongoing management of the facilities. One such development is under construction in Miami Beach and an agreement that will pave the way for the development of a Canyon Ranch Living community in Chicago, Illinois, and others, are under consideration or in negotiation.

During 2006, we conducted an extensive review of our strategic alternatives, and in late August received an offer to purchase certain assets. Our Board of Trust Managers established a special committee of independent trust managers to assist in its consideration of the strategic alternatives and to respond to the offer that was received. The Special Committee hired an independent investment banker and counsel to assist with its review. The Special Committee has rejected the offer received, and on November 1, 2006, instituted a formal review of our strategic alternatives.

On March 1, 2007, we announced that we had concluded the review of strategic alternatives first announced on November 1, 2006. Based on that review, we adopted a plan, which we refer to as the Strategic Plan, designed to simplify our business model by concentrating on our core office properties business.

Key elements of the Strategic Plan include:

*Sale of all resort and hotel assets.* Properties to be sold include the Fairmont Sonoma Mission Inn & Spa®, Ventana Inn & Spa in Big Sur, California, the Park Hyatt Beaver Creek Resort & Spa, and three business-class hotels.

*Sale of resort residential developments.* Properties and assets to be sold include Crescent Resort Development and Desert Mountain Development Corporation.

*Opportunistic sale of office properties.* Properties to be sold include virtually all suburban Dallas properties and all Austin properties, as well as our single assets in Phoenix, Arizona, and in Seattle, Washington.

*Reduction of general and administrative expenses by more than $17.0 million, or $0.14 per share.* Implementation of savings began immediately on March 1, 2007 and is expected to be fully phased in by the end of 2007. We expect to take a charge of approximately $5.0 million for severance costs.

*Use of sales proceeds to retire debt*. We plan to first use the proceeds from asset sales to retire debt. We expect that our balance sheet will be significantly strengthened and our cost of capital lowered, giving us capacity for growth.

*Alignment of dividend*. We intend to align our dividend with industry-accepted pay-out ranges to allow for retention of capital for growth.

In addition to the above elements, we are considering alternatives for our interest in Canyon Ranch® in conjunction with the founders of Canyon Ranch®. We will communicate our dividend plans as we execute asset sales. After completing these dispositions, our remaining office portfolio is expected to consist of 22.6 million square feet, of which 11.7 million square feet, or 52%, will be owned in joint venture. Our effective ownership will be 14.0 million square feet.

**Available Information**

You can find our Web site on the Internet at www.crescent.com. We provide free of charge on our Web site our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports as soon as reasonably practicable after electronically filed with or furnished to the Securities and Exchange Commission.

**Employees**

As of March 5, 2007, we had approximately 748 employees. In connection with our Strategic Plan, the number of employees is expected to be reduced significantly by the end of 2007. None of these employees are covered by collective bargaining agreements. We consider our employee relations to be good.

**Tax Status**

We have elected to be taxed as a REIT under Sections 856 through 860 of the U.S. Internal Revenue Code of 1986, as amended, or the Code, and operate in a manner intended to enable us to continue to qualify as a REIT. As a REIT, we generally will not be subject to corporate federal income tax on net income that we currently distribute to our shareholders, provided that we satisfy certain organizational and operational requirements including the requirement to distribute at least 90% of our REIT taxable income to our shareholders each year. If we fail to qualify as a REIT in any taxable year, we will be subject to federal income tax (including any applicable alternative minimum tax) on our taxable income at regular corporate tax rates. We are subject to certain state and local taxes.

We have elected to treat certain of our corporate subsidiaries as taxable REIT subsidiaries, each of which we refer to as a TRS. In general, a TRS may perform additional services for our tenants and may engage in any real estate or non-real estate business (except for the operation or management of health care facilities or lodging facilities or the provision to any person, under a franchise, license or otherwise, of rights to any brand name under which any lodging facility or health care facility is operated). A TRS is subject to corporate federal income tax.

**Table of Contents**

### Environmental and Health and Safety Matters

We and our Properties are subject to a variety of federal, state and local environmental, health and safety laws, including:

- Comprehensive Environmental Response, Compensation, and Liability Act, as amended (CERCLA);
- Resource Conservation & Recovery Act;
- Clean Water Act;
- Clean Air Act;
- Toxic Substances Control Act; and
- Occupational Safety & Health Act.

The application of these laws to a specific property that we own will be dependent on a variety of property-specific circumstances, including the former uses of the property and the building materials used at each property. Under certain environmental laws, principally CERCLA and comparable state laws, a current or previous owner or operator of real estate may be required to investigate and clean up certain hazardous or toxic substances, asbestos-containing materials, or petroleum product releases at the property. They may also be held liable to a governmental entity or third parties for property damage and for investigation and clean up costs such parties incur in connection with the contamination, whether or not the owner or operator knew of, or was responsible for, the contamination. In addition, some environmental laws create a lien on the contaminated site in favor of the government for damages and costs it incurs in connection with the contamination. The owner or operator of a site also may be liable under certain environmental laws and common law to third parties for damages and injuries resulting from environmental contamination emanating from the site. Such costs or liabilities could exceed the value of the affected real estate. The presence of contamination or the failure to remediate contamination may adversely affect the owner s ability to sell or lease real estate or to borrow using the real estate as collateral.

Our compliance with existing environmental, health and safety laws has not had a material adverse effect on our financial condition or results of operations. To further protect our financial interests regarding environmental matters, we have in place a Pollution and Remediation Legal Liability insurance policy which will respond in the event of certain future environmental liabilities. Certain of our properties contain asbestos-containing building materials, or ACBM. Environmental law requires that ACBM be properly managed and maintained and may impose fines and penalties on building owners or operators for failure to comply with these requirements. For properties where ACBM have been identified or are suspected, an operations and maintenance plan has been prepared and implemented. If properties undergo major renovations or are demolished, certain environmental regulations are in place which specify the manner in which ACBM must be handled and disposed. We believe that we are compliant with current environmental regulations and that any ACBM have been appropriately contained.

Table of Contents

# INDUSTRY SEGMENTS

## Office Segment

### Ownership Structure

As of December 31, 2006, we owned or had an interest in 71 Office Properties located in 26 metropolitan submarkets in eight states, with an aggregate of approximately 27.6 million net rentable square feet. As lessor, we have retained substantially all of the risks and benefits of ownership of the Office Properties and account for the leases of our 55 consolidated Office Properties as operating leases. Fifty-four of the Office Properties are wholly-owned and 17 are owned through joint ventures, one of which is consolidated and 16 of which are unconsolidated. Additionally, we provide management and leasing oversight services for all of our Office Properties.

### Market Information

The Office Property portfolio reflects our strategy of investing in first-class assets within markets that have significant potential for long-term rental growth. Within our selected submarkets, we have focused on premier locations that management believes are able to attract and retain the highest quality tenants and command premium rents. We have sought new acquisitions that have strong economic returns based on in-place tenancy and/or strong value-creation potential given the market and our core competencies. Moreover, we have also sought assets with dominant positions within their markets and submarkets due to quality and/or location, which mitigates the risks of market volatility. Accordingly, management s investment strategy not only demands an acceptable current cash flow return on invested capital, but also considers cash flow growth prospects. We apply a well-defined leasing strategy in order to capture the potential revenue growth in our portfolio of Office Properties from occupancy gains and rental rate increases in the markets and the submarkets in which we have invested.

In selecting the Office Properties, we have analyzed demographic, economic and market data to identify metropolitan areas expected to enjoy significant long-term employment and office demand growth. The markets in which we are currently invested are projected to continue to exceed national employment and population growth rates, as illustrated in the following table. In addition, we consider these markets demand-driven. Our office investment strategy also includes metropolitan regions with above national average economic expansion rates combined with significant office development supply constraints. Additionally, our investment strategy seeks geographic and regional economic diversification within the markets expected to experience excellent economic and office demand growth.

Our major office markets, which include Dallas, Houston, Austin, Denver, Miami and Las Vegas, currently enjoy rising employment and are anticipated to be among the leading metropolitan areas for population and employment growth over the next three years.

**Projected Population Growth and Employment Growth for all Company Markets**

| Metropolitan Statistical Area | Population Growth 2007-2009 | Employment Growth 2007-2009 |
|---|---|---|
| United States | 2.7% | 3.4% |
| Atlanta, GA | 6.2 | 6.0 |
| Austin, TX | 8.6 | 9.2 |
| Colorado Springs, CO | 4.2 | 5.7 |
| Dallas, TX | 6.1 | 6.1 |
| Denver, CO | 3.6 | 4.3 |
| Fort Worth, TX | 6.1 | 6.3 |
| Houston, TX | 6.0 | 6.2 |
| Las Vegas, NV | 10.9 | 10.1 |
| Miami, FL | 3.6 | 3.9 |
| Orange County, CA | 3.1 | 4.3 |
| Phoenix, AZ | 7.0 | 9.0 |
| Seattle, WA | 4.9 | 6.0 |

Source: Moody s | Economy.com, data represents total percentage change for years 2007, 2008 and 2009.

**Table of Contents**

**Unemployment Rates for Company Markets**

| Market | As of December 31, 2006 | 2005 |
|---|---|---|
| United States | 4.3% | 4.6% |
| Texas | 4.1 | 4.8 |
| Dallas | 4.0 | 4.6 |
| Houston | 4.0 | 5.1 |
| Austin | 3.2 | 3.9 |
| Denver | 3.9 | 4.5 |
| Miami | 3.5 | 3.6 |
| Las Vegas | 4.2 | 3.5 |

Source: U.S. Bureau of Labor Statistics and Texas Workforce Commission. Not seasonally adjusted.

The performance of all of our office markets improved in 2006. Occupancy rose in all of our major markets with the exception of Las Vegas. All markets had positive net absorption, and Dallas, Houston, and Austin significantly outpaced 2005. Occupancy increases of 2.7 percentage points in Houston and 3.8 percentage points in Austin were particularly strong. Miami and Las Vegas remain very healthy markets even though gains slowed from the 2005 pace.

**Office Market Absorption and Occupancy for Major Company Markets**

| | Economic Net Absorption(1) All Classes (in square feet) | | Economic Net Absorption(1) Class A (in square feet) | | Economic Occupancy(2) All Classes | | Economic Occupancy(2) Class A | |
|---|---|---|---|---|---|---|---|---|
| **Market** | **2006** | **2005** | **2006** | **2005** | **2006** | **2005** | **2006** | **2005** |
| Dallas | 3,514,000 | 549,000 | 2,707,000 | 1,250,000 | 78.3% | 77.5% | 82.6% | 80.9% |
| Houston | 5,814,000 | 1,007,000 | 4,443,000 | (207,000) | 85.8 | 83.1 | 88.4 | 83.7 |
| Austin | 1,966,000 | 1,177,000 | 1,300,000 | 458,000 | 88.3 | 84.5 | 89.7 | 83.7 |
| Denver | 2,473,000 | 2,761,000 | 1,672,000 | 887,000 | 85.6 | 84.5 | 88.1 | 85.5 |
| Miami | 778,000 | 1,998,000 | 692,000 | 757,000 | 92.7 | 91.4 | 92.0 | 88.7 |
| Las Vegas | 900,000 | 2,068,000 | 241,000 | 305,000 | 89.8 | 91.5 | 92.6 | 91.9 |

Sources: CoStar Group for non-medical and non-owner-occupied buildings greater than 15,000 square feet (Dallas, Houston, Austin, Denver and Miami); Grubb & Ellis Las Vegas (Las Vegas).

(1) Economic net absorption is the change in leased space from one period to another.

(2) Economic occupancy reflects the occupancy of all tenants paying rent.

One of the reasons for the improved occupancy in 2006 is that all of our major markets, except Dallas, have relatively low levels of Class A office construction and demand levels outpacing new supply. Dallas has an active development arena, about on par with demand levels. Most markets experienced increases in new supply delivered in 2006, and all of the major markets had much higher levels of space under construction at the end of 2006.

**Office Market Construction Activity for Major Company Markets**

| (in square feet) | Office Space Completions All Classes | | Office Space Completions Class A | | Office Space Under Construction 2006 | |
|---|---|---|---|---|---|---|
| **Market** | **2006** | **2005** | **2006** | **2005** | **All Classes** | **Class A** |
| Dallas | 2,759,000 | 649,000 | 1,699,000 | 215,000 | 3,087,000 | 2,596,000 |
| Houston | 1,377,000 | 970,000 | 850,000 | 192,000 | 2,514,000 | 889,000 |
| Austin | 378,000 | 384,000 | 148,000 | | 1,247,000 | 807,000 |
| Denver | 1,677,000 | 454,000 | 596,000 | | 803,000 | 292,000 |
| Miami | 369,000 | 588,000 | 255,000 | 36,000 | 3,077,000 | 1,170,000 |
| Las Vegas | 2,956,000 | 2,569,000 | | 365,000 | 2,821,000 | 1,187,000 |

Sources: CoStar Group (Dallas, Houston, Austin, Denver and Miami); Restrepo Consulting Group, LLC (Las Vegas).

**Competition**

Our Office Properties, primarily Class A properties located within the Southwest, individually compete against a wide range of property owners and developers, including property management companies and other REITs that offer space in similar classes of office properties (specifically Class A properties). A number of these owners and developers may own more than one property. The number and type of competing properties in a particular market or submarket could have a material effect on our ability to lease space and maintain or increase occupancy or rents in our existing Office Properties. We believe, however, that the quality services and individualized attention that we offer our tenants, together with our active preventive maintenance program and superior building locations within markets, enhance our ability to attract and retain tenants for our Office Properties. In addition, as of December 31, 2006, on a weighted average basis, we owned approximately 12% of the Class A office space in the 26 submarkets in which we owned Class A office properties. We believe that ownership of a significant percentage of office space in a particular market reduces property operating expenses, enhances our ability to attract and retain tenants and potentially results in increases in our net income.

**Diversified Tenant Base**

Our top ten tenants accounted for approximately 13.5% of our total Office Segment revenues as of December 31, 2006. The loss of major tenants could have a temporary adverse effect on our financial condition and results of operations until we are able to re-lease the space previously leased to these tenants. Based on rental revenues from office leases in effect as of December 31, 2006, no single tenant accounted for more than 2.5% of our total Office Segment revenues for 2006.

In June 2005, we entered into an agreement with our then largest office tenant, El Paso Energy Services Company and certain of its subsidiaries, which terminated El Paso s leases totaling 888,000 square feet at Greenway Plaza in Houston, Texas, effective December 31, 2007. Under the agreement, El Paso is required to pay us $65.0 million in termination fees in periodic installments through December 31, 2007, and $62.0 million in rent according to the original lease terms from July 1, 2005 through December 31, 2007. As of December 31, 2006, we have collected $35.0 million of the lease termination fee. For the years ended December 31, 2006 and 2005, we recognized $38.8 million and $8.5 million, respectively, in net termination fees, which includes accelerated termination fees and contractual full-service rents resulting from the re-lease of approximately 463,000 square feet. As of December 31, 2006, El Paso was current on all rent obligations.

Table of Contents

## Resort Residential Development Segment

### Ownership Structure

As of December 31, 2006, we owned equity interests of 98% to 100% in four Resort Residential Development Corporations and two limited partnerships which are consolidated. These Resort Residential Development Corporations, through partnership arrangements, owned in whole or in part 30 active and planned upscale resort residential development properties, which we refer to as the Resort Residential Development Properties. The partnerships, for the majority of which we are not the general partner, are responsible for the continued development and the day-to-day operations of the Resort Residential Development Properties.

### Competition and Market Information

Our Resort Residential Development Properties compete against a variety of other housing alternatives in each of their respective areas. These alternatives include other planned developments, pre-existing single-family homes, condominiums and townhouses. These developments focus primarily on the buying power of aging baby boomers. Management believes that the properties owned by Crescent Resort Development Inc., or CRDI, and Desert Mountain Development Corporation, or Desert Mountain, representing our most significant investments in Resort Residential Development Properties, contain certain features that provide competitive advantages to these developments.

CRDI invests primarily in mountain resort residential real estate in Colorado and California, as well as in downtown Denver, Colorado. Management believes that the Properties owned by CRDI have limited direct competitors because of the projects locations, unique product offerings, limited land availability and restricted development rights.

Desert Mountain, a luxury resort residential and recreational private community in Scottsdale, Arizona, offers six 18-hole Jack Nicklaus signature golf courses with adjacent clubhouses. Management believes Desert Mountain has few direct competitors due in part to the superior natural surroundings and the amenity package that Desert Mountain offers to its members. Sources of competition come from the resale market of existing lots and homes within Desert Mountain and from a few smaller projects in the area. In addition, future resort residential golf development in the Scottsdale area is limited due to the lack of water available for golf course use.

Resort residential development demand is highly dependent upon the national economy, home sales and, to a lesser extent, on mortgage interest rates. The national economy achieved healthy economic expansion in 2006 as a result of strong business growth, and mortgage rates rose only marginally (the 30-year average mortgage rate rose by 50 basis points in the first half of the year and then declined by the same in the second half). Nevertheless, the housing sector did slow down considerably. Our markets were somewhat impacted by the housing slowdown, but less than most primary housing markets. In general, we found that the volume of housing transactions declined in our markets, but the pricing held up well or improved. For example, in Eagle County, Colorado where a large CRDI resort development is located, sales volume fell 23% compared to 2005, but the average sales price climbed due to the rising percentage of high end sales in the area.

## Resort/Hotel Segment

### Ownership Structure

As of December 31, 2006, we owned or had an interest in five luxury and destination fitness resorts and spas and three upscale business-class hotel properties, which we refer to as the Resort/Hotel Properties. We hold one of the Resort/Hotel Properties, the Fairmont Sonoma Mission Inn & Spa, through a joint venture arrangement, pursuant to which we own an 80.1% interest in the limited liability company, which is consolidated, that owns the property. We hold two of the Resort/Hotel Properties, Canyon Ranch Tucson and Canyon Ranch Lenox, through an unconsolidated joint-venture arrangement, pursuant to which we own a 48% interest in the limited liability companies that own the properties. The remaining five Resort/Hotel Properties are wholly-owned.

Seven of the Resort/Hotel Properties are leased to taxable REIT subsidiaries that we own or in which we have an interest. The Omni Austin Hotel is leased to HCD Austin Corporation, an unrelated third party. Third-party operators manage all of the Resort/Hotel Properties.

**Market Information**

Lodging demand is highly dependent upon the global economy and volume of business travel as well as leisure travel. The hospitality market has enjoyed three years of strong market recovery as measured by occupancy, room rates and revenue per available room, or RevPAR, (RevPAR is a combination of occupancy and room rates and is the chief measure of hotel market performance). In 2006, the national occupancy rate, as reported by Smith Travel Research, experienced a 0.3 percentage point increase to 63.4%, a 7.5% gain in RevPAR and a 7.0% rise in average daily room rates, or ADR. For the luxury section of the industry, the most comparable to our portfolio, hotel occupancy rose 1.2 percentage points to 71.4%, RevPAR climbed 11.7% and ADR increased 9.1% . New hotel construction is still very limited in the nation and in our markets, although it is rising. In 2006, the increase to total hotel supply in the United States was a low 0.6%. The luxury hotel inventory rose by 3.0%.

**Competition**

We believe that our luxury and destination fitness resorts and spas are unique properties due to location, concept and high replacement cost, all of which create barriers for competition to enter. However, the luxury and destination fitness resorts and spas do compete against business-class hotels or middle-market resorts in their geographic areas, as well as against luxury resorts nationwide and around the world. Our upscale business-class Resort/Hotel Properties in Denver, Austin and Houston are business and convention center hotels that compete against other business and convention center hotels.

**Temperature-Controlled Logistics Segment**

**Ownership Structure**

As of December 31, 2006, the Temperature-Controlled Logistics Segment consisted of our 31.7% interest in AmeriCold Realty Trust, or AmeriCold, a REIT, which is unconsolidated. AmeriCold operates 104 facilities, of which 91 are wholly-owned or leased, one is partially-owned and 12 are managed for outside owners. The 92 owned or leased facilities, which we refer to as the Temperature-Controlled Logistics Properties, have an aggregate of approximately 497.8 million cubic feet (19.0 million square feet) of warehouse space. AmeriCold also owns one quarry and the related land.

**Business and Industry Information**

AmeriCold provides the food industry with refrigerated warehousing, transportation management services and other logistical services. The Temperature-Controlled Logistics Properties consist of production, distribution and public facilities. In addition, AmeriCold manages facilities owned by its customers for which it earns fixed and incentive fees. Production facilities differ from distribution facilities in that they typically serve one or a small number of customers located nearby. These customers store large quantities of processed or partially processed products in the facility until they are further processed or shipped to the next stage of production or distribution. Distribution facilities primarily serve customers who store a wide variety of finished products to support shipment to end-users, such as food retailers and food service companies, in a specific geographic market. Public facilities generally serve the needs of local and regional customers under short-term agreements. Food manufacturers and processors use public facilities to store capacity overflow from their production facilities or warehouses. These facilities also provide a number of additional services such as blast freezing, import/export and labeling.

AmeriCold provides supply chain management solutions to food manufacturers and retailers who require multi-temperature storage, handling and distribution capability for their products. Service offerings include comprehensive transportation management, supply chain network modeling and optimization, consulting and grocery retail-based distribution strategies such as multi-vendor consolidation, direct-store delivery (DSD) and seasonal product distribution. AmeriCold s technology provides food manufacturers with real-time detailed inventory information via the Internet.

Table of Contents

AmeriCold s customers consist primarily of national, regional and local food manufacturers, distributors, retailers and food service organizations. A breakdown of AmeriCold s largest customers includes:

| | Percentage of 2006 Segment Revenue |
|---|---|
| H.J. Heinz Company | 17.9% |
| ConAgra Foods, Inc. | 9.6 |
| Altria Group Inc. (Kraft Foods) | 5.7 |
| Schwan Corp. | 4.3 |
| Tyson Foods, Inc. | 4.1 |
| General Mills, Inc. | 3.5 |
| Sara Lee Corp. | 3.3 |
| McCain Foods Limited | 3.2 |
| U.S. Government | 3.1 |
| Smithfield Companies Inc. | 2.9 |
| Wayne Farms LLC | 2.6 |
| Rich Products Corp. | 2.4 |
| Jack in the Box Inc. | 2.3 |
| J. R. Simplot Company | 2.2 |
| Other | 32.9 |
| **Total** | 100.0% |

**Competition**

AmeriCold is the largest operator of temperature-controlled warehouse space in North America. As a result, AmeriCold does not have any competitors of comparable size. AmeriCold operates in an environment in which competition is national, regional and local in nature and in which the range of service, temperature-controlled logistics facilities, customer mix, service performance and price are the principal competitive factors.

## Item 1A. Risk Factors

**If we are unable to effectively implement the Strategic Plan, our business, financial condition, operating results and common share price could suffer.**

The implementation of the Strategic Plan requires us to complete sales of numerous properties and businesses, and effect a substantial reduction in our general and administrative expenses, which will include a significant reduction in personnel. No assurance can be given that we will be able to fully implement the Strategic Plan, or that the implementation will not have an adverse effect on our operations or financial condition. If we fail to implement the Strategic Plan, or if the implementation is longer, more costly or otherwise less successful than projected, we could be subject to various adverse consequences, including, but not limited to, the following:

we may face various disruptions to the operation of our business as a result of the substantial time and effort invested by our management in connection with the Strategic Plan, and may be unable to respond effectively to competitive pressures or take advantage of new business opportunities;

our decision to implement the Strategic Plan may cause harm to relationships with our employees and/or may divert employee attention away from day-to-day operations of our business;

our decision to implement the Strategic Plan requires cooperation of our strategic business partners, including our relationships with the management of Canyon Ranch and East West Partners;

regardless of our ability to consummate the Strategic Plan, we would remain liable for significant costs relating thereto, including, among others, severance and retention payments, and accounting, legal and financial advisory expenses; and

an announcement that we have abandoned or cannot fully implement the Strategic Plan could trigger a decline in our common share price to the extent that our share price reflects a market assumption that we will complete the Strategic Plan.

**Our Strategic Plan calls for us to make substantial divestitures. We may be unable to make these divestitures on terms that are acceptable, or at all.**

We anticipate making a number of divestitures of our hotel and resort properties, our non-core office properties and our resort and residential development business in accordance with our Strategic Plan. Real estate investments generally cannot be sold quickly. Our ability to do so on favorable terms may be limited by the availability of interested purchasers and internal demand on our resources. We, and our advisors, may not be able to identify purchasers and negotiate acceptable terms on a timely basis or at all. We may not be able to sell these properties for a gain relative to current net book value of such properties. To the extent we are unable to sell these properties for our book value, we may be required to take a non-cash impairment charge or loss on the sale, either of which would reduce our net income.

Table of Contents

**Our failure to have an effective system of internal controls over financial reporting could hinder our ability to accurately or timely report our financial results, which could have an adverse effect on our business, results of operations or financial condition.**

Although we have received an opinion from our independent registered public accounting firm, Ernst & Young LLP, that the financial statements included in this Annual Report on Form 10-K present fairly, in all material respects, in conformity with U.S. generally accepted accounting principles, our consolidated financial position, results of operations and cash flows for the periods indicated therein, our management concluded, as of December 31, 2006, that our internal control over financial reporting was not effective as a result of three incorrect accounting items, described further in Item 8, Financial Statements and Supplementary Data , Note 1, Organization and Basis of Presentation, that constituted material weaknesses. These accounting items, which are highly complex and subject to interpretation, have since been corrected. You should note that any control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance of achieving the desired control objectives, and there can be no assurance that we will be able to maintain effective internal controls over financial reporting in the future. An ineffective control environment, if not remedied, could result in a misstatement of our financial statements that could cause a delay in periodic filings with the SEC and such delay could cause a violation of debt covenants.

**We derive the substantial majority of our office rental revenues from geographically concentrated markets.**

As of December 31, 2006, approximately 66% of our office portfolio, based on total net rentable square feet, was located in the metropolitan areas of Houston and Dallas, Texas. Due to our geographic concentration in these metropolitan areas, any deterioration in economic conditions in the Houston or Dallas metropolitan areas, or in other geographic markets in which we in the future may acquire substantial assets, could adversely affect our results of operations and our ability to make distributions to our shareholders and could decrease our cash flow. In addition, we compete for tenants based on rental rates, attractiveness and location of a property and quality of maintenance and management services. An increase in the supply of properties competitive with ours in these markets could have a material adverse effect on our ability to attract and retain tenants in these markets.

**Our performance and value are subject to general risks associated with the real estate industry.**

Our economic performance and the value of our real estate assets, and consequently the value of our investments, will be adversely affected if our Office, Resort Residential Development, Resort/Hotel and Temperature-Controlled Logistics Properties do not generate revenues sufficient to meet our operating expenses, including debt service and capital expenditures. Any reduction in the revenues that our properties generate will adversely affect our cash flow and ability to meet our obligations. As a real estate company, we are susceptible to the following real estate industry risks:

- downturns in the national, regional and local economic conditions where our properties are located;
- competition from other Office, Resort Residential Development, Resort/Hotel and Temperature-Controlled Logistics properties;
- adverse changes in local real estate market conditions, such as oversupply or reduction in demand for office space, luxury residences, Resort/Hotel space or Temperature-Controlled Logistics storage space;
- changes in tenant preferences that reduce the attractiveness of our properties to tenants;
- tenant defaults;
- zoning or other regulatory restrictions;
- decreases in market rental rates;
- costs associated with the need to periodically repair, renovate and re-lease space;

increases in the cost of maintenance, insurance and other operating costs, including real estate taxes, associated with one or more properties, which may occur even when circumstances such as market factors and competition cause a reduction in revenues from one or more properties; and

illiquidity of real estate investments, which may limit our ability to vary our portfolio promptly in response to changes in economic or other conditions.

Table of Contents

**We depend on leasing office space to tenants on economically favorable terms and collecting rent from our tenants, who may not be able to pay.**

Our financial results depend significantly on leasing space in our office properties to tenants on economically favorable terms. In addition, because a large portion of our income comes from the renting of real property, our income, funds available to pay debt and funds available for distribution to our shareholders will decrease if a significant number of our tenants cannot pay their rent. If a tenant does not pay its rent, we might not be able to enforce our rights as landlord without delays and might incur substantial legal costs.

A number of companies, including some of our tenants, have declared bankruptcy in recent years, and other tenants may declare bankruptcy or become insolvent in the future. If a major tenant declares bankruptcy or becomes insolvent, the rental property where it leases space may have lower revenues and financial difficulties. Our leases generally do not contain restrictions designed to ensure the creditworthiness of our tenants. As a result, the bankruptcy or insolvency of a major tenant could result in a lower level of funds from operations available for distribution to our shareholders or the payment of our debt.

We maintain an allowance for doubtful accounts that is reviewed for adequacy by assessing such factors as the credit quality of our tenants, any delinquency in payment, historical trends and current economic conditions. If our assumptions regarding the collectibility of tenant accounts receivable prove incorrect, we could experience write-offs in excess of the allowance for doubtful accounts, which would result in a decrease in our earnings. Bad debt as a percentage of office rental revenue has averaged less than 0.3% over the last three years.

**We may experience difficulty or delay in renewing leases or re-leasing space.**

We derive most of our revenue in the form of rent received from our tenants. We are subject to the risks that, upon expiration, leases for space in our office properties may not be renewed, the space may not be re-leased, or the terms of renewal or re-lease, including the cost of required renovations or concessions to tenants, may be less favorable than current lease terms. In the event of any of these circumstances, our results of operations and our ability to meet our obligations could be adversely affected.

As of December 31, 2006, leases of office space for approximately 2.0 million, 2.3 million and 2.5 million square feet, representing approximately 8.4%, 9.7% and 10.4% of net rentable area, expire in 2007, 2008 and 2009, respectively. During these same three years, leases of approximately 22.0% of the net rentable area of our office properties in Dallas and approximately 31.5% of the net rentable area of our office properties in Houston expire.

**Our results of operations depends on the ability of El Paso Energy to meet its obligations pursuant to its lease termination agreement with us.**

In June 2005, we entered into an agreement with our largest office tenant, El Paso Energy Services Company and certain of its subsidiaries, which terminated El Paso s leases totaling 888,000 square feet at Greenway Plaza in Houston, Texas, effective December 31, 2007. Original expirations for the space ranged from 2007 through 2014. Under the agreement, El Paso is required to pay in cash to us:

- $65.0 million in termination fees in periodic installments through December 31, 2007 (of which $35.0 million has been received as of December 31, 2006, and is included in restricted cash in our Consolidated Balance Sheets as it is required to be escrowed with the lender); and
- $62.0 million in rent according to original contractual lease terms from July 1, 2005, through December 31, 2007 (of which $39.8 million has been received as of December 31, 2006).

If El Paso does not comply with the terms of the agreement, our revenues will decline, which will adversely affect our results of operations and reduce the cash available for distribution to our shareholders or the payment of our debt.

**We may have limited flexibility in dealing with our jointly owned investments.**

Our organizational documents do not limit the amount of funds that we may invest in properties and assets jointly with other persons or entities. As of December 31, 2006, approximately 43% of the net rentable area of our office properties was held jointly with other persons or entities. In addition, three of our five Resort/Hotel properties, all of our Resort Residential Development properties and our Temperature-Controlled Logistics properties were owned jointly.

Joint ownership of properties may involve special risks, including the possibility that our partners or co-investors might:

- become bankrupt;
- have economic or other business interests or goals which are unlike or incompatible with our business interests or goals;
- be in a position to take action contrary to our suggestions or instructions, or in opposition to our policies or objectives (including actions that may be inconsistent with our REIT status); and
- have different objectives from us regarding the appropriate timing and pricing of any sale or refinancing of the properties.

Joint ownership also gives a third party the opportunity to influence the return we can achieve on some of our investments and may adversely affect our results of operations and our ability to meet our obligations. In addition, in many cases we do not control the timing or amount of distributions that we receive from the joint investment, and amounts otherwise available for distribution to us instead may be reinvested in the property or used for other costs and expenses of the joint operation.

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

**The management and leasing agreements under which we operate our Office Properties owned through joint ventures may be terminated after an initial period.**

We generally manage the day-to-day operations of our 17 properties held through joint ventures pursuant to separate management and leasing agreements. Under these agreements we receive fees for management of the properties and leasing commissions. The management and leasing agreements may be terminated, after an initial period of one to five years, by our partners in the joint ventures. The termination of one or more of the management and leasing agreements would result in the loss of the management fees and leasing commissions payable under such agreement or agreements.

**The performance of our Resort Residential Development Properties is affected by national, regional and local economic conditions.**

Our Resort Residential Development Properties, which include Desert Mountain and CRDI properties, are generally targeted toward purchasers of high-end primary residences or seasonal secondary residences. As a result, the economic performance and value of these properties is particularly sensitive to changes in national, regional and local economic and market conditions. Economic downturns may discourage potential customers from purchasing new, larger primary residences or vacation or seasonal homes. In addition, other factors may affect the performance and value of a property adversely, including changes in laws and governmental regulations (including those governing usage, zoning and taxes), changes in interest rates (including the risk that increased interest rates may result in decreased sales of lots in any resort residential development property) and the availability to potential customers of financing. Adverse changes in any of these factors, each of which is beyond our control, could reduce the income that we receive from the properties, and adversely affect our ability to meet our obligations.

**In many cases, we do not develop our Resort Residential Development Properties and are dependent on the developer of these properties.**

Some of our Resort Residential Development Corporations co-own Resort Residential Development properties in partnership with third parties, which are the developers of the properties. Our partner for the majority of our Resort Residential Development properties is Harry Frampton and his East West Partners development team. Our income from the development and sale of these properties may be adversely affected if East West Partners fails to control costs and provide quality services and workmanship or if it fails to maintain a quality brand name. In addition, although we have entered into agreements with East West Partners that contain limited non-competition provisions, at certain times and upon certain conditions, East West Partners may develop, and in some cases own or invest in, Resort

Residential Development properties that compete with our properties, which may result in conflicts of interest. As a result, East West Partners may in the future make decisions regarding competing properties that would not be in our best interests. While we believe that we could find a replacement for East West Partners, the loss of its services could have an adverse effect on the financial performance of our Resort Residential Development Segment.

**The revenues from our eight Resort/Hotel Properties depend on third-party operators that we do not control.**

We own or have an interest in eight Resort/Hotel properties, seven of which are leased to our own subsidiaries. We currently lease the remaining Resort/Hotel property, the Omni Austin Hotel, to a third-party entity, HCD Austin Corporation. To maintain our status as a REIT, third-party property managers manage each of the eight Resort/Hotel properties. As a result, we are unable to directly implement strategic business decisions with respect to the operation and marketing of our Resort/Hotel properties, such as decisions about quality of accommodations, room-rate structure and the quality and scope of other amenities such as food and beverage facilities and similar matters. The amount of revenue that we receive from the Resort/Hotel properties is dependent on the ability of the property managers to maintain and increase the gross receipts from these properties. If the gross receipts of our Resort/Hotel Properties decline, our revenues will decrease as well, which could adversely affect our results of operations and reduce the amount of cash available to meet our obligations.

**The revenues from our eight Resort/Hotel Properties are subject to risks associated with the hospitality industry.**

The following factors, among others, are common to the Resort/Hotel industry, and may reduce the receipts generated by our Resort/Hotel Properties.

- Based on features such as access, location, quality of accommodations, room-rate structure and, to a lesser extent, the quality and scope of other amenities such as food and beverage facilities, our Resort/Hotel properties compete for guests with other resorts and hotels, a number of which have greater marketing and financial resources than our lessees or the Resort/Hotel property managers;

- If there is an increase in operating costs resulting from inflation or other factors, we or the property managers may not be able to offset the increase by increasing room rates;

- Our Resort/Hotel Properties are subject to fluctuating and seasonal demands for business travel and tourism; and

- Our Resort/Hotel Properties are subject to general and local economic conditions that may affect the demand for travel in general and other factors that are beyond our control, such as acts of terrorism.

Military actions against terrorists, new terrorist attacks (actual or threatened) and other political events could cause a lengthy period of uncertainty that might increase customer reluctance to travel and therefore adversely affect our results of operations and our ability to meet our obligations.

**Development and construction risks could adversely affect our profitability.**

We currently are developing, expanding or renovating some of our office or Resort/Hotel Properties. In addition, our Resort Residential Development Properties engage in the development of raw land and construction of single-family homes, condominiums, town homes and time-share units. These activities may be exposed to the following risks, each of which could adversely affect our results of operations and our ability to meet our obligations:

- We may be unable to obtain, or suffer delays in obtaining, necessary zoning, land-use, building, occupancy and other required governmental permits and authorizations, which could result in increased costs or our abandonment of these activities;

- We may incur costs for development, expansion or renovation of a property which exceed our original estimates due to increased costs for materials or labor or other costs that were unexpected;

- We may not be able to obtain financing with favorable terms, which may make us unable to proceed with our development and other related activities on the schedule we originally planned or at all;

- We may be unable to complete construction and sale or lease-up of a lot, office property or resort residential development unit on schedule, which could result in increased debt service expense or construction costs;

- We may lease, rent or sell developed properties at below expected rental rates, room rates or unit prices; and

Occupancy rates, rents or unit sales at newly completed properties may fluctuate depending on a number of factors, including market and economic conditions, and may result in our investment not being profitable.

Additionally, the time frame required for development, construction and lease-up of these properties means that we may have to wait a few years for a significant cash return. As a REIT, we are required to make cash distributions to our shareholders. If our cash flows from operations are not sufficient, we may be forced to borrow to fund these distributions, which could affect our ability to meet our other obligations.

**Many real estate costs are fixed, even if income from our properties decreases.**

Our financial results depend primarily on leasing space in our office properties to tenants, renting rooms at our resorts and hotels and successfully developing and selling lots, single-family homes, condominiums, town homes and time-share units at our residential development properties, in each case on terms favorable to us. Fixed costs associated with real estate investment, such as real estate taxes and insurance costs, generally do not decrease even when a property is not fully occupied, or the rate of sales at a project decreases, or other circumstances cause a reduction in income from the investment.

**Payment of distributions on any class of our shares may be adversely affected by the level of our debt and the terms and number of our other shares that rank on an equal basis with or senior to that class of shares.**

Payment of distributions due on our common shares is subordinated to distributions on our preferred shares, and distributions on both our common and our preferred shares will be subordinated to all of our existing and future debt and will be structurally subordinated to the payment of dividends and distributions on equity, if any, issued by our subsidiaries, including the Operating Partnership. In addition, we may issue additional shares of the same or another class or series of shares that rank on a parity with any class or series of our shares as to the payment of distributions and the amounts payable upon liquidation, dissolution or winding up of our business.

**The amount of debt that we have and the restrictions imposed by that debt could adversely affect our business and our financial condition.**

We have a substantial amount of debt. As of December 31, 2006, we had approximately $2.3 billion of consolidated debt outstanding, of which approximately $1.5 billion was secured by approximately 57% of our gross total assets.

Our organizational documents do not limit the level or amount of debt that we may incur. We do not have a policy limiting the ratio of our debt to our total capitalization or assets. The amount of debt we have and may have outstanding could have important consequences to you. For example, it could:

- make it difficult to satisfy our debt service requirements;
- prevent us from making distributions on our outstanding common shares and preferred shares;
- require us to dedicate a substantial portion of our cash flow from operations to payments on our debt, thereby reducing funds available for operations, property acquisitions and other appropriate business opportunities that may arise in the future;
- require us to dedicate increased amounts of our cash flow from operations to payments on our variable rate, unhedged debt if interest rates rise;
- limit our flexibility in planning for, or reacting to, changes in our business and the factors that affect the profitability of our business;
- limit our ability to obtain additional financing, if we need it in the future for working capital, debt refinancing, capital expenditures, acquisitions, development or other general corporate purposes; and
- limit our flexibility in conducting our business, which may place us at a disadvantage compared to competitors with less debt.

Our ability to make scheduled payments of the principal of, to pay interest on, or to refinance, our indebtedness will depend on our future performance, which to a certain extent is subject to economic, financial, competitive and other factors beyond our control. There can be no assurance that our business will continue to generate sufficient cash flow from operations in the future to service our debt or meet our other cash needs. If we are unable to do so, we may be required to refinance all or a portion of our existing debt, or to sell assets or obtain additional financing. We cannot assure you that any such refinancing, sale of assets or additional financing would be possible on terms that we would find acceptable.

If we were to breach certain of our debt covenants, our lenders could require us to repay the debt immediately, and, if the debt is secured, could immediately take possession of the property securing the loan. In addition, if any other lender declared its loan in an amount in excess of $5.0 million due and payable as a result of a default, the holders of our public and private notes, along with the lenders under our credit facility and certain other lenders would be able to require that those debts be paid immediately. As a result, any default under our debt

Table of Contents

covenants could have an adverse effect on our financial condition, results of operations and our ability to meet our obligations.

**We are obligated to comply with financial and other covenants in our debt that could restrict our operating activities, and the failure to comply could result in defaults that accelerate the payment under our debt.**

Our secured debt generally contains customary covenants, including, among others, provisions:

- relating to the maintenance of the property securing the debt;
- relating to minimum acceptable insurance coverage on our properties;
- restricting our ability to pledge assets or create other liens;
- restricting our ability to incur additional debt;
- restricting our ability to amend or modify existing leases; and
- restricting our ability to enter into transactions with affiliates.

Our unsecured debt generally contains various restrictive covenants. The covenants in our unsecured debt include, among others, provisions restricting our ability to:

- incur additional debt;
- incur additional secured debt and subsidiary debt;
- make certain distributions, investments and other restricted payments, including distribution payments on our or our subsidiaries outstanding common and preferred equity;
- limit the ability of restricted subsidiaries to make payments to us;
- enter into transactions with affiliates;
- create certain liens;
- enter into certain sale-leaseback transactions; and
- consolidate, merge or sell all or substantially all of our assets.

In addition, certain covenants in our bank facilities require us and our subsidiaries to maintain certain financial ratios, which include minimum debt service ratios, maximum leverage ratios, maximum distributions on preferred and common shares and, in the case of the Operating Partnership, a minimum tangible net worth limitation and a fixed charge coverage ratio. The indentures under which our senior unsecured debt have been issued require us to meet thresholds for a number of customary financial and other covenants, including maximum leverage ratios, minimum debt service coverage ratios, maximum secured debt as a percentage of total undepreciated assets, and ongoing maintenance of unencumbered assets, in order to incur additional debt.

Any of the covenants described in this risk factor may restrict our operations and our ability to pursue potentially advantageous business opportunities. Our failure to comply with these covenants could also result in an event of default that, if not cured or waived, could result in the acceleration of all or a substantial portion of our debt.

**Many factors affect the trading price of our shares.**

As with other publicly traded securities, the trading price of our shares will depend on a number of factors that change from time to time, including:

- our financial condition, performance and prospects;

the market for similar securities;

additional issuance of other classes or series of our shares, particularly preferred shares, or the issuance of debt securities;

the amount of distributions paid on our common and preferred shares;

an announcement regarding future dividend pay-out ranges on our common shares;

general economic and financial market conditions; and

prevailing interest rates, increases in which may have a negative effect on the trading value of our preferred shares.

**Rising interest rates could adversely affect our cash flow and the market price of our outstanding debt securities and preferred shares.**

Of our approximately $2.3 billion of debt outstanding as of December 31, 2006, approximately $479.6 million bears interest at variable rates and is unhedged. We also may borrow additional funds at variable interest rates in the future. To mitigate part of this risk, we have entered, and in the future may enter into other transactions to limit our exposure to rising interest rates. Increases in interest rates, or the loss of the benefits of any interest rate hedging arrangements, would increase our interest expense on our variable rate debt, which could adversely affect cash flow and our ability to service our debt and meet our obligations. In addition, an increase in market interest rates may lead purchasers of our securities to demand a higher annual yield, which could adversely affect the market price of our outstanding debt securities and preferred shares.

**The level of our distributions to our common shareholders is highly dependent on the implementation of our Strategic Plan.**

Lower occupancy levels, reduced rental rates, increased leasing costs and reduced revenues as a result of asset sales have had the effect of reducing our cash flow from operations. For year ended December 31, 2006, our cash flow from operations was insufficient to fully cover the distributions on our common shares. We funded this shortfall primarily with a combination of proceeds from asset sales and joint ventures and borrowings under our credit facility. While we believe that cash flow from operations will be sufficient to cover our normal operating expenses, interest payments on our debt, distributions on our preferred shares, non-revenue enhancing capital expenditures and revenue enhancing capital expenditures (including property improvements, tenant improvements and leasing commissions) in 2007, if our Board of Trustees continues to declare distributions on our common shares at current levels, we expect that our cash flow from operations will continue to be insufficient to fully cover distributions to our common shareholders in 2007. We intend to use proceeds from asset sales and joint ventures pursuant to our Strategic Plan to cover this shortfall. In addition, as we implement our Strategic Plan, we intend to align our dividend with industry-accepted pay-out ranges to allow for retention of capital for growth.

**The terms of some of our debt may prevent us from paying distributions on our shares.**

Some of our debt limits the Operating Partnership s ability to make some types of payments on equity and other distributions to us, which would limit our ability to make some types of payments, including payment of distributions on our shares, unless we meet certain financial tests or are required to make the distributions to maintain our qualification as a REIT. As a result, if we are unable to meet the applicable financial tests, we may not be able to pay distributions on our shares in one or more periods.

**Mezzanine loans involve greater risks of loss than senior loans secured by income producing properties.**

We invest in mezzanine loans that typically take the form of limited recourse loans made to a special purpose entity which is the direct or indirect parent of another special purpose entity owning a commercial real estate property. These mezzanine loans are secured by a pledge of the ownership interest in the property owner (or in an entity that directly or indirectly owns the property owner) and are thus structurally subordinate to a conventional first mortgage loan made to the property owner. We also offer mezzanine financing by taking a junior participating interest in a first mortgage loan.

These types of investments involve more risk than conventional senior mortgage lending directly secured by real property because these investments are structurally or contractually subordinated to the senior loans (or senior participations) and may become unsecured as a result of foreclosure by a senior lender on its collateral. While we will typically have cure rights with respect to loans senior to ours and the right to purchase these senior loans if in default, an exercise of this right may require our investing substantial additional capital on short notice to avoid loss of our initial investment.

In addition, mezzanine loans usually have higher loan-to-value ratios than conventional mortgage loans, resulting in less equity in the property and increasing the risk of loss of principal. Reflecting the risk of these loans, mezzanine borrowers are generally required to pay significantly higher rates of interest than conventional mortgage loan borrowers, increasing borrowers cash-flow vulnerability. In the event of a bankruptcy of the borrower, we may not have full recourse to the borrower s assets, or the assets of the borrower may not be sufficient to satisfy our mezzanine loan. Additionally, we have no right to participate in the bankruptcy proceedings of any senior borrower (including the property owner). While we normally obtain recourse guaranties to protect against a voluntary bankruptcy or uncontested involuntary bankruptcy of the mezzanine borrower and the senior borrowers, these guaranties may not fully cover our debt.

As a result of any or all of the foregoing, we may not recover some or all of our mezzanine loan investment.

**The use of repurchase agreements to fund our mezzanine notes exposes us to risks.**

We finance certain of our mezzanine loans through the use of warehouse facilities governed by repurchase agreements. We sell those mezzanine loans financed through a warehouse facility to a counterparty and agree to repurchase the same loans at a price equal to the original sales price plus periodic interest payments. Our repurchase agreement counterparties are commercial and investment banks. During the term of the repurchase agreement, we receive the principal and interest payments on the related mezzanine loan and pay interest to the counterparty. The use of this type of leverage to finance our mezzanine investments involves a number of risks, including the following:

*If we are unable to renew our borrowings at favorable rates, it may force us to sell assets or find other financing and our profitability may be adversely affected.* If we are not able to renew or replace maturing borrowings, we would be forced to sell some of our assets under possibly adverse market conditions, which may adversely affect our profitability.

*A decline in the market value of the pool of assets in the warehouse facility may result in margin calls that may force us to sell assets under adverse market conditions.* The market value of a pool of assets in a warehouse facility is valued by the lender in order to determine the advance rate, and to ensure adequate collateral secures the advances under the repurchase agreement. Repurchase agreements involve the risk that the market value of the securities sold by us may decline and that we will be required to post additional collateral, reduce the amount borrowed or suffer forced sales of the collateral. If forced sales were made at prices lower than the carrying value of the collateral, we would experience additional losses.

*If a mezzanine loan defaults, we may not be able to fund the repurchase of the loan from our warehouse facility or the stabilization of the property by drawings under our credit facility which could cause liquidity concerns.* If a default occurs under one of our mezzanine loans and, if financed under our warehouse facilities, it may need to be repurchased from the warehouse lender on two business days notice. If we do not have sufficient liquidity under our credit facility for funds to repurchase these loans, the counterparty may foreclose on all of the pledged assets in the facility. Even if, following a default on a mezzanine loan, we are able to foreclose on the collateral, which is a direct or indirect equity interest in an entity owning real property, we may need to commit substantial additional capital to stabilize the property and prevent defaults on other loans outstanding on the real property.

*Our use of repurchase agreements to borrow money may give our lenders greater rights in the event of bankruptcy.* Borrowings made under repurchase agreements may qualify for special treatment under the U.S. Bankruptcy Code, which may make it difficult for us to recover our pledged assets if a lender files for bankruptcy. In addition, if we were to file for bankruptcy, lenders under our repurchase agreements may be able to avoid the automatic stay provisions of the U.S. Bankruptcy Code and take possession of, and liquidate, the assets we pledged under these agreements without the delay associated with the automatic stay.

**Environmental problems are possible and may be costly.**

Under various federal, state and local laws, ordinances and regulations, we may be required to investigate and clean up certain hazardous or toxic substances released on or in properties we own or operate, and also may be required to pay other costs relating to hazardous or toxic substances. This liability may be imposed without regard to whether we knew about the release of these types of substances or were responsible for their release. The presence of contamination or the failure to remediate properly contamination at any of our properties may adversely affect our ability to sell or lease those properties or to borrow using those properties as collateral. The costs or liabilities could exceed the value of the affected real estate. We have not been notified by any governmental authority, however, of any material environmental non-compliance, liability or other environmental claim in connection with any of our properties, and we are not aware of any other environmental condition with respect to any of our properties that management believes would have a material adverse effect on our business, assets or results of operations taken as a whole.

The uses of any of our properties prior to our acquisition of the property and the building materials used at the property are among the property-specific factors that will affect how the environmental laws are applied to our properties. In general, before we purchased each of our properties, independent environmental consultants conducted Phase I environmental assessments, which generally do not involve invasive techniques such as soil or ground water sampling, and where indicated, based on the Phase I results, conducted Phase II environmental assessments which do involve this type of sampling. None of these assessments revealed any materially adverse environmental condition relating to any particular property not previously known to us. We believe that all of those previously known conditions either have been remediated or are in the process of being remediated at this time. There can be no assurance, however, that environmental liabilities have not developed since these environmental assessments were prepared or that future uses or conditions (including changes in applicable environmental laws and regulations) or new information about previously unidentified historical conditions will not result in the imposition of environmental liabilities. If we are subject to any material environmental liabilities, the liabilities could adversely affect our results of operations and our ability to meet our obligations.

**Compliance with the Americans with Disabilities Act could be costly.**

Under the Americans with Disabilities Act of 1990, all public accommodations and commercial facilities must meet certain federal requirements related to access and use by disabled persons. Compliance with the ADA requirements could involve removal of structural barriers from certain disabled persons entrances. Other federal, state and local laws may require modifications to or restrict further renovations of our properties with respect to such accesses. Although we believe that our properties are substantially in compliance with present requirements, noncompliance with the ADA or related laws or regulations could result in the United States government s imposition of fines or in the award to private litigants of damages against us. Costs such as these, as well as the general costs of compliance with these laws or regulations, may adversely affect our ability to meet our obligations.

**Our insurance coverage on our properties may be inadequate or unavailable, which may have a material adverse effect on our business.**

We currently carry insurance on all of our properties, including insurance for property damage and third-party liability. We believe this coverage is of the type and amount customarily obtained for or by an owner of real property assets. We intend to obtain similar insurance coverage on subsequently acquired properties. Our existing primary insurance policies expire on November 1 annually.

In the future, we may be unable to renew or duplicate our current insurance coverage in adequate amounts or at reasonable prices. In addition, due to events such as the September 11, 2001 terrorist attacks and the recent hurricanes in Louisiana, Mississippi and Florida, insurance companies may no longer offer coverage against certain types of losses, such as losses due to terrorist acts, environmental liabilities, or other catastrophic events including named storms and floods, or, if offered, the expense of obtaining these types of insurance may increase dramatically or may not be justifiable. We therefore may cease to have insurance coverage against certain types of losses and/or there may be decreases in the limits of insurance available. In 2006, insurance companies lowered the amount of named storm insurance offered substantially, or, where offered, the expense increased dramatically. As a result, the amount of named storm coverage we obtained is significantly lower than 2005. If an uninsured loss or a loss in excess of our insured limits occurs, we could lose all or a portion of the capital we have invested in a property, as well as the anticipated future revenue from the property, but still remain obligated for any mortgage debt or other financial obligations related to the property. We cannot guarantee that material losses in excess of insurance proceeds will not occur in the future. If any of our properties were to experience a catastrophic loss, it could seriously disrupt our operations, delay revenue and result in large expenses to repair or rebuild the property. Also, due to inflation, changes in codes and ordinances, environmental considerations and other factors, it may not be feasible to use insurance proceeds to replace a building after it has been damaged or destroyed. Events such as these could adversely affect our results of operations and our ability to meet our obligations.

In addition, the debt we use to finance our properties includes covenants that require us to maintain designated levels of insurance coverage with insurers having minimum credit ratings. For example, certain of our loans secured by our coastal properties include requirements that we maintain minimum levels of named storm insurance. If we are unable to maintain insurance that meets the requirements of our lenders and if we are unable to amend or obtain waivers of those requirements, we could be in default under these loan agreements, which could have a material adverse effect on our business.

**Competition for acquisitions and dispositions could adversely affect us.**

We may compete for available investment opportunities with entities that have greater liquidity or financial resources. Several real estate companies may compete with us in seeking properties for acquisition or land for development and prospective tenants, guests or purchasers. This competition may increase the costs of any acquisitions that we make and adversely affect our results of operations and our ability to meet our obligations by:

reducing the number of suitable investment opportunities offered to us; and
increasing the bargaining power of property owners.

We face similar competition with other real estate companies in our efforts to dispose of properties, which may result in lower sales prices. In addition, if a competitor succeeds in making an acquisition in a market in which our properties compete, ownership of that investment by a competitor may adversely affect our results of operations and our ability to meet our obligations by:

- interfering with our ability to attract and retain tenants, guests or purchasers; and
- adversely affecting our ability to minimize expenses of operation.

**Acquisitions may fail to perform as expected.**

We focus our investment strategy on investment opportunities and markets that offer attractive returns on our invested capital, primarily within our Office Property Segment, with a strategy of acquiring properties at a cost significantly below that which would be required to develop a comparable property. Acquisition of properties entails risks that include the following, any of which could adversely affect our results of operations and our ability to meet our obligations:

- We may not be able to identify suitable properties to acquire or may be unable to complete the acquisition of the properties we select for acquisition;

- We may not be able to integrate new acquisitions into our existing operations successfully;

- Our estimate of the costs of improving, repositioning or redeveloping an acquired property may prove to be too low, and, as a result, the property may fail to meet our estimates of the profitability of the property, either temporarily or for a longer time;

- Office properties, resorts or hotels we acquire may fail to achieve the occupancy and rental or room rates we anticipate at the time we make the decision to invest in the properties, resulting in lower profitability than we expected in analyzing the properties;

- Our pre-acquisition evaluation of the physical condition of each new investment may not detect certain defects or necessary repairs until after the property is acquired, which could significantly increase our total acquisition costs; and

- Our investigation of a property or building prior to its acquisition, and any representations we may receive from the seller, may fail to reveal various liabilities, which could effectively reduce the cash flow from the property or building, or increase our acquisition cost.

**We are dependent on our key personnel whose continued service is not guaranteed.**

Our officers, particularly John Goff and Dennis H. Alberts, are critical to the management and direction of our business, and to our implementation of our Strategic Plan. Our future success depends, in large part, on our ability to retain these officers, our Trust Managers and other capable management personnel. We do not presently have employment agreements with any of our executive officers. Although we believe that we will be able to attract and retain talented personnel and replace key personnel should the need arise, including by making retention payments in connection with the Strategic Plan, our inability to do so could disrupt our operations, including implementation of our Strategic Plan. We do not have key-man life insurance for our executive officers.

**Provisions of our declaration of trust and bylaws could inhibit changes in control or discourage takeover attempts beneficial to our shareholders.**

There are certain provisions of our declaration of trust and bylaws that may have the effect of discouraging, delaying or making more difficult a change in control and preventing the removal of incumbent directors. The existence of these provisions may discourage third-party bids and reduce any premiums paid to you for common shares that you own. These include a staggered Board of Trust Managers, which makes it more difficult for a third party to gain control of our Board, and the ownership limit described below. In addition, any future series of preferred shares may have certain voting provisions that could delay or prevent a change of control or other transaction that might involve a premium price or otherwise be beneficial to our security holders. The declaration of trust also establishes special requirements with respect to business combinations, including certain issuances of equity securities, between us and an interested shareholder, and mandates procedures for obtaining voting rights with respect to control shares acquired in a control share acquisition.

**Your ownership of our shares is subject to limitation for REIT tax purposes.**

To remain qualified as a REIT for federal income tax purposes, not more than 50% in value of our outstanding shares may be owned, directly or indirectly, by five or fewer individuals (as defined in the federal income tax laws applicable to REITs) at any time during the last half of any taxable year, and our outstanding shares must be beneficially owned by 100 or more persons at least 335 days of a taxable year. To facilitate maintenance of our REIT qualification, our declaration of trust, subject to certain exceptions, prohibits ownership by any single shareholder of more than 8.0% of our issued and outstanding common shares or such greater percentage as established by our Board of Trust Managers, but in no event greater than 9.9%, or more than 9.9% of any class of our issued and outstanding preferred shares. We refer to these limits together as the ownership limit. In addition, the declaration of trust prohibits ownership by Richard E. Rainwater, the Chairman of our Board of Trust Managers, together with certain of his affiliates or relatives, initially, of more than 8.0% and subsequently, of more than 9.5% of our issued and outstanding common shares. We refer to this limit as the Rainwater ownership limit. Any transfer of shares may be null and void if it causes a person to violate the ownership limit, or Mr. Rainwater, together with his affiliates and relatives, to violate the Rainwater ownership limit, and the intended transferee or holder will acquire no rights in the shares. Those shares will automatically convert into excess shares, and the shareholder s rights to distributions and to vote will terminate. The shareholder would have the right to receive payment of the purchase price for such excess shares and certain distributions upon our liquidation. Excess shares will be subject to repurchase by us at our election. While the ownership limit and the Rainwater ownership limit help preserve our status as a REIT, they could also delay or prevent any person or small group of persons from acquiring, or attempting to acquire, control of us and, therefore, could adversely affect our shareholders ability to realize a premium over the then-prevailing market price for their shares.

**The number of shares available for future sale could adversely affect the market price of our publicly traded securities.**

We have entered into various private placement transactions whereby units of limited partnership interests in our Operating Partnership were issued in exchange for properties or interests in properties. These units and interests are currently exchangeable for our common shares on the basis of two shares for each one unit or, at our option, an equivalent amount of cash. Upon exchange for our common shares, those common shares may be sold in the public market pursuant to registration rights. As of December 31, 2006, approximately 11,320,798 units were outstanding, 8,551,173 of which were exchangeable for 17,102,346 of our common shares or, at our option, an equivalent amount of cash. In addition, as of December 31, 2006, the Operating Partnership had outstanding options to acquire approximately 3,159,560 units, of which 482,408 were exercisable and exchangeable for 964,816 of our common shares or, at our option, an equivalent amount of cash. These options were exercisable at a weighted average exercise price of $34 per unit, or $17 per common share, with a weighted average remaining contractual life of five years. We have also reserved a number of common shares for issuance pursuant to our employee benefit plans, and such common shares will be available for sale from time to time. As of December 31, 2006, we had outstanding options to acquire approximately 4,562,950 common shares, of which approximately 4,266,446 options were exercisable at a weighted average exercise price of $20, with a weighted average remaining contractual life of three years. We cannot predict the effect that future sales of common shares, or the perception that such sales could occur, will have on the market prices of our equity securities.

**Failure to qualify as a REIT would cause us to be taxed as a corporation, which would substantially reduce funds available for payment of distributions.**

We intend to continue to operate in a manner that allows us to meet the requirements for qualification as a REIT under the Internal Revenue Code of 1986, as amended, which we refer to as the Code. A REIT generally is not taxed at the corporate level on income it distributes to its shareholders, as long as it distributes at least 90 percent of its income to its shareholders annually and satisfies certain other highly technical and complex requirements. Unlike many REITs, which tend to make only one or two types of real estate investments, we invest in a broad range of real estate products. Several of our investments also are more complicated than those of other REITs. As a result, we are likely to encounter a greater number of interpretative issues under the REIT qualification rules, and more issues which lack clear guidance, than are other REITs. We, as a matter of policy, consult with outside tax counsel in structuring our new investments in an effort to satisfy the REIT qualification rules.

We must meet the requirements of the Code in order to qualify as a REIT now and in the future, so it is possible that we will not continue to qualify as a REIT in the future. The laws and regulations governing federal income taxation are the subject of frequent review and amendment, and proposed or contemplated changes in the laws or regulations may affect our ability to qualify as a REIT and the manner in which we conduct our business. If we fail to qualify as a REIT for federal income tax purposes, we would not be allowed a deduction for distributions to our shareholders in computing taxable income and would be subject to federal income tax at regular corporate rates. In addition to these taxes, we may be subject to the federal alternative minimum tax. Unless we are entitled to relief under certain statutory provisions, we could not elect to be taxed as a REIT for four taxable years following any year during which we were first disqualified. Therefore, if we lose our REIT status, we could be required to pay significant income taxes, which would reduce our funds available for investments or for distributions to our shareholders. This would likely adversely affect the value of your investment in us. In addition, we would no longer be required by law or our operating agreements to make any distributions to our shareholders.

**The lower tax rate on dividends from regular corporations may cause investors to prefer to hold stock in regular corporations instead of REITs.**

On May 28, 2003, the President signed into law the Jobs and Growth Tax Relief Reconciliation Act of 2003, which we refer to as the Act. Under the Act, the current maximum tax rate on the long-term capital gains of non-corporate taxpayers is reduced to 15% for the tax years beginning on or before December 31, 2008. The Act also reduced the tax rate on qualified dividend income to the maximum capital gains rate. Because, as a REIT, we are not generally subject to tax on the portion of our REIT taxable income or capital gains distributed to our shareholders, our distributions are not generally eligible for this new tax rate on dividends. As a result, the non-capital-gain portion of our REIT distributions generally continues to be taxed at the higher tax rates applicable to ordinary income. Without further legislation, the maximum tax rate on long-term capital gains will revert to 20% in 2009, and dividends will again be subject to tax at ordinary rates.

**Our results of operations and financial condition may be affected by a recently enacted law, which subjects us to the revised Texas franchise tax**.

On May 18, 2006, the Texas Governor signed into law HB 3, a franchise tax reform bill. The revised franchise tax, which will first be due in May 2008 based on 2007 financial results, will be a tax based on taxable margin (commonly referred to as the Margin Tax ). Unlike the existing franchise tax, the Margin Tax will be imposed on substantially all businesses that have statutory liability protection, including Texas real estate investment trusts and limited partnerships, such as the Company and the Operating Partnership. Payment of the Margin Tax may adversely affect our results of operations and financial condition.

**Item 1B. Unresolved Staff Comments.**

We have received no written comments from the Commission staff regarding our periodic or current reports in the 180 days preceding December 31, 2006, that remain unresolved.

**Item 2. Properties**

We consider all of our Properties to be in good condition, well-maintained, suitable and adequate to carry on our business.

**Office Properties**

As of December 31, 2006, we owned or had an interest in 71 Office Properties, located in 26 metropolitan submarkets in eight states, with an aggregate of approximately 27.6 million net rentable square feet. Our Office Properties are located primarily in the Houston and Dallas, Texas, metropolitan areas. As of December 31, 2006, our Office Properties in Houston and Dallas represented an aggregate of approximately 66% of our office portfolio based on total net rentable square feet (39% for Houston and 27% for Dallas).

Table of Contents

**Office Property Table** (1)

The following table shows, as of December 31, 2006, certain information about our Office Properties. In the table, CBD means central business district.

| State, City, Property | No. of Properties | Submarket | Year Completed | Net Rentable Area (Sq. Ft.) | Economic Occupancy Percentage | Weighted Average Full-Service Rental Rate Per Occupied Sq. Ft. (2) | Our Ownership Percentage (1) |
|---|---|---|---|---|---|---|---|
| ***Texas*** | | | | | | | |
| **Dallas** | | | | | | | |
| The Crescent | 2 | Uptown/Turtle Creek | 1985 | 1,299,522 | 98.5 | 34.49 | 24% |
| Fountain Place | 1 | CBD | 1986 | 1,200,266 | 91.2 | 21.38 | 24% |
| Trammell Crow Center | 1 | CBD | 1984 | 1,128,331 | 90.1 | 24.20 | 24% |
| Stemmons Place | 1 | Stemmons Freeway | 1983 | 634,381 | 66.4 | 16.82 | 100% |
| Spectrum Center | 1 | Quorum/Bent Tree | 1983 | 598,250 | 92.1 | 20.60 | 100% |
| 125 E. John Carpenter Freeway | 1 | Las Colinas | 1982 | 446,031 | 88.3 | 20.78 | 100% |
| The Aberdeen | 1 | Quorum/Bent Tree | 1986 | 319,758 | 95.5 | 16.80 | 100% |
| MacArthur Center I & II | 1 | Las Colinas | 1982/1986 | 298,161 | 81.0 | 19.01 | 100% |
| Stanford Corporate Centre | 1 | Quorum/Bent Tree | 1985 | 274,684 | 88.5(3) | 21.29 | 100% |
| Palisades Central II | 1 | Richardson | 1985 | 240,935 | 95.3 | 20.83 | 100% |
| 3333 Lee Parkway | 1 | Uptown/Turtle Creek | 1983 | 233,543 | 98.3 | 19.47 | 100% |
| The Addison | 1 | Quorum/Bent Tree | 1981 | 215,016 | 100.0 | 23.09 | 100% |
| Palisades Central I | 1 | Richardson | 1980 | 180,503 | 76.3 | 18.16 | 100% |
| Greenway II | 1 | Richardson | 1985 | 154,329 | 99.9 | 18.03 | 100% |
| Greenway I & IA | 2 | Richardson | 1983 | 146,704 | 74.7 | 16.64 | 100% |
| Subtotal/Weighted Average | 17 | | | 7,370,414 | 89.9% | $ 23.38 | 63% |
| **Fort Worth** | | | | | | | |
| Carter Burgess Plaza | 1 | CBD | 1982 | 954,895 | 96.4% | $ 19.88 | 100% |
| **Houston** | | | | | | | |
| Greenway Plaza | 10 | Greenway Plaza | 1969-1982 | 4,348,052 | 86.5% | $ 19.67 | 100% |
| Houston Center | 4 | CBD | 1974-1983 | 2,960,544 | 91.5 | 19.96 | 24% |
| Post Oak Central | 3 | West Loop/Galleria | 1974-1981 | 1,279,759 | 96.7 | 20.90 | 24% |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Fulbright Tower | 1 | CBD | 1982 | 1,247,061 | 73.4(3) | 20.37 | 24% |
| Five Post Oak Park | 1 | West Loop/Galleria | 1986 | 567,396 | 88.9 | 19.04 | 30% |
| BriarLake Plaza | 1 | Westchase | 2000 | 502,410 | 87.3(3) | 24.61 | 30% |
| Subtotal/Weighted Average | 20 | | | 10,905,222 | 87.7% | $ 20.17 | 55% |
| **Austin** | | | | | | | |
| 816 Congress | 1 | CBD | 1984 | 433,024 | 77.3% | $ 20.81 | 100% |
| 301 Congress Avenue | 1 | CBD | 1986 | 418,338 | 82.1 | 23.03 | 50% |
| Austin Centre | 1 | CBD | 1986 | 343,664 | 97.2 | 18.95 | 100% |
| The Avallon | 3 | Northwest | 1993/1997 | 318,217 | 93.1 | 20.50 | 100% |
| Subtotal/Weighted Average | 6 | | | 1,513,243 | 86.5% | $ 20.84 | 86% |
| ***Colorado*** | | | | | | | |
| **Denver** Johns Manville Plaza | 1 | CBD | 1978 | 675,400 | 91.5% | $ 19.84 | 100% |
| 707 17th Street | 1 | CBD | 1982 | 550,805 | 91.9 | 20.42 | 100% |
| Regency Plaza | 1 | Denver Technology Center | 1985 | 309,862 | 86.5(3) | 18.76 | 100% |
| Peakview Tower | 1 | Greenwood Village | 2001 | 264,149 | 91.4 | 24.05 | 100% |
| 55 Madison | 1 | Cherry Creek | 1982 | 137,176 | 93.8 | 19.03 | 100% |
| The Citadel | 1 | Cherry Creek | 1987 | 130,652 | 92.4 | 24.94 | 100% |
| 44 Cook | 1 | Cherry Creek | 1984 | 124,174 | 81.2 | 18.87 | 100% |
| Subtotal/Weighted Average | 7 | | | 2,192,218 | 90.5% | $ 20.56 | 100% |
| **Colorado Springs** | | | | | | | |
| Briargate Office and Research Center | 1 | Northeast | 1988 | 260,046 | 87.3% | $ 18.16 | 100% |

Table of Contents

**Office Property Table Continued**[1]

| State, City, Property | No. of Properties | Submarket | Year Completed | Net Rentable Area (Sq. Ft.) | Economic Occupancy Percentage | Weighted Average Full-Service Rental Rate Per Occupied Sq. Ft. [2] | Our Ownership Percentage [1] |
|---|---|---|---|---|---|---|---|
| ***Florida*** | | | | | | | |
| **Miami** | | | | | | | |
| Miami Center | 1 | CBD | 1983 | 782,211 | 93.2% [3] | $ 32.44 | 40% |
| Datran Center | 2 | Kendall/Dadeland | 1986/1988 | 476,412 | 94.3 | 29.01 | 100% |
| The Alhambra | 2 | Coral Gables | 1961/1987 | 325,005 | 92.0 | 30.47 | 100% |
| The BAC Colonnade Building | 1 | Coral Gables | 1989 | 218,170 | 89.6 | 33.40 | 100% |
| Subtotal/Weighted Average | 6 | | | 1,801,798 | 92.8% | $ 31.28 | 74% |
| ***California*** | | | | | | | |
| **Orange County** | | | | | | | |
| Dupont Centre | 1 | Airport Office Area | 1986 | 250,782 | 97.3% | $ 27.41 | 100% |
| ***Nevada*** | | | | | | | |
| **Las Vegas** | | | | | | | |
| Hughes Center | 8 | Central East | 1986 - 1999 | 1,111,388 | 97.5% | $ 33.60 | 100% |
| ***Georgia*** | | | | | | | |
| **Atlanta** | | | | | | | |
| One Buckhead Plaza | 1 | Buckhead | 1987 | 461,669 | 91.3% | $ 30.48 | 35% |
| One Live Oak | 1 | Buckhead | 1981 | 201,488 | 88.7 | 24.24 | 100% |
| Subtotal/Weighted Average | 2 | | | 663,157 | 90.5% | $ 28.62 | 55% |
| ***Washington*** | | | | | | | |
| **Seattle** | | | | | | | |
| Exchange Building | 1 | CBD | 1930/2001 | 295,515 | 99.0% | $ 24.57 | 100% |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| **Total Office Portfolio Excluding Properties Not Stabilized** | 70 | | | 27,318,678 | 89.8% [3] | $ 22.78[4] | 68% |
| **PROPERTIES NOT STABILIZED** | | | | | | | |
| ***Arizona*** | | | | | | | |
| **Phoenix** | | | | | | | |
| Financial Plaza [5] | 1 | Mesa | 1986 | 309,983 | 80.6% | $ 25.06 | 100% |
| **Total Office Portfolio** | 71 | | | 27,628,661 | | | 69% |

(1) Office Property Table data is presented without adjustments to reflect our actual ownership percentage in joint ventured properties. Our actual ownership percentage in each property has been included for informational purposes.

(2) Calculated in accordance with GAAP based on base rent payable as of December 31, 2006, giving effect to free rent and scheduled rent increases and including adjustments for expenses payable by or

reimbursable from customers. The weighted average full-service rental rate for the El Paso lease (Greenway Plaza, Houston, Texas) reflects weighted average full-service rental rate over the shortened term (due to lease termination effective as of December 31, 2007) and excludes the impact of the net lease termination fee being amortized into revenue through December 31, 2007.

(3) Leases have been executed at certain Office Properties but had not commenced as of December 31, 2006. If such leases had commenced as of December 31, 2006, the percent leased for Office Properties would have been 92.6%. Properties whose percent leased exceeds

economic occupancy by 5 percentage points or more are as follows: Stanford Corporate Centre 94.1%, Fullbright Tower 91.7%, BriarLake Plaza 97.3, Regency Plaza 93.8% and Miami Center 98.8%.

(4) The weighted average full-service cash rental rate per square foot calculated based on base rent payable for Office Properties as of December 31, 2006, without giving effect to free rent and scheduled rent increases that are taken into consideration under GAAP but including adjustments for expenses paid by or reimbursed from customers is $22.55.

(5) Property statistics exclude Financial Plaza (acquired January 2006). This office property will be

included in portfolio statistics once stabilized. Stabilization is deemed to occur upon the earlier of (a) achieving 90% occupancy, (b) one year following the acquisition date or date placed in service (related to developments), or (c) two years following the acquisition date for properties which are being repositioned.

Table of Contents

The following table shows, as of December 31, 2006, the principal businesses conducted by the tenants at our Office Properties, based on tenants applicable 2-digit NAICS Code. Based on rental revenues from office leases in effect as of December 31, 2006, no single tenant accounted for more than 2.5% of our total Office Segment revenues for 2006.

| Industry Sector | Percent of Leased Sq. Ft. |
|---|---|
| Professional and Business Services | 32% |
| Financial Activities | 27 |
| Natural Resources, Mining, Construction | 18 |
| Information | 5 |
| Trade, Transportation, Utilities | 4 |
| Public Administration | 4 |
| Manufacturing | 4 |
| Leisure and Hospitality | 4 |
| Education and Health Services | 1 |
| Other Services | 1 |
| **Total Leased** | 100% |

**Aggregate Lease Expirations of Office Properties**

The following tables show schedules of lease expirations for leases in place as of December 31, 2006, for our total Office Properties and for Dallas, Houston and Austin, Texas; Denver, Colorado; Miami, Florida and Las Vegas, Nevada, individually, for each of the 10 years beginning 2007.

**Table of Contents**

**Total Office Portfolio**

| Year of Lease Expiration | Square Footage of Expiring Leases (Before Renewals and Relets) (1) | Signed Renewals and Relets of Expiring Leases (2) | Square Footage of Expiring Leases (After Renewals and Relets) (1) | % of Square Footage Expiring | Crescent s Share of Expiring Square Footage (After Renewals and Relets) | | Annual Full-Service Rent Under Expiring Leases (3) | % of Annual Full-Service Rent Expiring | | Annual Expiring PSF Full-Service Rent (3) | Number of Customers With Expiring Leases |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Q1 2007 | 1,529,501 | (1,008,685) | 520,816 | 2.2 | 356,887 | $ | 9,271,512 | 1.7 | $ | 17.80 | 192 |
| Q2 2007 | 676,701 | (250,959) | 425,742 | 1.8 | 262,548 | | 9,644,046 | 1.8 | | 22.65 | 76 |
| Q3 2007 | 401,377 | (109,255) | 292,122 | 1.2 | 238,632 | | 6,654,607 | 1.2 | | 22.78 | 65 |
| Q4 2007 | 597,153 | 173,046 | 770,199 | 3.2 | 426,478 | | 18,354,467 | 3.3 | | 23.83 | 63 |
| Total 2007 | 3,204,732(4) | (1,195,853) | 2,008,879(4) | 8.4% | 1,284,545 | $ | 43,924,632 | 8.0% | $ | 21.87 | 396 |
| Q1 2008 | 1,123,514 | (43,782) | 1,079,732 | 4.5 | 927,689 | $ | 24,763,642 | 4.5 | $ | 22.93 | 64 |
| Q2 2008 | 458,494 | (15,598) | 442,896 | 1.8 | 366,677 | | 10,610,394 | 1.9 | | 23.96 | 73 |
| Q3 2008 | 422,896 | (48,346) | 374,550 | 1.6 | 234,722 | | 8,845,813 | 1.6 | | 23.62 | 73 |
| Q4 2008 | 479,305 | (55,774) | 423,531 | 1.8 | 337,022 | | 10,120,853 | 1.8 | | 23.90 | 80 |
| Total 2008 | 2,484,209 | (163,500) | 2,320,709 | 9.7% | 1,866,110 | $ | 54,340,702 | 9.8% | $ | 23.42 | 290 |
| 2009 | 2,581,216 | (73,993) | 2,507,223 | 10.4 | 1,714,536 | $ | 58,488,832 | 10.6 | $ | 23.33 | 301 |
| 2010 | 2,111,239 | 169,775 | 2,281,014 | 9.5 | 1,462,189 | | 55,193,305 | 10.0 | | 24.20 | 250 |
| 2011 | 2,232,042 | 44,709 | 2,276,751 | 9.4 | 1,633,071 | | 56,202,831 | 10.2 | | 24.69 | 235 |
| 2012 | 1,498,307 | 317,784 | 1,816,091 | 7.5 | 1,410,079 | | 41,972,305 | 7.6 | | 23.11 | 111 |
| 2013 | 1,942,939 | 129,854 | 2,072,793 | 8.6 | 1,563,202 | | 47,746,034 | 8.7 | | 23.03 | 93 |
| 2014 | 3,273,247 | 187,140 | 3,460,387 | 14.3 | 2,172,475 | | 72,301,983 | 13.1 | | 20.89 | 48 |
| 2015 | 1,720,570 | 29,531 | 1,750,101 | 7.3 | 1,281,374 | | 40,189,224 | 7.3 | | 22.96 | 60 |
| 2016 | 1,213,952 | 11,713 | 1,225,665 | 5.1 | 539,239 | | 29,272,813 | 5.3 | | 23.88 | 59 |
| 2017 and thereafter | 1,853,425 | 542,840 | 2,396,265 | 9.8 | 1,450,899 | | 50,610,106 | 9.4 | | 21.12 | 36 |
| Total | 24,115,878 | | 24,115,878(5) | 100.0% | 16,377,719 | $ | 550,242,767 | 100.0% | $ | 22.82 | 1,879 |

(1) Square footage is presented without adjustment to reflect our actual ownership percentage in joint ventured properties.

(2) Signed renewals and relets extend the expiration dates of in-place leases to the end of the renewed or relet term.

(3) Calculated based on base rent payable under the lease for net rentable square feet expiring (after renewals and relets), giving effect to free rent and scheduled rent increases taken into account under GAAP and including adjustments for expenses payable by or reimbursable from customers based on current expense levels.

(4) As of December 31, 2006 leases totaling 1,825,691 square feet (including relets and renewals of 1,195,853 square feet and new leases of 629,838 square feet) have been signed and will commence during 2007. These signed leases represent approximately

57% of gross square footage expiring during 2007. Expiring square footage includes 247,361 square feet of month-to-month leases.

(5) Reconciliation of Occupied SF to Net Rentable Area:

| | |
|---|---|
| Occupied SF Per Above: | 24,115,878 |
| Non-revenue Generating Space: | 405,938 |
| Total Occupied Office SF: | 24,521,816 |
| Total Vacant SF: | 2,796,862 |
| Total Stabilized Office NRA: | 27,318,678 |

**Dallas Office Properties [1]**

| Year of Lease Expiration | Square Footage of Expiring Leases (Before Renewals and Relets) [1] | Signed Renewals and Relets of Expiring Leases [2] | Square Footage of Expiring Leases (After Renewals and Relets) [1] | % of Square Footage Expiring | Annual Full-Service Rent Under Expiring Leases [3] | % of Annual Full-Service Rent Expiring | Annual Expiring PSF Full-Service Rent [3] | Number of Customers With Expiring Leases |
|---|---|---|---|---|---|---|---|---|
| Q1 2007 | 458,157 | (403,976) | 54,181 | 0.8 | $ 1,265,432 | 0.8 | $ 23.36 | 33 |
| Q2 2007 | 106,697 | (15,259) | 91,438 | 1.4 | 1,743,619 | 1.1 | 19.07 | 16 |
| Q3 2007 | 87,395 | (39,350) | 48,045 | 0.7 | 844,161 | 0.5 | 17.57 | 11 |
| Q4 2007 | 76,704 | 316,377 | 393,081 | 6.0 | 9,398,804 | 6.1 | 23.91 | 9 |
| Total 2007 | 728,953(4) | (142,208) | 586,745(4) | 8.9% | $ 13,252,016 | 8.5 | $ 22.59 | 69 |
| Q1 2008 | 144,242 | 1,388 | 145,630 | 2.2 | $ 3,596,739 | 2.3 | $ 24.70 | 13 |
| Q2 2008 | 90,001 | 1,579 | 91,580 | 1.4 | 2,158,883 | 1.4 | 23.57 | 17 |
| Q3 2008 | 79,743 | (9,650) | 70,093 | 1.1 | 1,493,525 | 1.0 | 21.31 | 20 |
| Q4 2008 | 110,721 | (17,109) | 93,612 | 1.4 | 1,967,611 | 1.3 | 21.02 | 22 |
| Total 2008 | 424,707 | (23,792) | 400,915 | 6.1% | $ 9,216,758 | 6.0 | $ 22.99 | 72 |
| 2009 | 459,179 | (1,411) | 457,768 | 7.0 | $ 11,745,207 | 7.6 | $ 25.66 | 54 |
| 2010 | 640,621 | 12,222 | 652,843 | 10.0 | 16,302,254 | 10.6 | 24.97 | 59 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| 2011 | 469,972 | (65,847) | 404,125 | 6.2 | 10,331,270 | 6.7 | 25.56 | 38 |
| 2012 | 340,047 | 46,526 | 386,573 | 5.9 | 8,461,619 | 5.5 | 21.89 | 32 |
| 2013 | 503,065 | 80,544 | 583,609 | 8.9 | 14,362,393 | 9.3 | 24.61 | 26 |
| 2014 | 630,572 | 7,922 | 638,494 | 9.7 | 14,440,942 | 9.4 | 22.62 | 13 |
| 2015 | 936,483 | 17,599 | 954,082 | 14.6 | 22,054,983 | 14.3 | 23.12 | 22 |
| 2016 | 204,867 | | 204,867 | 3.1 | 5,809,013 | 3.8 | 28.36 | 14 |
| 2017 and thereafter | 1,214,468 | 68,445 | 1,282,913 | 19.6 | 27,753,961 | 18.3 | 21.63 | 13 |
| Total | 6,552,934 | | 6,552,934 | 100.0% | $ 153,730,416 | 100.0 | $ 23.46 | 412 |

(1) Square footage is presented without adjustment to reflect our actual ownership percentage in joint ventured properties.

(2) Signed renewals and relets extend the expiration dates of in-place leases to the end of the renewed or relet term.

(3) Calculated based on base rent payable under the lease for net rentable square feet expiring (after renewals and relets), giving effect to free rent and scheduled rent increases taken into account under GAAP and including adjustments for expenses payable by or reimbursable from customers based on current

expense levels.

(4) As of December 31, 2006 leases totaling 201,481 square feet (including relets and renewals of 142,208 square feet and new leases of 59,273 square feet) have been signed and will commence during 2007. These signed leases represent approximately 28% of gross square footage expiring during 2007. Expiring square footage includes 14,018 square feet of month-to-month leases.

Table of Contents

**Houston Office Properties**

| Year of Lease Expiration | Square Footage of Expiring Leases (Before Renwals and Relets) [(1)] | Signed Renewals and Relets of Expiring Leases [(2)] | Square Footage of Expiring Leases (After Renewals and Relets) [(1)] | % of Square Footage Expiring | Annual Full-Service Rent Under Expiring Leases [(3)] | % of Annual Full-Service Rent Expiring | Annual Expiring PSF Full-Service Rent [(3)] | Number of Customers With Expiring Leases |
|---|---|---|---|---|---|---|---|---|
| Q1 2007 | 789,946 | (502,076) | 287,870 | 3.1 | $ 4,428,987 | 2.4 | $ 15.39 | 95 |
| Q2 2007 | 343,944 | (163,389) | 180,555 | 1.9 | 3,577,680 | 1.9 | 19.81 | 21 |
| Q3 2007 | 176,376 | (65,187) | 111,189 | 1.2 | 2,197,816 | 1.2 | 19.77 | 21 |
| Q4 2007 | 173,733 | (27,070) | 146,663 | 1.6 | 2,969,467 | 1.6 | 20.25 | 24 |
| Total 2007 | 1,483,999 (4) | (757,722) | 726,277 (4) | 7.8% | $ 13,173,950 | 7.1% | $ 18.14 | 161 |
| Q1 2008 | 816,224 | (20,516) | 795,708 | 8.4 | $ 17,387,899 | 9.2 | $ 21.85 | 24 |
| Q2 2008 | 110,715 | 4,779 | 115,494 | 1.2 | 2,270,779 | 1.2 | 19.66 | 20 |
| Q3 2008 | 217,357 | (33,057) | 184,300 | 2.0 | 3,995,546 | 2.1 | 21.68 | 25 |
| Q4 2008 | 180,656 | (7,927) | 172,729 | 1.8 | 3,602,549 | 1.9 | 20.86 | 26 |
| Total 2008 | 1,324,952 | (56,721) | 1,268,231 | 13.4% | $ 27,256,773 | 14.4% | $ 21.49 | 95 |
| 2009 | 965,859 | 103 | 965,962 | 10.3 | $ 18,567,268 | 9.9 | $ 19.22 | 100 |
| 2010 | 548,711 | 107,150 | 655,861 | 7.0 | 12,697,593 | 6.7 | 19.36 | 80 |
| 2011 | 750,787 | 21,350 | 772,137 | 8.2 | 15,434,732 | 8.2 | 19.99 | 78 |
| 2012 | 601,136 | 138,685 | 739,821 | 7.9 | 15,697,606 | 8.3 | 21.22 | 36 |
| 2013 | 449,801 | 24,078 | 473,879 | 5.0 | 9,845,448 | 5.2 | 20.78 | 15 |
| 2014 | 1,829,951 | 102,963 | 1,932,914 | 20.5 | 38,897,610 | 20.6 | 20.12 | 16 |
| 2015 | 372,354 | | 372,354 | 4.0 | 6,963,821 | 3.7 | 18.70 | 14 |
| 2016 | 723,018 | 11,713 | 734,731 | 7.8 | 15,736,199 | 8.4 | 21.42 | 28 |
| 2017 and thereafter | 372,754 | 408,401 | 781,155 | 8.1 | 14,175,940 | 7.5 | 18.15 | 9 |
| Total | 9,423,322 | | 9,423,322 | 100.0% | $ 188,446,940 | 100.0% | $ 20.00 | 632 |

(1) Square footage is presented without adjustment to reflect our actual ownership percentage in joint ventured properties.

(2) Signed renewals and relets extend the expiration dates of in-place leases to the end of the renewed or relet term.

(3) Calculated based on base rent payable under the lease for net rentable square feet expiring (after renewals and relets), giving effect to free rent and scheduled rent increases taken into account under GAAP and including adjustments for expenses payable by or reimbursable from customers based on current expense levels.

(4) As of December 31, 2006 leases totaling 1,202,482 square feet (including relets and renewals of 757,722 square feet and new leases of 444,760 square feet) have been signed and will commence during 2007. These signed leases represent approximately

81% of gross square footage expiring during 2007. Expiring square footage includes 144,374 square feet of month-to-month leases.

**Austin Office Properties**

| Year of Lease Expiration | Square Footage of Expiring Leases (Before Renewals and Relets) (1) | Signed Renewals and Relets of Expiring Leases (2) | Square Footage of Expiring Leases (After Renewals and Relets) (1) | % of Square Footage Expiring | Annual Full-Service Rent Under Expiring Leases (3) | % of Annual Full-Service Rent Expiring | Annual Expiring PSF Full-Service Rent (3) | Number of Customers With Expiring Leases |
|---|---|---|---|---|---|---|---|---|
| Q1 2007 | 72,878 | (17,512) | 55,366 | 4.3 | $ 706,809 | 2.6 | $ 12.77 | 13 |
| Q2 2007 | 9,904 | 1,484 | 11,388 | 0.9 | 204,182 | 0.8 | 17.93 | 3 |
| Q3 2007 | 12,386 | (1,824) | 10,562 | 0.8 | 196,659 | 0.7 | 18.62 | 5 |
| Q4 2007 | 23,405 | | 23,405 | 1.8 | 494,407 | 1.8 | 21.12 | 6 |
| Total 2007 | 118,573 (4) | (17,852) | 100,721 (4) | 7.8% | $ 1,602,057 | 5.9% | $ 15.91 | 27 |
| Q1 2008 | 10,313 | | 10,313 | 0.8 | $ 160,125 | 0.6 | $ 15.53 | 5 |
| Q2 2008 | 4,788 | | 4,788 | 0.4 | 104,876 | 0.4 | 21.90 | 3 |
| Q3 2008 | 20,061 | | 20,061 | 1.6 | 491,386 | 1.8 | 24.49 | 8 |
| Q4 2008 | 32,708 | | 32,708 | 2.5 | 877,009 | 3.2 | 26.81 | 4 |
| Total 2008 | 67,870 | | 67,870 | 5.3% | $ 1,633,396 | 6.0% | $ 24.07 | 20 |
| 2009 | 199,764 | (48,767) | 150,997 | 11.8 | $ 3,371,645 | 12.5 | $ 22.33 | 26 |
| 2010 | 163,394 | 16,028 | 179,422 | 14.0 | 3,422,001 | 12.7 | 19.07 | 26 |
| 2011 | 102,375 | 50,591 | 152,966 | 11.9 | 3,589,116 | 13.3 | 23.46 | 15 |
| 2012 | 67,188 | | 67,188 | 5.2 | 1,501,417 | 5.6 | 22.35 | 8 |
| 2013 | 105,228 | | 105,228 | 8.2 | 2,220,392 | 8.2 | 21.10 | 9 |
| 2014 | 253,980 | | 253,980 | 19.8 | 5,517,181 | 20.4 | 21.72 | 4 |
| 2015 | 129,488 | | 129,488 | 10.1 | 2,610,609 | 9.7 | 20.16 | 10 |
| 2016 | 67,509 | | 67,509 | 5.3 | 1,288,715 | 4.8 | 19.09 | 3 |
| 2017 and thereafter | 9,434 | | 9,434 | 0.6 | 247,413 | 0.9 | 26.23 | 1 |
| Total | 1,284,803 | | 1,284,803 | 100.0% | $ 27,003,942 | 100.0% | $ 21.02 | 149 |

(1) Square footage is presented

without adjustment to reflect our actual ownership percentage in joint ventured properties.

(2) Signed renewals and relets extend the expiration dates of in-place leases to the end of the renewed or relet term.

(3) Calculated based on base rent payable under the lease for net rentable square feet expiring (after renewals and relets), giving effect to free rent and scheduled rent increases taken into account under GAAP and including adjustments for expenses payable by or reimbursable from customers based on current expense levels.

(4) As of December 31, 2006 leases totaling 38,127 square feet (including relets and renewals of 17,852 square feet and new leases of 20,275 square feet) have been signed and

will commence during 2007. These signed leases represent approximately 32% of gross square footage expiring during 2007. Expiring square footage includes 35,417 square feet of month-to-month leases.

**Table of Contents**

**Denver Office Properties**

| Year of Lease Expiration | Square Footage of Expiring Leases (Before Renewals and Relets) (1) | Signed Renewals and Relets of Expiring Leases (2) | Square Footage of Expiring Leases (After Renewals and Relets) (1) | % of Square Footage Expiring | Annual Full-Service Rent Under Expiring Leases (3) | % of Annual Full-Service Rent Expiring | Annual Expiring PSF Full-Service Rent (3) | Number of Customers With Expiring Leases |
|---|---|---|---|---|---|---|---|---|
| Q1 2007 | 64,250 | (34,159) | 30,091 | 1.5 | $ 507,542 | 1.2 | $ 16.87 | 13 |
| Q2 2007 | 18,646 | (5,993) | 12,653 | 0.6 | 300,929 | 0.7 | 23.78 | 4 |
| Q3 2007 | 16,298 | 549 | 16,847 | 0.9 | 328,868 | 0.8 | 19.52 | 3 |
| Q4 2007 | 14,214 | (7,955) | 6,259 | 0.3 | 134,015 | 0.3 | 21.41 | 2 |
| Total 2007 | 113,408 (4) | (47,558) | 65,850 (4) | 3.3% | $ 1,271,354 | 3.0% | $ 19.31 | 22 |
| Q1 2008 | 46,161 | (23,079) | 23,082 | 1.2 | $ 528,713 | 1.3 | $ 22.91 | 6 |
| Q2 2008 | 132,980 | (3,877) | 129,103 | 6.6 | 2,956,407 | 7.2 | 22.90 | 6 |
| Q3 2008 | 18,610 | | 18,610 | 0.9 | 396,545 | 1.0 | 21.31 | 3 |
| Q4 2008 | 12,700 | (2,978) | 9,722 | 0.5 | 220,596 | 0.5 | 22.69 | 4 |
| Total 2008 | 210,451 | (29,934) | 180,517 | 9.2% | $ 4,102,261 | 10.0% | $ 22.73 | 19 |
| 2009 | 234,658 | (52,720) | 181,938 | 9.2 | $ 3,729,509 | 9.1 | $ 20.50 | 26 |
| 2010 | 198,027 | 20,537 | 218,564 | 11.1 | 4,810,970 | 11.8 | 22.01 | 18 |
| 2011 | 200,877 | 7,615 | 208,492 | 10.6 | 4,562,349 | 11.1 | 21.88 | 22 |
| 2012 | 180,482 | 83,980 | 264,462 | 13.4 | 5,995,876 | 14.7 | 22.67 | 12 |
| 2013 | 160,969 | (57,190) | 103,779 | 5.3 | 2,138,630 | 5.2 | 20.61 | 9 |
| 2014 | 444,840 | 73,210 | 518,050 | 26.3 | 10,368,492 | 25.3 | 20.01 | 5 |
| 2015 | 18,637 | | 18,637 | 0.9 | 372,567 | 0.9 | 19.99 | 3 |
| 2016 | 64,075 | | 64,075 | 3.3 | 1,073,124 | 2.6 | 16.75 | 3 |
| 2017 and thereafter | 144,050 | 2,060 | 146,110 | 7.4 | 2,498,672 | 6.3 | 17.10 | 5 |
| Total | 1,970,474 | | 1,970,474 | 100.0% | $ 40,923,804 | 100.0% | $ 20.77 | 144 |

**(1)** Square footage is presented without adjustment to reflect our actual ownership percentage in joint ventured properties.

**(2)** Signed renewals and relets extend the expiration dates of in-place leases to the end of the renewed or relet term.

**(3)** Calculated based on base rent payable under the lease for net rentable square feet expiring (after renewals and relets), giving effect to free rent and scheduled rent increases taken into account under GAAP and including adjustments for expenses payable by or reimbursable from customers based on current expense levels.

**(4)** As of December 31, 2006 new leases totaling 88,007 square feet (including relets and renewals of 47,558 square feet and new leases of 40,449 square feet) have been signed and will commence during 2007. These signed leases represent approximately 78% of gross square footage expiring during 2007. Expiring square footage includes 6,751 square feet of month-to-month leases.

**Miami Office Properties**

| Year of Lease Expiration | Square Footage of Expiring Leases (Before Renewals and Relets) (1) | Signed Renewals and Relets of Expiring Leases (2) | Square Footage of Expiring Leases (After Renewals and Relets) (1) | % of Square Footage Expiring | Annual Full-Service Rent Under Expiring Leases (3) | % of Annual Full-Service Rent Expiring | Annual Expiring PSF Full-Service Rent (3) | Number of Customers With Expiring Leases |
|---|---|---|---|---|---|---|---|---|
| Q1 2007 | 71,586 | (18,295) | 53,291 | 3.2 | $ 1,419,646 | 2.7 | $ 26.64 | 22 |
| Q2 2007 | 86,478 | (9,610) | 76,868 | 4.6 | 2,415,668 | 4.6 | 31.43 | 20 |
| Q3 2007 | 23,791 | | 23,791 | 1.4 | 678,535 | 1.3 | 28.52 | 8 |
| Q4 2007 | 47,727 | (22,905) | 24,822 | 1.5 | 643,332 | 1.2 | 25.92 | 3 |
| Total 2007 | 229,582 (4) | (50,810) | 178,772 (4) | 10.7% | $ 5,157,181 | 9.8% | $ 28.85 | 53 |
| Q1 2008 | 18,764 | (1,249) | 17,515 | 1.1 | $ 555,165 | 1.1 | $ 31.70 | 5 |
| Q2 2008 | 29,853 | 5,995 | 35,848 | 2.2 | 1,120,978 | 2.1 | 31.27 | 9 |
| Q3 2008 | 21,544 | | 21,544 | 1.3 | 664,396 | 1.3 | 30.84 | 6 |
| Q4 2008 | 61,354 | (11,114) | 50,240 | 3.0 | 1,480,178 | 2.8 | 29.46 | 13 |
| Total 2008 | 131,515 | (6,368) | 125,147 | 7.6% | $ 3,820,717 | 7.3% | $ 30.53 | 33 |
| 2009 | 338,219 | (6,043) | 332,176 | 20.0 | $ 9,882,868 | 18.8 | $ 29.75 | 40 |
| 2010 | 279,776 | 2,072 | 281,848 | 17.0 | 9,137,800 | 17.4 | 32.42 | 25 |
| 2011 | 147,857 | 16,049 | 163,906 | 9.9 | 5,298,991 | 10.1 | 32.33 | 23 |
| 2012 | 98,434 | 5,524 | 103,958 | 6.3 | 3,629,533 | 6.9 | 34.91 | 7 |
| 2013 | 85,113 | 2,000 | 87,113 | 5.3 | 2,774,422 | 5.3 | 31.85 | 11 |
| 2014 | 36,952 | | 36,952 | 2.2 | 1,054,130 | 2.0 | 28.53 | 2 |
| 2015 | 110,242 | 11,932 | 122,174 | 7.4 | 3,995,035 | 7.6 | 32.70 | 4 |
| 2016 | 108,226 | | 108,226 | 6.5 | 3,805,138 | 7.3 | 35.16 | 7 |
| 2017 and thereafter | 92,440 | 25,644 | 118,084 | 7.1 | 3,909,838 | 7.5 | 33.11 | 6 |
| Total | 1,658,356 | | 1,658,356 | 100.0% | $ 52,465,653 | 100.0% | $ 31.64 | 211 |

**(1)** Square footage is presented without adjustment to reflect our actual ownership percentage in joint ventured properties.

**(2)** Signed renewals and relets extend the expiration dates of in-place leases to the end of the renewed or relet term.

**(3)** Calculated based on base rent payable under the lease for net rentable square feet expiring (after renewals and relets), giving effect to free rent and scheduled rent increases taken into account under GAAP and including adjustments for expenses payable by or reimbursable from customers based on current expense levels.

**(4)** As of December 31, 2006 leases totaling 99,189 square feet (including relets and renewals of 50,810 square feet and new leases of 48,379 square feet) have been signed and will commence during 2007.

These signed leases represent approximately 43% of gross square footage expiring during 2007. Expiring square footage includes 25,936 square feet of month-to-month leases.

Table of Contents

**Las Vegas Office Properties**

| Year of Lease Expiration | Square Footage of Expiring Leases (Before Renewals and Relets) (1) | Signed Renewals and Relets of Expiring Leases (2) | Square Footage of Expiring Leases (After Renewals and Relets) (1) | % of Square Footage Expiring | Annual Full-Service Rent Under Expiring Leases (3) | % of Annual Full-Service Rent Expiring | Annual Expiring PSF Full-Service Rent (3) | Number of Customers With Expiring Leases |
|---|---|---|---|---|---|---|---|---|
| Q1 2007 | 33,578 | (12,051) | 21,527 | 2.0 | $ 608,101 | 1.7 | $ 28.25 | 4 |
| Q2 2007 | 38,769 | (29,392) | 9,377 | 0.9 | 267,854 | 0.7 | 28.56 | 2 |
| Q3 2007 | 55,483 | | 55,483 | 5.2 | 1,695,604 | 4.7 | 30.56 | 9 |
| Q4 2007 | 58,908 | (10,426) | 48,482 | 4.5 | 1,580,136 | 4.3 | 32.59 | 10 |
| Total 2007 | 186,738 (4) | (51,869) | 134,869 (4) | 12.6% | $ 4,151,695 | 11.4% | $ 30.78 | 25 |
| Q1 2008 | 56,474 | 1,659 | 58,133 | 5.4 | $ 1,821,333 | 5.0 | $ 31.33 | 3 |
| Q2 2008 | 35,795 | | 35,795 | 3.3 | 1,203,659 | 3.3 | 33.63 | 7 |
| Q3 2008 | 15,505 | | 15,505 | 1.4 | 487,676 | 1.3 | 31.45 | 4 |
| Q4 2008 | 56,048 | | 56,048 | 5.2 | 1,756,564 | 4.8 | 31.34 | 6 |
| Total 2008 | 163,822 | 1,659 | 165,481 | 15.3% | $ 5,269,232 | 14.4% | $ 31.84 | 20 |
| 2009 | 165,447 | 977 | 166,424 | 15.5 | $ 5,469,670 | 15.0 | $ 32.87 | 21 |
| 2010 | 107,440 | 2,757 | 110,197 | 10.2 | 3,676,593 | 10.1 | 33.36 | 15 |
| 2011 | 259,486 | | 259,486 | 24.1 | 9,350,976 | 25.7 | 36.04 | 27 |
| 2012 | 35,380 | 21,119 | 56,499 | 5.2 | 2,018,546 | 5.5 | 35.73 | 3 |
| 2013 | 62,581 | | 62,581 | 5.8 | 2,207,007 | 6.1 | 35.27 | 7 |
| 2014 | 19,295 | | 19,295 | 1.8 | 605,642 | 1.7 | 31.39 | 2 |
| 2015 | 43,116 | | 43,116 | 4.0 | 1,373,599 | 3.8 | 31.86 | 1 |
| 2016 | 33,533 | | 33,533 | 3.1 | 1,268,591 | 3.5 | 37.83 | 2 |
| 2017 and thereafter | | 25,357 | 25,357 | 2.4 | 1,029,356 | 2.8 | 40.59 | |
| Total | 1,076,838 | | 1,076,838 | 100.0% | $ 36,420,907 | 100.0% | $ 33.82 | 123 |

**(1)** Square footage is presented without adjustment to reflect our actual ownership percentage in joint ventured properties.

**(2)** Signed renewals and relets extend the expiration dates of in-place leases to the end of the renewed or relet term.

**(3)** Calculated based on base rent payable under the lease for net rentable square feet expiring (after renewals and relets), giving effect to free rent and scheduled rent increases taken into account under GAAP and including adjustments for expenses payable by or reimbursable from customers based on current expense levels.

**(4)** As of December 31, 2006 leases totaling 58,652 square feet (including relets and renewals of 51,869 square feet and new leases of 6,783 square feet) have been signed and will commence during 2007. These signed leases represent approximately 31% of gross square footage expiring during 2007. Expiring square footage includes 8,399 square feet of month-to-month leases.

**Other Office Properties**

| Year of Lease Expiration | Square Footage of Expiring Leases (Before Renewals and Relets) (1) | Signed Renewals and Relets of Expiring Leases (2) | Square Footage of Expiring Leases (After Renewals and Relets) (1) | % of Square Footage Expiring | Annual Full-Service Rent Under Expiring Leases (3) | % of Annual Full-Service Rent Expiring | Annual Expiring PSF Full-Service Rent (3) | Number of Customers With Expiring Leases |
|---|---|---|---|---|---|---|---|---|
| Q1 2007 | 39,106 | (20,616) | 18,490 | 0.9 | $ 334,995 | 0.7 | $ 18.12 | 12 |
| Q2 2007 | 72,263 | (28,800) | 43,463 | 2.0 | 1,134,114 | 2.2 | 26.09 | 10 |
| Q3 2007 | 29,648 | (3,443) | 26,205 | 1.2 | 712,964 | 1.4 | 27.21 | 8 |
| Q4 2007 | 202,462 | (74,975) | 127,487 | 5.9 | 3,134,306 | 6.1 | 24.59 | 9 |
| Total 2007 | 343,479 (4) | (127,834) | 215,645 (4) | 10.0% | $ 5,316,379 | 10.4% | $ 24.65 | 39 |
| Q1 2008 | 31,336 | (1,985) | 29,351 | 1.4 | $ 713,668 | 1.4 | $ 24.31 | 8 |
| Q2 2008 | 54,362 | (24,074) | 30,288 | 1.4 | 794,812 | 1.6 | 26.24 | 11 |
| Q3 2008 | 50,076 | (5,639) | 44,437 | 2.1 | 1,316,739 | 2.6 | 29.63 | 7 |
| Q4 2008 | 25,118 | (16,646) | 8,472 | 0.4 | 216,346 | 0.4 | 25.54 | 5 |
| Total 2008 | 160,892 | (48,344) | 112,548 | 5.3% | $ 3,041,565 | 6.0% | $ 27.02 | 31 |
| 2009 | 218,090 | 33,868 | 251,958 | 11.7 | $ 5,722,665 | 11.2 | $ 22.71 | 34 |
| 2010 | 173,270 | 9,009 | 182,279 | 8.5 | 5,146,094 | 10.0 | 28.23 | 27 |
| 2011 | 300,688 | 14,951 | 315,639 | 14.7 | 7,635,397 | 14.9 | 24.19 | 32 |
| 2012 | 175,640 | 21,950 | 197,590 | 9.2 | 4,667,708 | 9.1 | 23.62 | 13 |
| 2013 | 576,182 | 80,422 | 656,604 | 30.6 | 14,197,742 | 27.7 | 21.62 | 16 |
| 2014 | 57,657 | 3,045 | 60,702 | 2.8 | 1,417,986 | 2.8 | 23.36 | 6 |
| 2015 | 110,250 | | 110,250 | 5.1 | 2,818,610 | 5.5 | 25.57 | 6 |
| 2016 | 12,724 | | 12,724 | 0.6 | 292,033 | 0.6 | 22.95 | 2 |
| 2017 and thereafter | 20,279 | 12,933 | 33,212 | 1.5 | 994,926 | 1.8 | 29.96 | 2 |
| Total | 2,149,151 | | 2,149,151 | 100.0% | $ 51,251,105 | 100.0% | $ 23.85 | 208 |

**(1)** Square footage is presented without adjustment to reflect our actual ownership percentage in joint ventured properties.

**(2)** Signed renewals and relets extend the expiration dates of in-place leases to the end of the renewed or relet term.

**(3)** Calculated based on base rent payable under the lease for net rentable square feet expiring (after renewals and relets), giving effect to free rent and scheduled rent increases taken into account under GAAP and including adjustments for expenses payable by or reimbursable from customers based on current expense levels.

**(4)** As of December 31, 2006 leases totaling 137,753 square feet (including relets and renewals of 127,834 square feet and new leases of 9,919 square feet) have been signed and will commence during 2007.

These signed leases represent approximately 40% of gross square footage expiring during 2007. Expiring square feet includes 12,466 square feet of month-to-month leases.

Table of Contents

**Resort Residential Development Properties**

The following table shows certain information as of December 31, 2006, relating to the Resort Residential Development Properties.

| Corporation / Project | Location | Our Preferred Return/Economic Ownership (1) | Product Type (2) | Planned Sales Lots/Units/ Acres | Closed Lots/Units/ Acres | Remaining Lots/Units/ Acres | Under Development Lots/Units/ Acres | Physical Inventory Lots/Units/ Acres | Average Sales Price on Closed Lots/Units/ Acres (3) | Proposed Average Sales Price on Remaining Lots/Units/ Acres |
|---|---|---|---|---|---|---|---|---|---|---|
| ***Desert Mountain Development Corporation*** | | | | | | | | | | |
| **Desert Mountain** (4) Custom Lots Homes | Scottsdale, AZ | 93% | SF, SH, THB | 2,489 | 2,415 | 74(5) | | 42 | 749 | 2,781 |
| ***Crescent Resort Development Inc.*** | | | | | | | | | | |
| **Tahoe Mountain Resorts** | | | | | | | | | | |
| ***Northstar Village*** | | | | | | | | | | |
| Big Horn and Catamount | Lake Tahoe, CA | 13%/57% | COS | 113 | 21 | 92 | 92 | | 1,862 | 1,331 |
| Identified Future Projects | Lake Tahoe, CA | 13%/23%-57% | THS, TSS | 133 | | 133 | | | | 3,210 |
| ***Northstar Highlands*** | | | | | | | | | | |
| Northstar Trailside Townhomes | Lake Tahoe, CA | 13%/57% | THS | 16 | | 16 | 6 | | | 3,718 |
| Northstar Ritz Condos | Lake Tahoe, CA | 13%/23% | COS | 84 | | 84 | 23 | | | 4,189 |
| Highlands Acreage | Lake Tahoe, CA | 13%/23% | ACR | 4.8 | | 4.8 | | 4.8 | | 4,688 |
| Identified Future Projects | Lake Tahoe, CA | 13%/57% | CO, TH, TS | 1,272 | | 1,272 | | | | 2,680 |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | | S | | | | | | | |
| ***Old Greenwood*** | | | | | | | | | | |
| Units | Lake Tahoe, CA | 13%/71% | TH B | 19 | 15 | 4 | | 4 | 1,428 | 938 |
| Fractional Units[6] | Lake Tahoe, CA | 13%/71% | TS S | 146.00 | 42.12 | 103.88 | 11.00 | 30.00 | 1,922 | 2,185 |
| ***Gray s Crossing*** | | | | | | | | | | |
| Lots | Lake Tahoe, CA | 13%/71% | SF B | 377 | 254 | 123 | 84 | 39 | 314 | 421 |
| Units[8] | Lake Tahoe, CA | 13%/71% | CO B | 170 | | 170 | | | | 412 |
| **Denver Development** | | | | | | | | | | |
| Creekside Townhomes at Riverfront Park | Denver, CO | 12%/64% | TH P | 23 | 21 | 2 | | 2 | 737 | 1,107 |
| Brownstones (Phase I) | Denver, CO | 12%/64% | TH P | 16 | 14 | 2 | | 2 | 1,634 | 1,582 |
| Delgany | Denver, CO | 12%/64% | CO P | 42 | 38 | 4 | | 4 | 673 | 835 |
| One Riverfront | Denver, CO | 12%/56% | CO P | 50 | | 50 | 50 | | | 843 |
| Identified Future Projects | Denver, CO | 12%/56%-64% | TH, CO B | 328 | | 328 | | | | 754 |
| Downtown Acreage | Denver, CO | 12%/64% | ACR | 6.76 | | 6.76 | | 6.76 | | 4,350 |
| **Mountain and Other Development** | | | | | | | | | | |
| Eagle Ranch | Eagle, CO | 12%/76% | SF P | 1,398 | 1,198 | 200 | 65 | 135 | 89 | 168 |
| Main Street Station Vacation Club [7] | Breckenridge, CO | 12%/30% | TS S | 42.00 | 30.93 | 11.07 | | 11.07 | 1,221 | 1,055 |
| Riverbend | Charlotte, NC | 12%/68% | SF P | 659 | 491 | 168 | 144 | 24 | 31 | 39 |
| Three Peaks | Silverthorne, CO | 12%/49% | SF S | 325 | 312 | 13 | | 13 | 193 | 281 |
| Village Walk | Beaver Creek, CO | 12%/58% | TH S | 26 | 5 | 21 | 21 | | 5,907 | 5,205 |
| The Residences at Park Hyatt Beaver Creek [7] | Beaver Creek, CO | N/A/91% | TS S | 15.00 | 3.10 | 11.90 | | 11.90 | 4,554 | 3,573 |
| Beaver Creek Landing | Beaver Creek, CO | 12%/59% | CO B | 52 | | 52 | 52 | | | 1,250 |
| Riverfront Village | | 12%/27% | | 311 | | 311 | 210 | | | 1,112 |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Beaver Creek, CO | | CO, TH[B] | | | | | | | |
| Identified Future Projects | Colorado | 12%/30%-64% | CO[S] | 81 | | 81 | | | | 2,096 |
| ***Houston Area Development Corp.*** | | | | | | | | | | |
| Spring Lakes | Houston, TX | 98% | SF[P] | 497 | 477 | 20 | | 20 | $ 35 | $ 44 |
| ***Crescent Plaza Residential*** | | | | | | | | | | |
| The Residences at the Ritz-Carlton (Phase I) | Dallas, TX | 100% | CO | 70 | | 70 | 70 | | $ | $ 1,902 |
| The Tower Residences and Regency Row (Phase II) | Dallas, TX | 100% | CO, TH[P] | 100 | | 100 | | | | 1,548(8) |

(1) We receive our invested capital plus a preferred return on our invested capital before profits are allocated to the partners based on ownership percentage. Some projects listed assume an equity partner will participate.

(2) SF (Single-Family Lot); CO (Condominium); TH (Townhome); TS (Timeshare Equivalent Unit); ACR (Acreage); and SH (Single-Family Home). Superscript items represent P (Primary residence); S (Secondary

residence); and B (Both Primary and Secondary residence)

(3) Based on lots, units, and acres closed during our ownership period.

(4) Average Sales Price includes golf membership, which as of December 31, 2006 is $0.3 million.

(5) As of December 31, 2006 there were 57 units and 17 lots in inventory or planned for development.

(6) Selling 17 shares per unit.

(7) Selling 20 shares per unit.

(8) Proposed Average Sales Price for The Tower Residences and Regency Row excludes the four Regency Row townhomes, which are expected to have a range in price of $7.0 million to $8.0 million.

32

Table of Contents

**Resort/Hotel Properties**[1]

The following table shows certain information for the years ended December 31, 2006 and 2005, with respect to our Resort/Hotel Properties. The information for the Resort/Hotel Properties is based on available rooms, except for the Canyon Ranch-Tucson and Canyon Ranch-Lenox, which measure their performance based on available guest nights.

| PROPERTY | Location | Year Completed/ Renovated | Rooms | Average Occupancy Rate 2006 | Average Occupancy Rate 2005 | Average Daily Rate 2006 | Average Daily Rate 2005 | Revenue Per Available Room/Guest Night 2006 | Revenue Per Available Room/Guest Night 2005 |
|---|---|---|---|---|---|---|---|---|---|
| ***Canyon Ranch®*** | | | | | | | | | |
| Canyon Ranch Tucson & Lenox[2] | Tuscon, AZ / Lenox, MA | 1980/1989 | 471(3) | 83% | 82% | $ 769 | $ 739 | $ 598 | $ 567 |
| ***Luxury Resorts and Spas:*** | | | | | | | | | |
| Park Hyatt Beaver Creek Resort and Spa | Avon, CO | 1989/2001/2006 | 190(4) | 54% | 57% | $ 365 | $ 303 | $ 197 | $ 172 |
| Fairmont Sonoma Mission Inn & Spa | Sonoma, CA | 1927/1987/1997/2004 | 228 | 77 | 71 | 306 | 292 | 235 | 207 |
| Ventana Inn & Spa | Big Sur, CA | 1975/1982/1988 | 60 | 72 | 73 | 520 | 480 | 375 | 349 |
| **Total/Weighted Average** | | | 478 | 66% | 64% | $ 354 | $ 319 | $ 235 | $ 206 |
| ***Upscale Business Class Hotels:*** | | | | | | | | | |
| Denver Marriott City Center | Denver, CO | 1982/1994 | 613 | 72% | 73% | $ 138 | $ 130 | $ 100 | $ 95 |
| Renaissance Houston Hotel | Houston, TX | 1975/2000 | 388 | 68 | 70 | 128 | 105 | 87 | 74 |
| Omni Austin Hotel [5] | Austin, TX | 1986 | 375 | 79 | 77 | 150 | 128 | 119 | 99 |
| **Total/Weighted Average** | | | 1,376 | 73% | 73% | $ 139 | $ 123 | $ 101 | $ 90 |
| **Total/Weighted Average Luxury Resorts and Spas and Upscale Business Class Hotels** | | | 1,854 | 71% | 71% | $ 192 | $ 175 | $ 137 | $ 124 |

(1) Property Table is presented at

100% without any adjustment to give effect to our actual ownership percentage in the properties.

(2) We own 48% of the Canyon Ranch companies which own or manage: Canyon Ranch Tucson and Canyon Ranch Lenox Destination Resorts, Canyon Ranch SpaClub at the Venetian Resort in Las Vegas, the Canyon Ranch SpaClub on the Queen Mary 2 ocean liner, the Canyon Ranch Living Community in Miami, Fl., the Canyon Ranch SpaClub at The Gaylord Palms Resort in Kissimmee, Fl., Canyon Ranch Living Community in Chicago, IL., and all Canyon Ranch trade names and trademarks.

(3) Represents available guest nights, which is the maximum number of

guests the resort can accommodate per night.

(4) In April 2006, 85 rooms were taken out of service at the Park Hyatt Beaver Creek Resort and Spa. The floor space occupied by 55 of these rooms is to be converted into time-share units for sale by CRDI. The remaining space was used to expand the Allegria Spa within the hotel.

(5) The Omni Austin Hotel is leased pursuant to a lease to HCD Austin Corporation.

**Temperature-Controlled Logistics Properties**

The following table shows the number and aggregate size of Temperature-Controlled Logistic Properties by state as of December 31, 2006:

| State | Number of Properties[1] | Total Cubic Footage (in millions) | Total Square feet (in millions) |
|---|---|---|---|
| Alabama | 5 | 13.8 | 0.5 |
| Arizona | 1 | 2.9 | 0.1 |
| Arkansas | 6 | 33.1 | 1.0 |
| California | 7 | 29.5 | 1.0 |
| Colorado | 1 | 2.8 | 0.1 |
| Florida | 5 | 6.5 | 0.3 |
| Georgia | 9 | 61.8 | 2.1 |
| Idaho | 2 | 18.7 | 0.8 |
| Illinois | 3 | 21.7 | 0.6 |
| Indiana | 1 | 9.1 | 0.3 |
| Iowa | 2 | 12.5 | 0.5 |
| Kansas | 2 | 5.0 | 0.2 |
| Kentucky | 1 | 2.7 | 0.1 |
| Maine | 1 | 1.8 | 0.2 |
| Massachusetts | 4 | 10.2 | 0.5 |
| Minnesota | 1 | 3.0 | 0.1 |
| Mississippi | 1 | 4.7 | 0.2 |
| Missouri | 2 | 46.8 | 2.7 |
| Nebraska | 2 | 4.4 | 0.2 |
| New York | 1 | 11.8 | 0.4 |
| North Carolina | 4 | 15.1 | 0.5 |
| Ohio | 2 | 8.9 | 0.4 |
| Oklahoma | 1 | 1.4 | 0.1 |
| Oregon | 5 | 35.6 | 1.5 |
| Pennsylvania | 3 | 39.0 | 1.1 |
| South Carolina | 1 | 1.6 | 0.1 |
| South Dakota | 1 | 2.9 | 0.1 |
| Tennessee | 3 | 10.6 | 0.4 |
| Texas | 3 | 16.5 | 0.5 |
| Utah | 1 | 8.6 | 0.4 |
| Virginia | 2 | 8.7 | 0.3 |
| Washington | 6 | 28.7 | 1.1 |
| Wisconsin | 3 | 17.4 | 0.6 |
| **TOTAL** | 92 | 497.8 | 19.0 |

(1) As of December 31, 2006 we held a 31.72% interest in AmeriCold

Realty Trust which operates 104 facilities, of which 91 are wholly-owned or leased, one is partially owned and 12 are managed for outside owners.

**Item 3. Legal Proceedings**

We are not currently subject to any material legal proceeding nor, to our knowledge, is any material legal proceeding contemplated against us.

**Item 4. Submission of Matters to a Vote of Security Holders**

No matter was submitted to a vote of security holders during the fourth quarter of our fiscal year ended December 31, 2006.

## PART II

### Item 5. Market for Registrant s Common Equity, Related Shareholder Matters and Issuer Purchases of Equity Securities

### Common Equity

Our common shares have been traded on the New York Stock Exchange under the symbol CEI since the completion of our initial public offering in May 1994. For each calendar quarter indicated, the following table reflects the high and low sales prices during the quarter for the common shares and the distributions declared with respect to each quarter.

| | Price | | |
|---|---|---|---|
| | High | Low | Distributions |
| **2005** | | | |
| First Quarter | $ 18.14 | $ 16.12 | $ 0.375 |
| Second Quarter | 18.99 | 16.02 | 0.375 |
| Third Quarter | 20.65 | 17.95 | 0.375 |
| Fourth Quarter | 21.06 | 19.23 | 0.375 |
| **2006** | | | |
| First Quarter | $ 21.60 | $ 20.14 | $ 0.375 |
| Second Quarter | 20.64 | 17.61 | 0.375 |
| Third Quarter | 22.80 | 18.72 | 0.375 |
| Fourth Quarter | 22.42 | 19.28 | 0.375 |

As of March 5, 2007, there were approximately 652 holders of record of our common shares.

Our actual results of operations and the amounts actually available for distribution will be affected by a number of factors, including:

- the general condition of the United States economy;
- general leasing activity and rental rates in the markets in which the Office Properties are located;
- the ability of tenants to meet their rent obligations;
- our operating and interest expenses;
- consumer preferences relating to the Resort/Hotel Properties and the Resort Residential Development Properties;
- cash flows from unconsolidated and consolidated entities;
- the level of our property acquisitions and dispositions;
- capital expenditure requirements;
- federal, state and local taxes payable by us; and
- the adequacy of cash reserves.

Our future distributions will be at the discretion of our Board of Trust Managers. The Board of Trust Managers has indicated that it will review our distribution rate on a quarterly basis and, as part of the implementation of the Strategic Plan, we intend to align our dividend with industry-accepted pay-out ranges to allow for retention of capital for growth.

35

Table of Contents

**Performance Graph**

The following graph sets forth a comparison of the percentage change in the cumulative total shareholder return on the Common Shares compared to the cumulative total return of the NAREIT All Equity REIT Index and the S&P 500 Index for the period December 31, 2001 through December 31, 2006. The graph depicts the actual increase in the market value of the Common Shares relative to an initial investment of $100 on December 31, 2001, assuming a reinvestment of cash distributions.

**Crescent Real Estate Equities Company**

| | Years Ending | | | | | |
|---|---|---|---|---|---|---|
| **Company / Index** | **12/31/01** | **12/31/02** | **12/31/03** | **12/31/04** | **12/31/05** | **12/31/06** |
| **Crescent Real Estate Equities Company** | 100.00 | 100.25 | 113.72 | 132.81 | 156.49 | 167.61 |
| **S&P 500** | 100.00 | 77.90 | 100.25 | 111.15 | 116.61 | 135.03 |
| **NAREIT All Equity REIT Index** | 100.00 | 103.82 | 142.37 | 187.33 | 210.12 | 283.78 |

We no longer use SNL as a provider of this performance graph, and therefore, the SNL Office REITs Index is excluded because it is not readily available. We believe the S&P 500 and the NAREIT All Equity REIT Index are sufficient indices for comparison of five year total return.

Table of Contents

**Distributions**

Under the Code, REITs are subject to numerous organizational and operational requirements, including the requirement to distribute at least 90% of REIT taxable income each year. Pursuant to this requirement, we were required to distribute $108.3 million and $128.0 million for 2006 and 2005, respectively. Our actual distributions to common and preferred shareholders were $185.1 million and $182.2 million for 2006 and 2005, respectively.

Distributions to the extent of our current and accumulated earnings and profits for federal income tax purposes generally will be taxable to a shareholder as ordinary dividend income. For tax years beginning after December 31, 2002, qualified dividends paid to shareholders are taxed at capital gains rates, as added by the Jobs and Growth Tax Relief Reconciliation Act of 2003. Distributions in excess of current and accumulated earnings and profits will be treated as a nontaxable reduction of the shareholder s basis in such shareholder s shares, to the extent thereof, and thereafter as taxable gain. Distributions that are treated as a reduction of the shareholder s basis in its shares will have the effect of deferring taxation until the sale of the shareholder s shares. No assurances can be given regarding what portion, if any, of distributions in 2007 or subsequent years will constitute a return of capital for federal income tax purposes.

Following is the income tax status of distributions paid during the years ended December 31, 2006 and 2005, to common shareholders:

| | **2006** | **2005** |
|---|---|---|
| Ordinary dividend | 27.1% | 6.3% |
| Qualified dividend eligible for 15% tax rate | 8.0 | 2.7 |
| Capital gain | 15.5 | 47.2 |
| Return of capital | 45.5 | 29.5 |
| Unrecaptured Section 1250 gain | 3.9 | 14.3 |
| | 100.0% | 100.0% |

Distributions on the 14,200,000 Series A Convertible Cumulative Preferred Shares issued by us in February 1998, April 2002 and January 2004 are payable at a rate of $1.6875 per annum per Series A Convertible Cumulative Preferred Share, prior to distributions on the common shares.

Distributions on the 3,400,000 Series B Cumulative Redeemable Preferred Shares issued by us in May and June 2002 are payable at a rate of $2.3750 per annum per Series B Cumulative Redeemable Preferred Share, prior to distributions on the common shares.

Following is the income tax status of distributions paid during the years ended December 31, 2006 and 2005, to preferred shareholders:

| | **Class A Preferred** (1) | | **Class B Preferred** (2) | |
|---|---|---|---|---|
| | **2006** | **2005** | **2006** | **2005** |
| Ordinary dividend | 49.8% | 8.9% | 49.8% | 8.9% |
| Qualified dividend eligible for 15% tax rate | 14.8 | 3.8 | 14.8 | 3.8 |
| Capital gain | 28.3 | 67.1 | 28.3 | 67.1 |
| Unrecaptured Section 1250 Gain | 7.1 | 20.2 | 7.1 | 20.2 |
| | 100.0% | 100.0% | 100.0% | 100.0% |

(1) The Series A Preferred Shares are convertible at any time, in

whole or in part, at the option of the holders into common shares at a conversion price of $40.86 per common share (equivalent to a conversion rate of 0.6119 common shares per Series A Preferred Share). We pay distributions on the Series A Preferred Shares in an amount totaling $1.6875 per share each year (equivalent to 6.75% of the $25.00 liquidation preference per share), payable on a quarterly basis. The Series A Preferred Shares are redeemable, on or after February 28, 2003, in whole or in part, at our option.

(2) The Series B Preferred Shares are redeemable on or after May 17, 2007, in whole or in part, at our option. We pay distributions on the Series B Preferred Shares in an amount totaling $2.375

per share each year (equivalent to 9.50% of the $25.00 liquidation preference per share), payable on a quarterly basis.

Table of Contents

**Item 6. Selected Financial Data**

The following table includes certain of our financial information on a consolidated historical basis. You should read this section in conjunction with Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, and Item 8, Financial Statements and Supplementary Data.

**CRESCENT REAL ESTATE EQUITIES COMPANY**
**CONSOLIDATED HISTORICAL FINANCIAL DATA**
**(Dollars in thousands, except share data)**

| | For Years Ended December 31, | | | | |
|---|---|---|---|---|---|
| | **2006** | **2005 (Restated)** | **2004 (Restated)** | **2003 (Restated)** | **2002 (Restated)** |
| **Operating Data:** | | | | | |
| Total Property revenue | $ 928,696 | $ 1,018,100 | $ 1,000,273 | $ 892,005 | $ 946,311 |
| Income from Property Operations | $ 270,672 | $ 278,839 | $ 314,977 | $ 304,333 | $ 339,319 |
| Income from continuing operations before minority interests and income taxes | $ 18,864 | $ 28,827 | $ 191,216 | $ 58,147 | $ 72,662 |
| Net income (loss) available to common shareholders | $ 1,395 | $ 69,547 | $ 147,061 | $ 4,732 | $ 67,445 |
| Basic (loss) earnings per common share: | | | | | |
| (Loss) income available to common shareholders before discontinued operations and cumulative effect of a change in accounting principle | $ (0.12) | $ (0.23) | $ 1.40 | $ 0.02 | $ 0.12 |
| Net income available to common shareholders-basic | $ 0.01 | $ 0.69 | $ 1.49 | $ 0.05 | $ 0.65 |
| Diluted earnings (loss) per common share: | | | | | |
| (Loss) income available to common shareholders before discontinued operations and cumulative effect of a change in accounting principle | $ (0.12) | $ (0.23) | $ 1.40 | $ 0.02 | $ 0.12 |
| Net income available to common shareholders diluted | $ 0.01 | $ 0.69 | $ 1.48 | $ 0.05 | $ 0.65 |

| | | | | | |
|---|---|---|---|---|---|
| **Balance Sheet Data (at period end):** | | | | | |
| Total assets | $ 4,046,971 | $ 4,163,256 | $ 4,060,325 | $ 4,335,875 | $ 4,309,325 |
| Total debt | $ 2,296,358 | $ 2,259,473 | $ 2,152,255 | $ 2,558,699 | $ 2,382,910 |
| Total shareholders equity | $ 1,122,286 | $ 1,251,626 | $ 1,303,603 | $ 1,223,889 | $ 1,347,232 |
| **Other Data:** | | | | | |
| Cash distribution declared per common share | $ 1.50 | $ 1.50 | $ 1.50 | $ 1.50 | $ 1.50 |
| Weighted average Common shares and units outstanding basic | 121,515,791 | 118,012,402 | 116,747,408 | 116,634,546 | 117,523,248 |
| Weighted average Common shares and units outstanding diluted | 122,979,783 | 118,836,421 | 116,965,897 | 116,676,242 | 117,725,984 |
| Funds from operations available to common shareholders diluted[(1)] | $ 99,448 | $ 118,987 | $ 97,001 | $ 175,901 | $ 212,572 |

(1) Funds from operations, or FFO, is a supplemental non-GAAP financial measurement used in the real estate industry to measure and compare the operating performance of real estate companies, although those companies may calculate funds from operations in different ways. The National Association of Real Estate Investment Trusts (NAREIT) defines funds from operations as Net

Income (Loss) determined in accordance with generally accepted accounting principles (GAAP), excluding gains (or losses) from sales of depreciable operating property, excluding extraordinary items (determined by GAAP), plus depreciation and amortization of real estate assets, and after adjustments for unconsolidated partnerships and joint ventures. We calculate FFO available to common shareholders diluted in the same manner, except that Net Income (Loss) is replaced by Net Income (Loss) Available to Common Shareholders and we include the effect of Operating Partnership unitholder minority interests. For a more detailed definition and description of FFO and a reconciliation to net income determined in accordance with GAAP, see Funds from Operations included in Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations.

**Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations**

**Index to Management s Discussion and Analysis of Financial Condition and Results of Operations**

Table of Contents

## Overview

We are a REIT with assets and operations divided into four investment segments: Office, Resort Residential Development, Resort/Hotel and Temperature-Controlled Logistics. Our strategy, prior to full implementation of the Strategic Plan discussed below, had two key elements as outlined below.

First, we selectively invest in premier office properties in markets that offer attractive returns on invested capital. We may align ourselves with institutional partners to enhance our return on equity when compared to the returns we receive as a 100% owner. Where possible, we negotiate performance-based incentives on our joint ventures that allow for additional equity to be earned if return targets are exceeded. For example, we earned promoted interests on the sales of the Three Westlake and Four Westlake Office Properties in 2006. We also evaluate our existing portfolio for joint-venture opportunities that enable us to increase our return on equity and provide access to equity for reinvestment. We currently hold 43% of our office portfolio in joint ventures.

We selectively develop new office properties where the opportunity exists for attractive returns. In August 2006, we completed, with JMI Realty, a 232,330 square-foot, three-building complex in San Diego, California and sold our interest in the property in December 2006 for a $10.4 million gain. We are also developing a 239,000 square-foot office building as an addition to the Hughes Center complex in Las Vegas, Nevada. We are co-developing with Hines a 267,000 square-foot office building in Irvine, California, and with Champion Partners, a 144,380 square-foot, two-building office complex in Austin, Texas.

Second, we invest in real estate businesses that offer returns equal to or superior to what we are able to achieve in our office investments. We develop and sell residential properties in resort locations primarily through Harry Frampton and his East West Partners development team with the most significant project in terms of future cash flow being our investment in Tahoe Mountain Resorts in California. This development encompasses more than 2,500 total lots and units, of which 532 have been sold, 73 are currently in inventory and over 1,950 are scheduled for development over the next 14 years, and is expected to generate in excess of $5.0 billion in sales. We expect our investment in Tahoe to be a long-term source of earnings and cash flow growth as new projects are designed and developed. We view our resort residential developments as a business and believe that, beyond the net present value of existing projects, there is value in our strategic relationships with the development teams and our collective ability to identify and develop new projects. In addition, we sometimes serve as the primary developer, such as The Ritz-Carlton Phases I and II. Also, we provide mezzanine financing to other office, hotel and residential investors where we see attractive returns relative to owning the equity. We currently have approximately $124.3 million of mezzanine notes.

In 2005, we also completed the recapitalization of our Canyon Ranch investment. In addition to its wellness facilities in Tucson, Arizona and Lenox, Massachusetts and its Spa Club operation at the Venetian Resort in Las Vegas, Nevada, Canyon Ranch partners with developers to establish Canyon Ranch Living communities at which the focal point is a large, comprehensive wellness facility and earns fees for the licensing of the brand name to these communities, providing design and technical services, and the ongoing management of the facilities. One such development is under construction in Miami Beach and an agreement that will pave the way for the development of a Canyon Ranch Living community in Chicago, Illinois, and others, are under consideration or in negotiation.

During 2006, we conducted an extensive review of our strategic alternatives, and in late August received an offer to purchase certain assets. Our Board of Trust Managers established a special committee of independent trust managers to assist in its consideration of the strategic alternatives and to respond to the offer that was received. The Special Committee hired an independent investment banker and counsel to assist with its review. The Special Committee rejected the offer received, and on November 1, 2006, instituted a formal review of our strategic alternatives.

On March 1, 2007, we announced that we had concluded the review of strategic alternatives first announced on November 1, 2006. Based on that review, we adopted a plan, which we refer to as the Strategic Plan, designed to simplify our business model by concentrating on our core office properties business.

Key elements of the Strategic Plan include:

- *Sale of all resort and hotel assets.* Properties to be sold include the Fairmont Sonoma Mission Inn & Spa®, Ventana Inn & Spa in Big Sur, California, the Park Hyatt Beaver Creek Resort & Spa, and three business-class hotels.

*Sale of resort residential developments.* Properties and assets to be sold include Crescent Resort Development and Desert Mountain Development Corporation.

*Opportunistic sale of office properties.* Properties to be sold include virtually all suburban Dallas properties and all Austin properties, as well as our single assets in Phoenix, Arizona, and in Seattle, Washington.

*Reduction of general and administrative expenses by more than $17.0 million, or $0.14 per share.* Implementation of savings began immediately on March 1, 2007 and is expected to be fully phased in by the end of 2007. We expect to take a charge of approximately $5.0 million for severance costs.

*Use of sales proceeds to retire debt.* We plan to first use the proceeds from asset sales to retire debt. We expect that our balance sheet will be significantly strengthened and our cost of capital lowered, giving us capacity for growth.

*Alignment of dividend.* We intend to align our dividend with industry-accepted pay-out ranges to allow for retention of capital for growth.

In addition to the above elements, we are considering alternatives for our interest in Canyon Ranch® in conjunction with the founders of Canyon Ranch®. We will communicate our dividend plans as we execute asset sales. After completing these dispositions, our remaining office portfolio is expected to consist of 22.6 million square feet, of which 11.7 million square feet, or 52%, will be owned in joint venture. Our effective ownership will be 14.0 million square feet.

Table of Contents

## Recent Developments

### Office Segment

### Joint Ventures

*Paseo Del Mar*

On September 21, 2005, we entered into a joint venture arrangement, Crescent-JMIR Paseo Del Mar LLC, with JMI Realty. The joint venture committed to co-develop a 232,330 square-foot, three-building office complex in the Del Mar Heights submarket of San Diego, California. The development was completed in August 2006. The joint venture was structured such that we owned an 80% interest and JMI Realty owned the remaining 20% interest. On December 14, 2006, we completed the sale of our 80% interest in Crescent JMIR Paseo Del Mar LLC. The sale generated proceeds, net of selling costs, of approximately $42.1 million and a gain of approximately $10.4 million, net of promoted interest due JMI Realty and income taxes. Proceeds from the sale were used to pay down our credit facility.

*Bank One Center*

On December 14, 2006, we completed the sale of Bank One Center on behalf of Main Street Partners, L.P., the joint venture which was owned 50% by an affiliate of The Blackstone Group and 50% by us. The sale generated proceeds to the joint venture, net of selling costs and after a $104.7 million loan repayment, of approximately $110.0 million and a net gain of approximately $4.4 million. Our share of the net gain was approximately $1.6 million inclusive of the write-off of unamortized deal costs from the original joint venture of the property. Our share of the proceeds was approximately $55.0 million, which was used to pay down our credit facility.

*Three Westlake Park*

On December 11, 2006, we completed the sale of Three Westlake Park on behalf of Houston PT Three Westlake Office Limited Partnership, the joint venture which was owned 80% by an affiliate of GE Asset Management, or GE and 20% by us. The sale generated proceeds to the joint venture, net of selling costs and after a $33.0 million loan repayment, of approximately $46.7 million and a net gain of approximately $33.4 million. Our share of the net gain, including a promoted interest of approximately $7.7 million, recognition of the unamortized deferred gain, and write-off of unamortized deal costs from the original joint venture of the property, was approximately $17.3 million. Our share of the proceeds was approximately $15.8 million, which was used to pay down our credit facility.

*Four Westlake Park*

On September 26, 2006, we completed the sale of Four Westlake Park on behalf of Houston PT Four Westlake Office Limited Partnership, the joint venture which was owned 80% by an affiliate of GE and 20% by us. The sale generated proceeds to the joint venture, net of selling costs and after a $46.1 million loan repayment, of approximately $73.0 million and a net gain of approximately $55.0 million. Our share of the net gain, including a promoted interest of approximately $14.7 million, was approximately $24.2 million. Our share of the proceeds was approximately $28.7 million, which was used to pay down our credit facility.

*Chase Tower*

On June 20, 2006, we completed the sale of Chase Tower on behalf of Austin PT BK One Tower Office Limited Partnership, the joint venture which was owned 80% by an affiliate of GE and 20% by us. The sale generated proceeds to the joint venture, net of selling costs and after a $36.0 million loan repayment, of approximately $28.0 million and a net gain of approximately $10.1 million. Our share of the net gain, including recognition of the unamortized deferred gain was approximately $4.3 million. Our share of the proceeds was approximately $5.6 million, which was used to pay down the credit facility.

*Parkway at Oakhill*

On March 31, 2006, we entered into a joint venture arrangement, C-C Parkway Austin, L.P., or Parkway, with Champion Partners. The joint venture has committed to co-develop a 144,380 square-foot, two-building office complex in Austin, Texas. The venture is structured such that we own a 90% interest and Champion Partners owns the remaining 10% interest. In connection with the joint venture, Parkway entered into a maximum $18.3 million construction loan. Our equity commitment to the joint venture was $8.2 million, of which $7.0 million has been funded as of December 31, 2006. The development, which is currently

Table of Contents

underway, is scheduled for delivery in the third quarter of 2007.

**Asset Purchase**

| (in millions) Date | Property | | Location | Purchase Price |
|---|---|---|---|---|
| January 23, 2006 | Financial Plaza | Class A Office Property | Phoenix, Arizona | $55.0[(1)] |

(1) The acquisition was funded by the assumption of a $23.6 million loan from Allstate, a new $15.9 million loan from Allstate and a draw on our credit facility. This property is wholly-owned.

**Asset Sale**

| (in millions) Date | Property | | Location | Proceeds |
|---|---|---|---|---|
| February 17, 2006 | Waterside Commons | Class A Office Property | Dallas, Texas | $24.8[(2)] |

(2) We previously recorded an impairment charge of approximately $1.0 million during the year ended December 31, 2005. The proceeds from the sale were used primarily to pay down the credit facility.

**Significant Tenant Lease Termination**

In June 2005, we entered into an agreement with our largest office tenant, El Paso Energy Services Company and certain of its subsidiaries, which terminated El Paso s leases totaling 888,000 square feet at Greenway Plaza in Houston, Texas, effective December 31, 2007. Under the agreement, El Paso is required to pay us $65.0 million in termination fees in periodic installments through December 31, 2007, and $62.0 million in rent according to the original lease terms from July 1, 2005 through December 31, 2007. As of December 31, 2006, we have collected $35.0 million of the lease termination fee. For the years ended December 31, 2006 and 2005, we recognized $38.8 million and $8.5 million, respectively, in net termination fees, which includes accelerated termination fees and contractual full-service rents resulting from the re-lease of approximately 463,000 square feet. As of December 31, 2006, El Paso was current on all rent obligations.

**Resort Residential Development Segment**

**Joint Venture**

*Riverfront Village*

On March 21, 2006, CRDI entered into a joint venture arrangement, East West Resort Development XIV, L.P., L.L.L.P. (Riverfront Village), with affiliates of Crow Holdings and our development partner. The joint venture was formed to co-develop a hotel and condominiums in Avon, Colorado. The development, which is currently underway, is scheduled for delivery in 2008. We provided 41.9% of the initial capitalization and the venture is structured such that we own a 26.8% interest after we receive a preferred return on our invested capital and return of our capital. Our initial equity commitment to the joint venture is $22.6 million, of which $17.2 million was funded as of December 31, 2006. In connection with construction financing obtained in November 2006 for the Riverfront Village project, the partners committed to contribute up to an additional $17.1 million in capital should certain financial covenants not be maintained. Our share of this capital commitment is $7.2 million, of which none was funded as of December 31, 2006.

**Asset Sale**

*Jefferson Station Apartments*

On October 21, 2004, we entered into a partnership agreement with affiliates of JPI Multi-Family Investments, L.P. to develop a multi-family luxury apartment project in Dedham, Massachusetts. The development was completed in November 2006. On December 8, 2006, the partnership, Jefferson Station, L.P., completed the sale of the apartment project. We consolidated the partnership which was owned 50% by JPI Multi-Family Investments, L.P. and 50% by us. The sale generated proceeds, net of selling costs and after the repayment of the $38.8 million loan with Bank of America, of approximately $35.9 million and a gain of approximately $20.3 million. Our share of the gain, net of minority interests and taxes, was approximately $5.4 million. Our share of the proceeds was approximately $24.1 million, which was used to pay down our credit facility.

Table of Contents

## Resort/Hotel Segment

*Park Hyatt Beaver Creek*

In the second quarter of 2006, 85 rooms were taken out of service at the Park Hyatt Beaver Creek in Avon, Colorado. The area occupied by 55 of these rooms is being converted into 15 fractional units for sale in our Resort Residential Development Segment. Sales of fractional units commenced in 2006. The remaining space was used to expand the Allegria Spa within the hotel. In addition, the Resort is adding air conditioning and upgrading the common areas. The spa expansion and common area upgrade were completed in December 2006.

## Temperature-Controlled Logistics Segment

In August 2006, AmeriCold entered into a definitive agreement to acquire from ConAgra Foods, Inc. or ConAgra, four refrigerated warehouse facilities and the lease on a fifth facility, with an option to purchase. These five warehouses contain a total of 1.7 million square feet and 48.9 million cubic feet. The aggregate purchase price is approximately $190.0 million, consisting of $152.0 million in cash to ConAgra and $38.0 million representing the recording of a capital lease obligation for the fifth facility. During the fourth quarter of 2006, AmeriCold completed the acquisition of two of these facilities and assumed the leasehold on the fifth facility and the related capital lease obligation. In January 2007, AmeriCold completed the acquisition of the third facility. The acquisition of the remaining facility is expected to be completed during the first half of 2007.

In December 2006, AmeriCold completed a 5.45% fixed-rate, interest-only financing in an aggregate principal amount of $1.05 billion which matures in approximately equal tranches in seven, nine and ten years. The proceeds were used to repay $449.0 million of fixed-rate mortgages with a rate of 6.89% and a $430.0 million variable rate mortgage. The mortgages that were repaid were collateralized by 84 temperature-controlled warehouses which were released upon repayment. Fifty of the warehouses are used to collateralize the new loan. A portion of the remaining proceeds were distributed to the owners, of which our portion was approximately $58.7 million.

## Other Segment

### Mezzanine Notes

We offer mezzanine financing in the form of limited recourse loans that are made to a special purpose entity which is the direct or indirect parent of another special purpose entity owning a commercial real estate property. These mezzanine loans are secured by a pledge of the ownership interest in the property owner (or in an entity that directly or indirectly owns the property owner) and are thus structurally subordinate to a conventional first mortgage loan made to the property owner. We also offer mezzanine financing by taking a junior participating interest in a first mortgage loan.

The underlying real estate assets may be a single office, hotel or residential property, or a portfolio of cross-collateralized real estate assets. We typically require recourse guaranties from the ultimate owners of the property for such matters as voluntary bankruptcy filings, failure to contest involuntary bankruptcy filings, violation of special purpose entity covenants, environmental liability and other events such as misappropriation of rents or insurance. Although these types of loans generally have greater repayment risks than first mortgages due to the subordinated nature of the loans and the higher loan-to-value ratio, we have a disciplined approach in underwriting the value of the asset. The yield on these investments may be enhanced by front-end fees, prepayment fees, yield look-backs, participating interests and additional fees to allow prepayment during a prepayment black-out period.

| (in millions) Note | | Date of Transaction | Maturity Date | Balance at December 31, 2006 | Interest Rate at December 31, 2006 |
|---|---|---|---|---|---|
| *Fixed Rate:* | | | | | |
| Three Dallas Office Properties | (1) | 8/31/05 | 2010 | $ 7.6 | 11.04% |
| 21 California Condominiums | (2) | 12/28/06 | 2008 | 9.8(3) | 17.00% |
| *Variable Rate:* | | | | | |
| Dallas Office Property | (4) | 6/9/05 | 2007 | 12.0 | 13.85% |
| Two Luxury Hotel Properties in California | (5) | 11/16/05 | 2007 | 15.0 | 16.35% |
| Office Portfolio in Southeastern U.S. | (6) | 12/30/05 | 2007 | 20.7 | 12.23% |
| Florida Hotel Portfolio Investment | (7) | 1/20/06 | 2009 | 15.0 | 13.35% |
| California Ski Resort | (8) | 4/12/06 | 2009 | 20.0 | 9.85% |
| New York City Residential | (9) | 5/8/06 | 2007 | 24.2 | 18.18% |
| **Total Mezzanine Notes** | | | | $ 124.3 | |
| **Total Weighted Average Interest Rate** | | | | | 14.09% |

(1) The loan has an interest-only term through September 2007. Beginning October 2007, the borrower must make principal payments based on a 30-year amortization schedule until maturity. We determined that the entity to which the loan

was funded is a VIE under FIN 46R of which we are not the primary beneficiary; therefore, we do not consolidate the entity. Our maximum exposure to loss is limited to the amount of the loan.

(2) The loan has an interest-only term until maturity, subject to the right of the borrower to extend the loan pursuant to one six-month extension.

(3) The condominiums securing this note were sold by CRDI to a third party. Due to restrictions under SFAS No. 66, *Accounting for Sales of Real Estate* regarding seller financed transactions, the profit from the sale of $4.7 million was deferred and recorded under the cost recovery method and reflected as a reduction of the note such that the face value of the note is included

in the table above.

(4) The loan bears interest at LIBOR plus 850 basis points with an interest-only term until maturity, subject to the right of the borrower to extend the loan pursuant to three one-year extension options.

(5) The loan bears interest at LIBOR plus 1,100 basis points with an interest-only term until maturity, subject to the right of the borrower to extend the loan pursuant to five one-year extension options.

(6) The loan bears interest at LIBOR plus 685 basis points with an interest-only term until maturity, subject to the right of the borrower to extend the loan pursuant to three one-year extension options.

(7) The loan bears interest at

LIBOR plus 800 basis points with an interest-only term until maturity, subject to the right of the borrower to extend the loan pursuant to two one-year extension options.

(8) The loan bears interest at LIBOR plus 450 basis points with an interest-only term until maturity, subject to the right of the borrower to extend the loan pursuant to two one-year extension options.

(9) The loan bears interest at LIBOR plus 1,283 basis points with an interest-only term until maturity, subject to the right of the borrower to extend the loan pursuant to two one-year extension options. We determined that the entity to which the loan was funded is a VIE under FIN 46R of which we are not the primary

beneficiary; therefore, we do not consolidate the entity. Our maximum exposure to loss is limited to the amount of the loan.

In 2006, we received approximately $110.2 million of net proceeds, after the repayment of debt, for the repayment of five of our mezzanine notes, which included $6.2 million of prepayment fees.

Table of Contents

## 2006 Operating Performance

### Office Segment

The following table shows the performance factors on stabilized properties, excluding properties held for sale, used by management to assess the operating performance of the Office Segment:

| | 2006 | 2005 |
|---|---|---|
| Economic Occupancy [(1)] | 89.8% | 88.5% |
| Leased Occupancy [(2)] | 92.6% | 90.8% |
| In-Place Weighted Average Full-Service Rental Rate [(3)] | $22.78 | $22.48 |
| Tenant Improvement and Leasing Costs per Sq. Ft. per year | $ 3.56 | $ 3.55 |
| Average Lease Term [(4)] | 5.7 yrs | 6.2 yrs |
| Same-Store NOI [(5)] Decline | (1.0)% | (1.5)% |
| Same-Store Average Occupancy | 89.3% | 87.3% |

(1) Economic occupancy reflects the occupancy of all tenants paying rent.

(2) Leased occupancy reflects the amount of contractually obligated space, whether or not commencement has occurred.

(3) Calculated based on base rent payable at December 31 giving effect to free rent and scheduled rent increases and including adjustments for expenses payable by or reimbursable from tenants. The weighted average full-service rental rate for

the El Paso lease reflects weighted average full-service rental rate over the shortened term and excludes the impact of the net lease termination fee being recognized ratably to income through December 31, 2007.

(4) Reflects leases executed during the period.

(5) Same-store NOI (net operating income) represents office property net income excluding depreciation, amortization, interest expense and non-recurring items such as lease termination fees for Office Properties owned for the entirety of the comparable periods.

**Resort Residential Development Segment**

The following tables show the performance factors used by management to assess the operating performance of the Resort Residential Development Segment. Information is provided for the CRDI Resort Residential Development Properties and the Desert Mountain Resort Residential Development Properties, which represent our significant investments in this segment as of December 31, 2006.

*CRDI*

| (dollars in thousands) | For the years ended December 31, 2006 | 2005 |
|---|---|---|
| Resort Residential Lot Sales | 212 | 545 |
| Resort Residential Unit Sales: | | |
| Townhome Sales | 30 | 25 |
| Condominium Sales | 59 | 187 |
| Equivalent Timeshare Sales | 19.3 | 15.7 |
| Average Sales Price per Resort Residential Lot | $ 125 | $ 164 |
| Average Sales Price per Resort Residential Unit | $ 2,003 | $ 1,265 |

CRDI, which invests primarily in mountain residential real estate in Colorado and California and residential real estate in downtown Denver, Colorado, is highly dependent upon the national economy and customer demand.

*Desert Mountain*

| | For the years ended December 31, | |
|---|---|---|
| (dollars in thousands) | **2006** | **2005** |
| Resort Residential Lot Sales | 5 | 40 |
| Average Sales Price per Lot [1] | $ 1,837 | $ 1,082 |
| Resort Residential Unit Sales | 12 | |
| Average Sales Price per Unit [1] | $ 1,485 | $ |

(1) Includes equity golf membership

Desert Mountain is in the latter stages of development and management anticipates minor additions to its decreasing available inventory.

**Resort/Hotel Segment**

The following table shows the performance factors used by management to assess the operating performance of our Resort/Hotel Properties.

| | For the years ended December 31, | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Same-Store NOI[1] % Change | | Average Occupancy Rate | | Average Daily Rate | | Revenue Per Available Room/Guest Night | |
| | **2006** | **2005** | **2006** | **2005** | **2006** | **2005** | **2006** | **2005** |
| Luxury Resorts and Spas [2] | 15% | 127%[3] | 76% | 72% | $349 | $332 | $264 | $237 |
| Upscale Business Class Hotels | 23% | 26% | 73% | 73% | $139 | $123 | $101 | $ 90 |

(1) Same-Store NOI (net operating income) represents net income excluding depreciation and amortization, interest expense and rent expense for Resort/Hotel Properties owned for the entirety of the comparable periods.

(2) Excludes the Park Hyatt

Beaver Creek Resort and Spa which had 85 rooms taken out of service in April 2006. The onsite construction and closure of the spa has impacted performance at the property. The floor space occupied by 55 of these rooms was converted into 15 fractional units for sale in our Resort Residential Development Segment. The remaining space was used to expand the Allegria Spa within the hotel.

(3) In November 2003, the Fairmont Sonoma Mission Inn placed 97 historic inn rooms out of service for renovation. The renovation was completed in July 2004, resulting in an increase in 2005 Same-Store NOI as compared to 2004.

Our luxury and destination fitness resorts and spas are unique properties due to location, concept and high replacement cost, but do compete against business-class hotels or middle-market resorts in their geographic areas, as well as against luxury resorts nationwide and around the world. Our upscale Resort/Hotel Properties in Denver, Austin and Houston are business and convention center hotels that compete against other business and convention hotels.

46

**Results of Operations**

The following table shows the variance in dollars for certain of our operating data between the years ended December 31, 2006 and 2005 and the years ended December 31, 2005 and 2004.

| (in millions) | Total variance in dollars between the years ended December 31, 2006 and 2005 (Restated) | Total variance in dollars between the years ended December 31, 2005 and 2004 (Restated) |
|---|---|---|
| **REVENUE:** | | |
| Office Property | $ 41.5 | $ (103.0) |
| Resort Residential Development Property | (130.6) | 192.8 |
| Resort/Hotel Property | (0.4) | (71.9) |
| **Total Property Revenue** | $ (89.5) | $ 17.9 |
| **EXPENSE:** | | |
| Office Property real estate taxes | $ 3.6 | $ (19.3) |
| Office Property operating expenses | 7.3 | (19.1) |
| Resort Residential Development Property expense | (89.2) | 160.9 |
| Resort/Hotel Property expense | (2.9) | (68.5) |
| **Total Property Expense** | $ (81.2) | $ 54.0 |
| **Income from Property Operations** | $ (8.3) | $ (36.1) |
| **OTHER INCOME (EXPENSE):** | | |
| Income from sale of investment unconsolidated company | $ 17.8 | $ 29.9 |
| Income from investment land sales | (8.6) | (10.3) |
| (Loss) gain on joint venture of properties | 2.7 | (268.5) |
| Interest and other income | 18.2 | 11.3 |
| Corporate general and administrative | 5.4 | (11.3) |
| Interest expense | 2.4 | 40.1 |
| Amortization of deferred financing costs | 0.5 | 5.0 |
| Extinguishment of debt | 2.2 | 40.4 |
| Depreciation and amortization | (6.0) | 18.5 |
| Impairment charges related to real estate assets | | 4.1 |
| Other expenses | (9.0) | (3.3) |
| Equity in net income (loss) of unconsolidated companies: | | |
| Office Properties | (2.3) | 5.2 |
| Resort Residential Development Properties | 0.1 | 1.8 |
| Resort/Hotel Properties | (3.6) | (1.3) |

| | | | | |
|---|---|---|---|---|
| Temperature-Controlled Logistics Properties | | (15.9) | | (6.0) |
| Other | | (5.7) | | 18.2 |
| **Total other income (expense)** | $ | (1.8) | $ | (126.2) |
| **INCOME FROM CONTINUING OPERATIONS BEFORE MINORITY INTERESTS AND INCOME TAXES** | $ | (10.1) | $ | (162.3) |
| Minority interests | | 8.4 | | 21.6 |
| Income tax benefit (expense) | | 12.0 | | (20.7) |
| **INCOME BEFORE DISCONTINUED OPERATIONS AND CUMULATIVE EFFECT OF A CHANGE IN ACCOUNTING PRINCIPLE** | $ | 10.3 | $ | (161.4) |
| (Loss) income from discontinued operations, net of minority interests and taxes | | (4.5) | | (6.4) |
| Impairment charges related to real estate assets from discontinued operations, net of minority interests | | 0.9 | | 2.0 |
| Gain on sale of real estate from discontinued operations, net of minority interests and taxes | | (74.8) | | 88.1 |
| Cumulative effect of a change in accounting principle, net of minority interests | | | | 0.4 |
| **NET INCOME** | $ | (68.1) | $ | (77.3) |
| Series A Preferred Share distributions | | | | (0.3) |
| Series B Preferred Share distributions | | | | |
| **NET (LOSS) INCOME AVAILABLE TO COMMON SHAREHOLDERS** | $ | (68.1) | $ | (77.6) |

Table of Contents

**Comparison of the year ended December 31, 2006, to the year ended December 31, 2005 (Restated)**

**Property Revenues**

Total property revenues decreased $89.5 million, or 8.8%, to $928.7 million for the year ended December 31, 2006, as compared to $1,018.2 million for the year ended December 31, 2005. The primary components of the decrease in total property revenues are discussed below.

Office Property revenues increased $41.5 million, or 11.1%, to $414.3 million, primarily due to:

- an increase of $28.1 million in net lease termination fees (from $11.2 million to $39.3 million) primarily due to the El Paso lease termination and related re-leasing;
- an increase of $9.4 million from the 51 consolidated Office Properties (excluding properties acquired, disposed or stabilized during 2005 and 2006) that we owned or had an interest in, primarily due to a 1.6 percentage point increase in average occupancy (from 86.6% to 88.2%), increased expense recovery revenue related to the increase in occupancy and increased recoverable expenses, and increased parking revenue; partially offset by a decline in full service weighted average rental rates;
- an increase of $8.8 million due to the acquisition of Financial Plaza in January 2006 and increased occupancy at One Live Oak, the Exchange Building and Peakview Tower; and
- an increase of $1.0 million related to third party management and leasing services primarily due to increased reimbursement revenue as a result of increased reimbursable expenses; partially offset by
- a decrease of $5.8 million due to the joint ventures of Fulbright Tower in February 2005 and One Buckhead Plaza in June 2005.

Resort Residential Development Property revenues decreased $130.6 million, or 26.0%, to $372.1 million, primarily due to:

- a decrease of $121.6 million in CRDI revenues primarily related to:
  - o a net decrease of $195.7 million primarily related to product mix in lots and units available for sale in 2005 versus 2006 at Hummingbird Lodge in Bachelor Gulch, Colorado, Northstar Ironhorse and Gray s Crossing in Lake Tahoe, California, Creekside Townhomes, Brownstones Phase I, and Delgany, all in Denver, Colorado, and Eagle Ranch in Eagle, Colorado, which had sales in the twelve months ended December 31, 2005, but reduced sales in the same period 2006, partially offset by Old Greenwood Timeshares in Lake Tahoe, California, and Main Street Station in Breckenridge, Colorado, which had sales in the twelve months ended December 31, 2005, but increased sales in the same period 2006; and
  - o a decrease of $38.5 million primarily related to product mix in lots and units available for sale in 2005 versus 2006 at Horizon Pass Lodge in Bachelor Gulch, Colorado, Creekside Phase II in Denver, Colorado, and Old Greenwood Lots in Lake Tahoe, California, which had sales in the twelve months ended December 31, 2005, but no sales in the same period 2006; partially offset by
  - o an increase of $112.0 million primarily related to product mix in lots and units available for sale in 2006 versus 2005 at Village Walk and EW Hotel Residences in Beaver Creek, Colorado, Northstar Big Horn, Northstar Village Commercial and Old Greenwood Townhomes in Lake Tahoe, California and Union Center land in Denver, Colorado, which had sales in the twelve months ended December 31, 2006, but no sales in the same period 2005.
- a decrease of $10.5 million at Desert Mountain primarily related to reduced net revenue from lot sales due to a decrease in the number of lots sold partially offset by an increase in the average sales price per lot and lower membership transfer fee income, partially offset by

increased unit sales revenue due to an increase in the number of units sold.

Resort/Hotel Property revenues decreased $0.4 million, or 0.3%, to $142.2 million, primarily due to:

a decrease of $4.7 million in revenue at the Park Hyatt Beaver Creek related to a decrease in occupancy due to construction activity on the property and the closure of the Allegria Spa for expansion; and

a decrease of $4.6 million due to the contribution in January 2005, of the Canyon Ranch® Properties to a newly formed entity, CR Operating, LLC, in which we have a 48% member interest that is accounted for as an unconsolidated investment; partially offset by

an increase of $4.9 million in revenue at the remaining Luxury Resort and Spa Properties primarily at the Fairmont Sonoma Mission Inn, which experienced an 14% increase in revenue per available room (from $207 to $235) resulting from an increase of 5% in average daily rate (from $292 to $306) and a six percentage point increase in occupancy (from 71% to 77%); and

an increase of $4.0 million in room revenue at the Upscale Business Class Hotel Properties primarily related to a 12% increase in revenue per available room (from $90 to $101) resulting from a 13% increase in average daily rate (from $123 to $139) with occupancy remaining flat.

Table of Contents

## Property Expenses

Total property expenses decreased $81.2 million, or 11.0%, to $658.0 million for the year ended December 31, 2006, as compared to $739.2 million for the year ended December 31, 2005. The primary components of the decrease in total property expenses are discussed below.

Office Property expenses increased $10.9 million, or 5.6%, to $206.6 million, primarily due to:

- an increase of $9.4 million in operating expenses of the 51 consolidated Office Properties (excluding properties acquired, disposed, or stabilized in 2005 and 2006) that we owned or had an interest in primarily due to increased property taxes, utilities, general building expenses, cleaning expenses, insurance expense and non-recoverable administrative expenses (primarily bad debt);
- an increase of $3.4 million from the acquisition of Financial Plaza in January 2006;
- an increase of $1.4 million related to lease termination expenses; and
- an increase of $1.1 million related to the cost of providing third-party management services primarily due to increased staffing and salary expenses and the joint venture of One Buckhead Plaza in June 2005, which are recouped by increased third party fee income and direct expense reimbursements; partially offset by
- a decrease of $3.1 million primarily due to the joint venturing of Fulbright Tower in February 2005 and One Buckhead Plaza in June 2005; and
- a decrease of $1.3 million related to decreased consulting and legal fees.

Resort Residential Development Property expenses decreased $89.2 million, or 20.6%, to $343.0 million, primarily due to:

- a decrease of $86.2 million in CRDI expenses primarily related to:
  - o a net decrease of $151.4 million primarily related to product mix in lots and units available for sale in 2005 versus 2006 at Hummingbird Lodge in Bachelor Gulch, Colorado, Northstar Ironhorse and Gray s Crossing in Lake Tahoe, California, Creekside Townhomes, Brownstones Phase I, and Delgany, all in Denver, Colorado, and Eagle Ranch in Eagle, Colorado, which had sales in the twelve months ended December 31, 2005, but reduced sales in the same period 2006, partially offset by Old Greenwood Timeshares in Lake Tahoe, California, and Main Street Station in Breckenridge, Colorado, which had sales in the twelve months ended December 31, 2005, but increased sales in the same period 2006; and
  - o a decrease of $30.4 million primarily related to product mix in lots and units available for sale in 2005 versus 2006 at Horizon Pass Lodge in Bachelor Gulch, Colorado, Creekside Phase II in Denver, Colorado, and Old Greenwood Lots in Lake Tahoe, California, which had sales in the twelve months ended December 31, 2005, but no sales in the same period 2006; partially offset by
  - o an increase of $93.2 million primarily related to product mix in lots and units available for sale in 2006 versus 2005 at Village Walk and EW Hotel Residences in Beaver Creek, Colorado, Northstar Big Horn, Northstar Village Commercial and Old Greenwood Townhomes in Lake Tahoe, California and Union Center land in Denver, Colorado, which had sales in the twelve months ended December 31, 2006, but no sales in the same period 2005.
- an increase of $1.1 million in at CRDI marketing expense at CRDI; and
- a decrease of $7.1 million at Desert Mountain, primarily related to a decrease of $9.8 million in cost of sales primarily due to decreased lot sales and product mix and a decrease of $4.1 million in general and

administrative expenses; partially offset by an increase of $5.5 million in the development costs recognized using the percentage complete method, and an increase of $1.4 million in club operating expense; partially offset by

an increase of $2.4 million primarily due to marketing expenses related to the Ritz-Carlton Tower Residences and Regency Row in Dallas, Texas.

Resort/Hotel Property expenses decreased $2.9 million, or 2.6%, to $108.4 million, primarily due to:

a decrease of $4.1 million due to the contribution, in January 2005, of the Canyon Ranch Properties to a newly formed entity, CR Operating, LLC, in which we have a 48% member interest that is accounted for as an unconsolidated investment; and

a decrease of $2.3 million at the Park Hyatt Beaver Creek related to a decrease in occupancy due to construction activity on the property and the closure of the Allegria Spa for expansion; partially offset by

an increase of $2.8 million at the remaining Luxury Resort and Spa Properties, primarily at Sonoma Mission Inn, related to a 6 percentage point increase in occupancy (from 71% to 77%); and

an increase of $0.6 million primarily due to pre-opening expenses at The Ritz-Carlton Dallas.

Table of Contents

## Other Income/Expense

Total other expenses increased $1.8 million, or 0.7%, to $251.8 million for the year ended December 31, 2006, compared to $250.0 million for year ended December 31, 2005. The primary components of the increase in total other income and expenses are discussed below.

## Other Income

Other income increased $2.7 million, or 2.8%, to $95.3 million for the year ended December 31, 2006, as compared to $92.6 million for the year ended December 31, 2005. The primary components of the increase in other income are discussed below.

Income from sale of investment in unconsolidated company increased $17.8 million due primarily to the sale of the Four Westlake Park, Three Westlake Park and Chase Tower Office Properties in 2006, partially offset by the sale of our interests in the entity that owned the 5 Houston Center Office Property in 2005.

Income from investment land sales decreased $8.6 million due primarily to the gain on the sale of two parcels of undeveloped investment land in Houston, Texas in 2005.

Loss on joint venture of properties decreased $2.7 million, primarily due to the 2005 write-off of capitalized internal leasing costs related to prior year joint venture of properties.

Interest and other income increased $18.2 million, or 62.1% to $47.4 million primarily due to:

§ an increase of $13.0 million from mezzanine loans and other loans attributable to an increase of $86.6 million in the weighted average mezzanine loan balance (from $88.7 million to $175.3 million) and a 1.10 percentage point increase in the weighted average interest rate (from 11.92% to 13.02%);

§ an increase of $6.2 million due to prepayment fees on two mezzanine loans that were paid off in first quarter 2006; and

§ an increase of $2.6 million related to the amortization of imputed interest related to the El Paso lease termination and contractual full service rents to interest income; partially offset by

§ a decrease of $2.3 million interest earned on U.S. Treasury and government sponsored agency securities purchased for debt defeasance in order to release the lien on properties securing the LaSalle Note I and Note II and Nomura Funding VI Note; and

§ a decrease of $1.7 million in other income from legal settlement proceeds received in 2005 in connection with certain deed transfer taxes.

Equity in net income of unconsolidated companies decreased $27.4 million to $0.3 million primarily due to:

§ a decrease of $15.9 million in Temperature-Controlled Logistics equity in net income primarily attributable to:
  - ° an increase of $6.8 million in debt related expense due to
    - Ø a prepayment fee related to Goldman Sachs debt defeasance of $4.6 million;
    - Ø a write-off of $2.2 million of unamortized deferred financing costs associated with the Goldman Sachs and Morgan Stanley debt paid off in 2006; and
  - ° an increase of $2.7 million related to adjustments for vacation accrual, workers compensation and legal expenses; and
  - ° a decrease of $5.7 million in operating margins, primarily in the transportation segment due to services with FEMA in 2005 in the wake of Hurricane Katrina.

§ a decrease of $5.7 million in Other equity in net income primarily attributable to a decrease of income from the G2 and SunTx investments;

- § a decrease of $3.6 million in Resort/Hotel equity in net income primarily attributable to a $3.0 million license fee from Canyon Ranch Living in Miami, Florida, of which our portion was $1.4 million, in the first quarter of 2005 and $2.2 million due to increased expenses in 2006 compared to 2005 associated with Canyon Ranch Operating, LLC; and

- § a decrease of $2.3 million in Office equity in net income primarily due to a $0.8 million decline in operations at Bank One Center, a $0.7 million decrease in operations at Houston Center and a $0.5 million decrease related to the disposition of 5 Houston Center in December 2005.

**Other Expenses**

Other expenses increased $4.5 million, or 1.3%, to $347.2 million for the year ended December 31, 2006, compared to $342.7 million for the year ended December 31, 2005. The primary components of the increase in other expenses are discussed below.

Corporate general and administrative costs decreased $5.4 million, or 10.7%, to $44.9 million primarily due to changes in the short-term incentive compensation plans and lower compensation expense associated with restricted units granted under our long-term incentive compensation plans in December 2004 and May 2005.

Interest expense decreased $2.4 million, or 1.8%, to $134.3 million due to an increase of $11.8 million in capitalized interest (from $21.9 million to $33.7 million); partially offset by an increase of $123.0 million in the weighted average debt balance (from $2.271 billion to $2.394 billion) and a 0.12 percentage point increase in the hedged weighted average interest rate (from 6.98% to 7.10%).

Extinguishment of debt expense decreased $2.2 million due to the write off of deferred financing costs, of which $0.7 million related to the joint venture or sale of real estate assets in 2005.

Depreciation and amortization expense increased $6.0 million, or 4.2%, primarily due to;

§ an increase of $5.3 million related to additions to leasehold and building improvements and lease conversions; and

§ an increase of $5.1 million due to the acquisition of Financial Plaza in January 2006; partially offset by

§ a decrease of $2.3 million related to lease terminations in 2005; and

§ a decrease of $2.0 million due to the joint venture of Fulbright Tower in February 2005 and One Buckhead Plaza in June 2005.

Other expense increased $9.0 million to $13.0 million due primarily to legal and advisory fees for certain contemplated strategic alternatives.

**Income Tax Benefit/Expense**

The $12.0 million increase in the income tax benefit for the year ended December 31, 2006, compared to the income tax expense of $8.5 million for the year ended December 31, 2005, is primarily due to a $10.8 million increased tax benefit due to decreases from 2005 to 2006 in taxable income of the Resort Residential Development Properties and a $2.1 million decrease in tax expense related to 2005 income from the G2 and SunTx investments.

**Discontinued Operations**

Income from discontinued operations on assets sold and held for sale, net of minority interests and taxes, decreased $78.4 million to $13.8 million primarily due to:

a decrease of $74.8 million, net of minority interest and taxes due to an $89.2 million aggregate gain on the sale of four properties in 2005 compared to $14.4 million aggregate gain on sale of three properties in 2006; and

a decrease of $4.5 million income, net of minority interest and taxes, due to the reduction of net income associated with properties held for sale in 2006 compared to 2005.

**Comparison of the year ended December 31, 2005 (Restated), to the year ended December 31, 2004 (Restated)**

**Property Revenues**

Total property revenues increased $17.9 million, or 1.8%, to $1,018.1 million for the year ended December 31, 2005, as compared to $1,000.2 million for the year ended December 31, 2004. The primary components of the increase in total property revenues are discussed below.

Office Property revenues decreased $103.0 million, or 21.6%, to $372.8 million, primarily due to:

§ a decrease of $154.9 million due to the joint ventures of The Crescent, Trammell Crow Center, Fountain Place, Houston Center and Post Oak Central in November 2004; partially offset by Fulbright Tower, which was acquired in December 2004 and joint ventured in February 2005, and One Buckhead Plaza which was acquired in April 2005 and joint ventured in June 2005; partially offset by

§ an increase of $26.9 million from the acquisition of Hughes Center in January through May 2004, Dupont Centre in March 2004, The Alhambra in August 2004, One Live Oak and Peakview Tower in December 2004 and the Exchange Building in February 2005;

§ an increase of $17.3 million resulting from third party management and leasing services and related direct expense reimbursements due to the joint ventures of The Crescent, Trammell Crow Center, Fountain Place, Houston Center and Post Oak Central in November 2004, and Fulbright Tower in February 2005 and One Buckhead Plaza in June 2005;

§ an increase of $6.2 million from the 42 consolidated Office Properties (excluding 2004 and 2005 acquisitions, dispositions and properties held for sale) that we owned or had an interest in, primarily due to a 2.6 percentage point increase in average occupancy (from 83.3% to 85.9%), increased expense recovery revenue related to the increase in occupancy and increased recoverable expenses, and increased parking revenue; partially offset by a decline in full service weighted average rental rates; and

§ an increase of $2.2 million in net lease termination fees (from $9.0 million to $11.2 million) primarily due to the El Paso lease termination.

Resort Residential Development Property revenues increased $192.8 million, or 62.2%, to $502.7 million, primarily due to:

§ an increase of $189.7 million in CRDI revenues primarily related to:

  o an increase of $239.5 million primarily related to product mix in lots and units available for sale in 2005 versus 2004 at Hummingbird Lodge in Bachelor Gulch, Colorado, Northstar Village in Lake Tahoe, California, and Creekside Phase II, Creekside Townhomes, Brownstones Phase I and Delgany, all in Denver, Colorado, which had sales in the twelve months ended December 31, 2005, but no sales in the same period 2004; partially offset by

  o a decrease of $47.3 million primarily related to product mix in lots and units available for sale in 2004 versus 2005 at Horizon Pass Townhomes in Bachelor Gulch, Colorado, Park Place, Park Tower and Central Platte Valley, all in Denver, Colorado, and Cresta Run in Edwards, Colorado, which had sales in the twelve months ended December 31, 2004, but no sales in the same period 2005; and

  o a net decrease of $4.0 million primarily related to product mix in lots and units available for sale in 2004 versus 2005 at Horizon Pass Lodge in Bachelor Gulch, Colorado, Old Greenwood Lots in Lake Tahoe, California, Creekside Phase I in Denver, Colorado, and Main Street Station in Breckenridge, Colorado, which had sales in the twelve months ended December 31, 2004, but reduced sales in the same period 2005, partially offset by Gray s Crossing and Old Greenwood Timeshares in Lake Tahoe, California, and Eagle Ranch in Eagle, Colorado, which had sales in the twelve months ended December 31, 2004, but increased sales in the same period 2005.

Resort/Hotel Property revenues decreased $71.9 million, or 33.5%, to $142.6 million, primarily due to:

§ a decrease of $88.8 million due to the contribution, in January 2005, of the Canyon Ranch Properties to a newly formed entity, CR Operating, LLC, in which we have a 48% member interest that is accounted for as an unconsolidated investment; partially offset by

§ an increase of $6.9 million in room revenue at the Luxury Resort and Spa Properties related to a 20% increase in revenue per available room (from $171 to $206) resulting from a 12% increase in average daily rate (from $285 to $319) and a 4 percentage point increase in occupancy (from 60% to 64%);

§ an increase of $4.5 million in food and beverage, spa and other revenue at the Luxury Resort and Spa Properties primarily due to a 12 percentage point increase in occupancy (from 59% to 71%) at the Sonoma

Mission Inn primarily related to the renovation of the 97 historic inn rooms which were out of service during the first two quarters of 2004;

§ an increase of $2.8 million in room revenue at the Upscale Business-Class Hotel Properties primarily due to a 13% increase in revenue per available room (from $80 to $90) resulting from an increase of 6% in average daily rate (from $116 to $123) and a 4 percentage point increase in occupancy (from 69% to 73%); and

§ an increase of $2.6 million in food and beverage and other revenue at the Upscale Business-Class Hotel Properties primarily related to the 4 percentage point increase in occupancy (from 69% to 73%) in conjunction with increased group volume.

**Property Expenses**

Total property expenses increased $54.0 million, or 7.9%, to $739.3 million for the year ended December 31, 2005, as compared to $685.3 million for the year ended December 31, 2004. The primary components of the variances in property expenses are discussed below.

Office Property expenses decreased $38.4 million, or 16.4%, to $195.8 million, primarily due to:

§ a decrease of $73.7 million due to the joint ventures of The Crescent, Trammell Crow Center, Fountain Place, Houston Center and Post Oak Central in November 2004, partially offset by Fulbright Tower, which was acquired in December 2004 and joint ventured in February 2005 and One Buckhead Plaza, which was acquired in April 2005 and joint ventured in June 2005; partially offset by

§ an increase of $14.7 million related to the cost of providing third-party management services due to the joint venture of The Crescent, Trammell Crow Center, Fountain Place, Houston Center and Post Oak Central in November 2004, and Fulbright Tower in February 2005 and One Buckhead Plaza in June 2005, which are recouped by increased third party fee income and direct expense reimbursements;

52

- § an increase of $10.7 million from the acquisition of Hughes Center in January through May 2004, Dupont Centre in March 2004, The Alhambra in August 2004, One Live Oak and Peakview Tower in December 2004 and the Exchange Building in February 2005;
- § an increase of $4.8 million in operating expenses of the 42 consolidated Office Properties (excluding 2004 and 2005 acquisitions, dispositions and properties held for sale) that we owned or had an interest in primarily due to increased administrative costs, utilities, general building and property taxes; and
- § an increase of $4.5 million due to increased payroll and benefit costs and Sarbanes-Oxley compliance costs.

Resort Residential Development Property expenses increased $160.9 million, or 59.3%, to $432.2 million, primarily due to:

- § an increase of $160.5 million in CRDI expenses primarily related to:
  - o an increase of $207.3 million primarily related to product mix in lots and units available for sale in 2005 versus 2004 at Hummingbird Lodge in Bachelor Gulch, Colorado, Northstar Village in Lake Tahoe, California, and Creekside Phase II, Creekside Townhomes, Brownstones Phase I, and Delgany, all in Denver, Colorado, which had sales in the twelve months ended December 31, 2005, but no sales in the same period 2004; partially offset by
  - o a decrease of $41.8 million primarily related to product mix in lots and units available for sale in 2004 versus 2005 at Horizon Pass Townhomes in Bachelor Gulch, Colorado, Park Place, Park Tower, and Central Platte Valley, all in Denver, Colorado, and Cresta Run in Edwards, Colorado, which had sales in the twelve months ended December 31, 2004, but no sales in the same period 2005; and
  - o a net decrease of $5.5 million primarily related to product mix in lots and units available for sale in 2004 versus 2005 at Horizon Pass Lodge in Bachelor Gulch, Colorado, Old Greenwood Lots in Lake Tahoe, California, Creekside Phase I in Denver, Colorado, and Main Street Station in Breckenridge, Colorado, which had sales in the twelve months ended December 31, 2004, but reduced sales in the same period 2005, partially offset by Gray s Crossing and Old Greenwood Timeshares in Lake Tahoe, California, and Eagle Ranch in Eagle, Colorado, which had sales in the twelve months ended December 31, 2004, but increased sales in the same period 2005.

Resort/Hotel Property expenses decreased $68.5 million, or 38.1%, to $111.3 million, primarily due to:

- § a decrease of $76.5 million due to the contribution, in January 2005, of the Canyon Ranch Properties to a newly formed entity, CR Operating, LLC, in which we have a 48% member interest that is accounted for as an unconsolidated investment; partially offset by
- § an increase of $5.2 million in operating expenses at the Luxury Resort and Spa Properties primarily due to a 12 percentage point increase in occupancy at Sonoma Mission Inn (from 59% to 71%) primarily related to the renovation of the 97 historic inn rooms which were out of service during the first two quarters of 2004; and
- § an increase of $2.7 million in operating expenses at the Upscale Business-Class Hotel Properties primarily related to a 9 percentage point increase in occupancy at Houston Renaissance (from 61% to 70%).

**Other Income/Expense**

Total expenses increased $126.2 million, or 101.9%, to $250.0 million for the year ended December 31, 2005, compared to $123.8 million for year ended December 31, 2004. The primary components of the increase in total other income and expenses are discussed below.

**Other Income**

Other income decreased $219.7 million, or 70.3%, to $92.6 million for the year ended December 31, 2005, as compared to $312.3 million for the year ended December 31, 2004. The primary components of the decrease in other income are discussed below.

Gain on joint venture of properties decreased $268.5 million, due primarily to:

- § $265.8 million decrease due to the gain on the joint venture of The Crescent, Fountain Place, Trammell Crow Center, Houston Center and Post Oak Central Office Properties in 2004; and

- § $4.9 million decrease due to the write-off of capitalized internal leasing costs related to prior year joint venture of properties; partially offset by

- § $1.9 million increase due to the gain on the joint venture of Fullbright Tower and One Buckhead in 2005.

Income from investment land sales decreased $10.3 million due to the gain of $8.6 million on sales of two parcels of undeveloped investment land in 2005 compared to $18.8 million gain on sales of five parcels of undeveloped investment land in 2004.

Income from sale of investment in unconsolidated company increased $29.9 million due to the sale of our interests in the entity that owned the 5 Houston Center Office Property in 2005.

Interest and other income increased $11.3 million to $29.3 million primarily due to:

- § $10.5 million interest from mezzanine loans;

- § $3.7 million interest from U.S. Treasury and government sponsored agency securities purchased in December 2004 and January 2005 related to debt defeasance in order to release the lien on properties securing the LaSalle Note I and Nomura Funding VI Note; and

- § $1.7 million increase in other income from legal settlement proceeds received in connection with certain deed transfer taxes; partially offset by

Table of Contents

§ $3.7 million received in 2004 from COPI pursuant to the COPI bankruptcy plan for notes receivable previously written off in 2001.

Equity in net income of unconsolidated companies increased $17.9 million to $27.6 million primarily due to:

§ an increase of $18.2 million in Other equity in net income primarily attributable to an increase of $6.1 million of income from the G2 investment and an increase of $11.5 million of income from the SunTx investment; and

§ an increase of $5.2 million in Office equity in net income primarily attributable to the joint ventures of The Crescent, Fountain Place, Trammell Crow Center, Houston Center and Post Oak Central Office Properties; partially offset by

§ a decrease of $6.0 million in Temperature-Controlled Logistics equity in net income primarily attributable to the gain on the sale of a portion of our interests in AmeriCold to The Yucaipa Companies in 2004.

**Other Expenses**

Other expenses decreased $93.5 million, or 21.4%, to $342.6 million for the year ended December 31, 2005, compared to $436.0 million for the year ended December 31, 2004. The primary components of the decrease in other expenses are discussed below.

Extinguishment of debt expense decreased $40.4 million, or 94.8%, to $2.2 million due to:

§ $17.5 million related to the securities purchased in excess of the debt balance to defease LaSalle Note I in connection with the joint venture of Office Properties in 2004;

§ $17.5 million prepayment penalty associated with the payoff of the JP Morgan Chase Mortgage Loan in connection with the joint venture of Office Properties in 2004;

§ $1.0 million mortgage prepayment fee associated with the payoff of the Lehman Brothers Holdings, Inc. Loan in connection with the joint venture of Office Properties in 2004; and

§ $6.6 million write-off of deferred financing costs, of which $3.1 million related to the joint venture or sale of real estate assets in 2004; partially offset by

§ $2.1 million write-off of deferred financing costs, of which $0.7 million related to the joint venture or sale of real estate assets in 2005.

Interest expense decreased $40.1 million, or 22.7%, to $136.7 million due to a decrease of $392.0 million in the weighted average debt balance (from $2,664 billion to $2,272 billion), partially offset by a .03 percentage point increase in the hedged weighted average interest rate (from 6.95% to 6.98%) and $3.0 million cash flow payments recorded as interest expense related to the Fountain Place transaction in June 2004.

Depreciation and amortization costs decreased $18.5 million, or 11.6%, to $141.4 million due to:

§ $19.0 million decrease in Office Property depreciation expense, primarily due to:

  ° $36.7 million decrease attributable to the joint ventures of The Crescent, Fountain Place, Trammell Crow Center, Houston Center and Post Oak Central in November 2004, partially offset by Fulbright Tower which was acquired in December 2004 and subsequently joint ventured in February 2005 and One Buckhead Plaza which was acquired in April 2005 and subsequently joint ventured in June 2005; partially offset by

  ° $13.2 million increase from the acquisitions of Hughes Center in January through May 2004, Dupont Centre in March 2004, The Alhambra in August 2004, One Live Oak, Fulbright Tower and Peakview Tower in December 2004 and the Exchange Building in February 2005; and

  ° $3.1 million increase primarily due to increased building and leasehold improvements; and

§ $5.2 million decrease in Resort/Hotel Property depreciation expense primarily related to the joint venture of the Canyon Ranch Properties, partially offset by the reclassification of the Denver City Marriott Hotel Property from held for sale to held and used; partially offset by

§ $6.6 million increase in Resort Residential Development Property depreciation expense primarily related to club amenities and golf course improvements at CRDI and Desert Mountain.

Amortization of deferred financing costs decreased $5.0 million, or 38.2%, to $8.1 million primarily due to the refinancing and modification of the Credit Facility in February 2005 and December 2005, partially offset by the reduction of the Fleet Fund I and II Term Loan in January 2004 and the payoff of the Lehman Capital Note in November 2004.

Impairment charges related to real estate assets decreased $4.1 million due to the impairment of $4.1 million related to the demolition of the old clubhouse at the Sonoma Club in the third quarter 2004 in order to construct a new clubhouse.

Corporate general and administrative costs increased $11.3 million, or 29.0%, to $50.4 million due primarily to an increase in compensation expense associated with restricted units granted under our long-term incentive compensation plans in December 2004 and May 2005.

**Income Tax Expense/Benefit**

The $20.7 million decrease in the income tax benefit to an $8.5 million income tax expense for the year ended December 31, 2005, as compared to the income tax benefit of $12.2 million for the year ended December 31, 2004, is primarily due to:

$8.5 million decreased tax benefit on the Resort Residential Development Properties primarily attributable to the results of operations at CRDI;

$5.8 million decreased tax benefit on the Resort/Hotel Properties due to the contribution of the Canyon Ranch Properties to a newly formed entity, CR Operating, LLC, in which we have a 48% member interest that is accounted for as an unconsolidated investment and reduced taxable losses at the other properties;

$4.0 million tax expense related to income from our investment in SunTx; and

$2.8 million tax expense related to income from our investment in G2.

**Discontinued Operations**

Income from discontinued operations on assets sold and held for sale, net of minority interests and taxes, increased $83.7 million to $92.3 million for the year ended December 31, 2005, due to:

an increase of $88.1 million, net of minority interest, primarily due to the $89.2 million gain on the sale of four properties in 2005; and

an increase of $2.0 million, net of minority interest, due to an aggregate $3.0 million impairment on three office properties in 2004 compared to $1.0 million impairment of Waterside Commons office property in 2005; partially offset by

a decrease of $6.4 million, net of minority interest, due to the reduction of net income associated with properties held for sale in 2005 compared to 2004.

## Liquidity and Capital Resources

**Overview**

Our primary sources of liquidity are cash flow from operations, our credit facility, construction loans and proceeds from asset sales and joint ventures. Our short-term liquidity requirements through December 31, 2007 consists primarily of our normal operating expenses, maturity of our 7.5% senior unsecured notes dues September 2007, the 2007 Notes, recurring principal and interest payments on our debt, Resort Residential Development capital expenditures, capital expenditures for operating properties, potential redemption of restricted units from our Operating Partnership and distributions to our shareholders. Our long-term liquidity requirements are substantially similar to our short-term liquidity requirements other than the level of debt obligations maturing after December 31, 2007.

We intend on using the proceeds from the substantial asset sales that we expect to make in accordance with our Strategic Plan which is discussed in the Overview to this Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations to address many of our long-term liquidity requirements early, including: retiring our 9.25% senior notes due April 2009, the 2009 Notes, selected mortgage debt, our Series B Preferred Shares and outstanding borrowings under our revolving credit facility. Additionally, if and when we sell our Resort Residential Development Properties, we expect to eliminate all related construction debt as well as future Resort Residential capital expenditures.

**Short-Term Liquidity**

We believe that cash flow from operations will be sufficient to cover our normal operating expenses, interest payments on our debt, distributions on our preferred shares, non-revenue enhancing capital expenditures and revenue enhancing capital expenditures (including property improvements, tenant improvements and leasing commissions) in 2007. The cash flow from our Resort Residential Development Segment is cyclical in nature and primarily realized in the last quarter of each year. While we expect to sell virtually all of the investments comprising this segment in 2007, we may meet temporary shortfalls in operating cash flow caused by this cyclicality through working capital draws under our credit facility, additional borrowings or asset sales in accordance with our Strategic Plan. As of December 31, 2006, we had up to $239.3 million of borrowing capacity available under our credit facility. If our Board of Trustees continues to declare distributions on our common shares at current levels, our cash flow from operations, after payments discussed above, is not expected to fully cover such distributions on our common shares in 2007. However, as part of our Strategic Plan, we intend to align our distributions with industry-accepted pay-out ranges to allow for retention of capital for growth. We will communicate our distribution plans as we execute asset sales. In the meantime, we intend to use proceeds from any asset sales and joint ventures and borrowings under our credit facility to cover any distribution shortfall.

In addition, through December 31, 2007, we may make capital expenditures that are not in the ordinary course of operations of our business of approximately $140.3 million, primarily relating to new developments of investment property. We anticipate funding these short-term liquidity requirements primarily through construction loans and borrowings under our credit facility and any asset sales. As of December 31, 2006, we also had maturing debt obligations of $750.0 million through December 31, 2007, made up primarily of the maturity of the 2007 Notes, the GACC Note (which has three one-year extension options), Funding I Defeasance (to be repaid from proceeds of defeasance investments), the Mass Mutual Note and the KeyBank II loan. The 2007 Notes are expected to be repaid using proceeds from asset sales in accordance with our Strategic Plan. We intend to refinance or pay off with asset sales the Mass Mutual and KeyBank II loans. In addition, $108.3 million of these maturing debt obligations relate to the Resort Residential Development Segment and are expected to be repaid with the sales of the corresponding land or units or are expected to be refinanced with additional debt facilities. The remaining maturities consist primarily of normal principal amortization and are expected to be met with cash flow from operations.

**Long-Term Liquidity**

Our long-term liquidity requirements as of December 31, 2006, consist primarily of $1.5 billion of debt maturing after December 31, 2007, some of which we expect to repay in 2007 from asset sales as discussed above. We anticipate meeting these obligations, to the extent that these obligations remain outstanding after we have fully implemented our Strategic Plan, primarily through refinancing maturing debt with long-term secured and unsecured debt, construction loans and through other debt and equity financing alternatives, as well as cash proceeds from joint ventures.

We anticipate that long-term liquidity requirements will also include amounts required for future unidentified property acquisitions, mezzanine notes and capital expenditures. Property acquisitions and capital expenditures are expected to be funded with any cash reserves remaining from asset sales made in accordance with our Strategic Plan, available cash flow from operations, borrowings under our credit facility, construction and permanent secured financing, other debt and equity financing alternatives, as well as cash proceeds from future asset sales and joint ventures. Mezzanine notes are expected to be funded with borrowings under our credit facility and through the use of our warehouse facilities governed by repurchase agreements.

**Cash Flows**

Our cash flow from operations is primarily attributable to the operations of our Office, Resort Residential Development and Resort/Hotel Properties. The level of our cash flow depends on multiple factors, including rental rates and occupancy rates at our Office Properties, sales of lots and units at our Resort Residential Development Properties and room rates and occupancy rates at our Resort/Hotel Properties. Our net cash provided by operating activities is also affected by the level of our operating and other expenses, as well as Resort Residential capital expenditures for existing and committed projects.

During the year ended December 31, 2006, our cash flow from operations was insufficient to fully cover the distributions on our common shares. We funded this shortfall primarily with a combination of proceeds from asset sales and borrowings under our credit facility.

| (in millions) | | **For the year ended December 31, 2006** |
|---|---|---|
| Cash used in Operating Activities | $ | (102.8) |
| Cash provided by Investing Activities | | 216.8 |
| Cash used in Financing Activities | | (122.7) |
| Decrease in Cash and Cash Equivalents | $ | (8.7) |
| Cash and Cash Equivalents, Beginning of Period | | 86.2 |
| Cash and Cash Equivalents, End of Period | $ | 77.5 |

*Operating Activities*

Our cash used in operating activities of $102.8 million is attributable to Property operations.

*Investing Activities*

Our cash provided by investing activities of $216.8 million is primarily attributable to:

- $186.4 million proceeds from defeasance investment maturities and other securities, primarily due to the maturity of the securities securing the LaSalle Note II which was repaid in March 2006 and the sale of our available for sale marketable securities;

- $102.9 million proceeds from sale of investment in unconsolidated company due to our sale of the Four Westlake Park, Three Westlake Park, Bank One Center and Chase Tower Office Properties, on behalf of the joint ventures in which we had an interest;

$103.9 million proceeds from property sales due to the sale of our interest in the Paseo Del Mar Office Property, the sale of the Waterside Commons Office Property, and the sale of the JPI Multi-Family Investments luxury apartment project;

$81.3 million return of investment in unconsolidated companies, primarily due to the distributions received from AmeriCold Realty Trust, Main Street Partners, L.P., Blue River Land Company, LLC and Redtail Capital Partners, L.P.;

$69.0 million decrease in notes receivable, primarily due to the repayment of five of our mezzanine loans, offset by four new mezzanine loans; and

$9.6 million decrease in restricted cash.

The cash provided by investing activities is partially offset by:

- $138.2 million for the development of investment properties, due to the development of the JPI Multi-Family Investments luxury apartment project, Paseo del Mar and Parkway at Oakhill office developments, Ritz-Carlton Hotel development and 3883 Hughes Parkway office development;

- $68.7 million for non-revenue enhancing tenant improvement and leasing costs for Office Properties;

- $47.6 million of property improvements for Office and Resort/Hotel Properties;

- $30.7 million for the acquisition of investment properties, primarily due to the acquisition of the Financial Plaza Office Property in January 2006;

- $27.6 million for development of amenities at the Resort Residential Development Properties; and

- $23.5 million additional investment in unconsolidated companies, primarily related to our investment in Riverfront Village and Redtail Capital Partners, L.P.

*Financing Activities*

Our cash used in financing activities of $122.7 million is primarily attributable to:

- $193.2 million payments under other borrowings, primarily due to the pay off of the LaSalle Note II funded by proceeds from the maturity of defeasance investments, the pay off of the FHI Finance loan, pay down of the Morgan Stanley note and principal payments related to other debt agreements;

- $184.1 million distributions to common shareholders and unitholders;

- $116.0 million net paydowns under our credit facility;

- $32.0 million distributions to preferred shareholders;

- $18.6 million capital distributions to joint venture partners, primarily due to distributions to JPI Multi-Family Investments, L.P., Desert Mountain and Fairmont Sonoma Mission Inn; and

- $4.1 million debt financing costs, primarily due to the Bank of America loan secured by the Fairmont Sonoma Mission Inn and the Goldman Sachs and Morgan Stanley repurchase agreements secured by mezzanine loans.

The cash used in financing activities is partially offset by:

- $282.4 million proceeds from other borrowings, primarily due to the Key Bank loan secured by distributions from Funding III, IV & V, the Bank of America loan secured by the Fairmont Sonoma Mission Inn, the Morgan Stanley and Goldman Sachs repurchase agreements secured by mezzanine loans and construction draws on our Office developments and The Ritz-Carlton hotel development;

- $111.2 million net proceeds from borrowings for construction costs at the Resort Residential Development Properties;

- $23.1 million proceeds from the exercise of share and unit options; and

- $8.6 million proceeds from capital contributions from our joint venture partners.

Table of Contents

## Liquidity Requirements

## Contractual Obligations

The table below presents, as of December 31, 2006, our future scheduled payments due under these contractual obligations.

| | | Payments Due by Period | | | |
|---|---|---|---|---|---|
| (in millions) | Total | Less than 1 yr | 1-3 years | 3-5 years | More than 5 yrs |
| Long-term debt[1][4] | | | | | |
| Principal payments | $ 2,296.4 | $ 750.0 | $ 1,008.4 | $ 321.5 | $ 216.5 |
| Interest payments | 511.3 | 152.0 | 155.9 | 47.6 | 155.8 |
| Share of unconsolidated debt | 705.6 | 38.6 | 61.8 | 185.1 | 420.1 |
| Ground lease obligations | 147.0 | 1.9 | 3.8 | 4.0 | 137.3 |
| Operating lease obligations [2] | 46.0 | 39.1 | 6.9 | | |
| Share of unconsolidated operating lease obligations | 13.4 | 11.4 | 2.0 | | |
| Significant capital expenditure obligations [3] | 145.3 | 140.3 | 5.0 | | |
| Total contractual obligations | $ 3,865.0 | $ 1,133.3 | $ 1,243.8 | $ 558.2 | $ 929.7 |

(1) Amounts include scheduled principal and interest payments for consolidated debt. We estimate variable rate debt interest payments using the interest rate as of December 31, 2006. Additionally, we have letters of credit issued under our credit facility of $9.5 million which reduces our borrowing capacity. These letters of credit are excluded from the table above as management

believes that this obligation is not reasonably likely to occur.

(2) As part of our ongoing operations, we execute operating lease agreements which generally provide tenants with leasehold improvement allowances and other lease concessions. In addition, we generally pay lease commissions to cooperating third-party brokers. Total committed but unfunded operating lease obligations as of December 31, 2006 are reflected in the above table.

(3) For further detail of significant capital expenditure obligations, see table under Significant Capital Expenditures in this Item 7.

(4) We intend on using the proceeds from the substantial asset sales that we expect to make in accordance with our Strategic Plan which is discussed in the Overview

section to this Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations to address many of our long-term liquidity requirements early, including: retiring our 9.25% senior notes due April 2009, the 2009 Notes, selected mortgage debt, our Series B Preferred Shares and outstanding borrowings under our revolving credit facility. Additionally, if and when we sell our Resort Residential Development Properties, we expect to eliminate all related construction debt as well as future Resort Residential capital expenditures.

We also pay preferred distributions to our Series A and Series B Preferred shareholders. The distributions per Series A Preferred share was $1.6875 per preferred share annualized, or $23.9 million for the year ended December 31, 2006. The distributions per Series B Preferred share was $2.3750 per preferred share annualized, or $8.1 million for the year ended December 31, 2006.

**Debt Financing Summary**

The following table shows summary information about our debt, including our pro rata share of unconsolidated debt, as of December 31, 2006. Listed below are the aggregate required principal payments by year as of December 31, 2006, excluding any extension options. Scheduled principal installments and amounts due at maturity are included.

**Share of**

| (in thousands) | Secured Debt | Defeased Debt | Unsecured Debt | Consolidated Debt | Unconsolidated Debt | Total |
|---|---|---|---|---|---|---|
| 2007 | $ 399,719 | $ 100,279 | $ 250,000 | $ 749,998 | $ 38,613 | $ 788,611 |
| 2008 | 234,290 | 289 | 118,000(1) | 352,579 | 43,465 | 396,044 |
| 2009 | 280,489 | 320 | 375,000 | 655,809 | 18,279 | 674,088 |
| 2010 | 134,043 | 6,337 | | 140,380 | 17,761 | 158,141 |
| 2011 | 181,120 | | | 181,120 | 167,303 | 348,423 |
| Thereafter | 139,151 | | 77,321 | 216,472 | 420,177 | 636,649 |
| | $ 1,368,812 | $ 107,225 | $ 820,321 | $ 2,296,358 | $ 705,598 | $ 3,001,956 |

(1) Borrowings under the credit facility.

Table of Contents

**Significant Capital Expenditures**

As of December 31, 2006, we had unfunded capital expenditures of approximately $145.3 million relating to capital investments that are not in the ordinary course of operations of our business segments. The table below specifies:

- our requirements for capital expenditures (not factoring in project level financing);
- the amounts funded as of December 31, 2006, on a cash basis; and
- amounts remaining to be funded (future funding classified between short-term and long-term capital requirements).

| (in millions) **Project** | **Total Project Cost** [1] | **Amount Spent as of December 31, 2006** | **Amount Remaining To Spend** | **Capital Expenditures Short-Term (Next 12 Months)** [2] | **Capital Expenditures Long-Term (12+ Months)** [2] |
|---|---|---|---|---|---|
| **Consolidated:** | | | | | |
| **Office Segment** | | | | | |
| 3883 Hughes Center [3] | $ 73.0 | $ 56.6 | $ 16.4 | $ 16.4 | $ |
| Parkway at Oakhill[4] | 24.6 | 13.1 | 11.5 | 6.5 | 5.0 |
| **Resort Residential Development Segment** | | | | | |
| Ritz-Carlton Highlands [5] | 402.2 | 22.3 | 8.0[6] | 8.0 | |
| Tahoe Mountain Club [7] | 107.2 | 92.2 | 15.0 | 15.0 | |
| The Ritz-Carlton Phase I[8] | 211.6 | 120.9 | 90.7 | 90.7 | |
| The Ritz-Carlton Phase II[9] | 136.8 | 14.2 | [10] | | |
| **Resort/Hotel Segment** | | | | | |
| Park Hyatt Beaver Creek[11] | 26.6 | 22.9 | 3.7 | 3.7 | |
| **Total** | $ 982.0 | $ 342.2 | $ 145.3 | $ 140.3 | $ 5.0 |

(1) All amounts are approximate.

(2) Reflects our estimate of the breakdown between short-term and long-term capital expenditures.

(3)

We have committed to a first phase office development of 239,000 square feet on land that we own within the Hughes Center complex. We expect to complete the building in the first quarter of 2007. We closed a $52.3 million construction loan in the third quarter of 2005.

(4) In March 2006, we entered into a joint venture agreement with Champion Partners. The joint venture has committed to develop a 144,380 square-foot, two-building office complex in Austin, Texas. The joint venture has a $18.3 million construction loan to fund construction of this project. Amounts in the table represent our portion (90%) of total project costs. The development is scheduled to be completed in first quarter 2007.

(5) We entered into agreements with Ritz-Carlton Hotel Company, L.L.C. for us to develop a 172 room luxury hotel in Lake Tahoe, California. The new luxury property will also include the Ritz-Carlton Residences.

(6) The funding of future potential capital expenditures is dependent upon obtaining a certain level of unit pre-sales, construction financing and assumes we will obtain a joint venture partner for 60% of the equity. In the interim, we have committed up to an additional \$8.0 million in development costs on the project.

(7) As of December 31, 2006, we had invested \$92.2 million in Tahoe Mountain Club, which includes the acquisition of land and development of

golf courses and club amenities. This table includes the development planned for 2007 only. We anticipate collecting membership deposits which will be utilized to fund a portion of the development costs.

(8) We entered into agreements with Ritz-Carlton Hotel Company, L.L.C. for us to develop the first Ritz-Carlton hotel and condominium project in Dallas, Texas. The development plans include a Ritz-Carlton with approximately 218 hotel rooms and 70 residences. Construction on the development is anticipated to be completed in the third quarter of 2007. We have a $169.0 million construction line of credit from KeyBank for the construction of this project.

(9)

We entered into agreements with Ritz-Carlton Hotel Company, L.L.C. for us to develop an additional 96 Ritz-Carlton residences and 4 townhomes adjacent to the Phase I development.

(10) The funding of future potential capital expenditures is dependent upon obtaining a certain level of unit pre-sales and construction financing.

(11) In April 2006, we began renovations at the Park Hyatt Beaver Creek in Avon, Colorado, which consist of the addition of air conditioning, upgrades to the common areas and taking 30 rooms out of service to expand the Allegria Spa within the hotel. The spa expansion and common area upgrade were completed in December 2006.

Table of Contents

**Units Subject to Redemption**

Restricted units granted under the 2004 and 2005 Unit Plans vest in 20% increments when the average closing price of Crescent common shares for the preceding 40 trading days achieves certain targets. Each vested restricted unit will be exchangeable, beginning on the second anniversary of the date of grant, for cash equal to the value of two Crescent common shares based on the closing price of the common shares on the date of exchange, and subject to a six-month hold period following vesting, unless, prior to the date of the exchange, Crescent requests and obtains shareholder approval authorizing it, at its discretion, to deliver instead two common shares in exchange for each such restricted unit. Regular quarterly distributions accrue on unvested restricted units and are payable upon vesting of the restricted units.

The following table presents the amount of restricted unit grants, vested restricted units and the redemption amount by year.

| (dollars in thousands) | Granted[1] | Vested[1] | Redeemed | Vested Unit Redemption Value at December 31, 2006 [2] | Redeemable at December 31, 2006 | Redeemable in 2007 | Redeemable in 2008 |
|---|---|---|---|---|---|---|---|
| 2004 Plan | 3,568,500 | 2,147,500 | 206,750 | $ 38,329 | $ 35,278 | $ 3,051 | $ |
| 2005 Plan | 2,187,500 | 437,500 | | 8,641[3] | | 8,542 | 99 |
| | 5,756,000 | 2,585,000 | 206,750 | $ 46,970 | $ 35,278 | $ 11,593 | $ 99 |

(1) Amounts listed in common share equivalents and are net of forfeitures.

(2) Vested units may be exchanged for cash unless, prior to the date of exchange, Crescent obtains shareholder approval authorizing it, at its discretion, to deliver instead two common shares for each such restricted unit. Redemption

value based on Crescent s closing stock price at December 31, 2006.

(3) Amount is redeemable beginning May 16, 2007.

**Off-Balance Sheet Arrangements Guarantee Commitments**

Our guarantees in place as of December 31, 2006, are listed in the table below. For the guarantees on indebtedness, no triggering events or conditions are anticipated to occur that would require payment under the guarantees and management believes the assets associated with the loans that are guaranteed are sufficient to cover the maximum potential amount of future payments and therefore, would not require us to provide additional collateral to support the guarantees.

| (in thousands)<br>**Debtor** | **Guaranteed Amount Outstanding at December 31, 2006** | **Maximum Guaranteed Amount at December 31, 2006** |
|---|---|---|
| CRDI U.S. Bank National Association[1] | $ 14,346 | $ 20,393 |
| CRDI Eagle Ranch Metropolitan District Letter of Credit[2] | 7,840 | 7,840 |
| Fresh Choice, LLC[3] | 1,000 | 1,000 |
| Total Guarantees | $ 23,186 | $ 29,233 |

(1) We entered into a Payment and Completion Guaranty with U.S. Bank National Association for the repayment of bonds that were issued by the Northstar Community Housing Corporation to fund construction of an employee housing project. The initial guaranty of $20.4 million

decreases to $5.1 million once construction is complete and certain conditions are met and decreases further and is eventually released as certain debt service coverage ratios are achieved.

(2) We provide a $7.8 million letter of credit to support the payment of interest and principal of the Eagle Ranch Metropolitan District Revenue Development Bonds.

(3) We provide a guarantee of up to $1.0 million to GE Capital Franchise Financing Corporation as part of Fresh Choice s bankruptcy reorganization.

**Other Commitments**

In July 2005, we purchased comprehensive insurance that covers us, contractors and other parties involved in the construction of the Ritz-Carlton hotel and condominium project in Dallas, Texas. Our insurance carrier, which will pay the associated claims as they occur under this program and will be reimbursed by us within our deductibles, requires us to provide a $1.7 million letter of credit supporting payment of claims. We believe there is a remote likelihood that payment will be required under the letter of credit.

In connection with the Canyon Ranch transaction, we have agreed to indemnify the founders regarding the tax treatment of the transaction, not to exceed $2.5 million, and certain other matters. We believe there is a remote likelihood that payment will ever be required related to these indemnities.

60

Table of Contents

## Debt and Equity Financing

The significant terms of our primary debt financing arrangements existing as of December 31, 2006, are shown below:

| Description[1] | Secured Asset | Maximum Borrowings | Balance Outstanding at December 31, 2006 | Interest Rate at December 31, 2006 | Maturity Date |
|---|---|---|---|---|---|
| ***Secured Fixed Rate Debt:*** | | | | | |
| AEGON Partnership Note | Greenway Plaza | $ 242,290 | $ 242,290 | 7.53% | July 2009 |
| Prudential Note | 707 17th Street/Denver Marriott | 70,000 | 70,000 | 5.22 | June 2010 |
| JP Morgan Chase III | Datran Center | 65,000 | 65,000 | 4.88 | October 2015 |
| Bank of America Note I | Fairmont Sonoma Mission Inn | 55,000 | 55,000 | 5.40 | February 2011 |
| Morgan Stanley I | The Alhambra | 50,000 | 50,000 | 5.06 | October 2011 |
| Allstate Life Note | Financial Plaza | 38,949 | 38,949 | 5.47 | October 2010 |
| Bank of America Note II | The BAC Colonnade Building | 37,439 | 37,439 | 5.53 | May 2013 |
| Metropolitan Life Note VII | Dupont Centre | 35,500 | 35,500 | 4.31 | May 2011 |
| Column Financial | Peakview Tower | 33,000 | 33,000 | 5.59 | April 2015 |
| Mass Mutual Note | 3800 Hughes | 32,203 | 32,203 | 7.75 | July 2007 |
| Northwestern Life Note | 301 Congress | 26,000 | 26,000 | 4.94 | November 2008 |
| JP Morgan Chase II | 3773 Hughes | 24,755 | 24,755 | 4.98 | September 2011 |
| Allstate Note [2] | 3993 Hughes | 24,025 | 24,025 | 6.65 | September 2010 |
| Metropolitan Life Note VI [2] | 3960 Hughes | 22,074 | 22,074 | 7.71 | October 2009 |
| Construction, Acquisition and other obligations | Various Office and Resort Residential Assets | 40,690 | 40,690 | 2.90 to 13.75 | July 2007 to Dec. 2016 |
| ***Secured Fixed Rate Defeased Debt [3]:*** | | | | | |
| LaSalle Note I | Funding I Defeasance | 100,017 | 100,017 | 7.83 | August 2007 |
| Nomura Funding VI Note | Funding VI Defeasance | 7,208 | 7,208 | 10.07 | July 2010 |
| Subtotal/Weighted Average | | $ 904,150 | $ 904,150 | 6.38% | |
| ***Unsecured Fixed Rate Debt:*** | | | | | |
| The 2009 Notes | | $ 375,000 | $ 375,000 | 9.25% | April 2009 |

| | | | | | |
|---|---|---|---|---|---|
| The 2007 Notes | | 250,000 | 250,000 | 7.50 | September 2007 |
| Subtotal/Weighted Average | | $ 625,000 | $ 625,000 | 8.55% | |
| ***Secured Variable Rate Debt:*** | | | | | |
| GACC Note [4] | Funding One Assets | $ 165,000 | $ 165,000 | 6.82% | June 2007 |
| Morgan Stanley II [5][6] | Mezzanine Investments | 100,000 | 22,311 | 7.37 | March 2009 |
| Goldman Sachs[6][7] | Mezzanine Investments | 100,000 | 10,000 | 6.72 | May 2009 |
| KeyBank II | Distributions from Funding III, IV and V | 75,000 | 75,000 | 7.35 | June 2007 |
| National Bank of Arizona | DMDC Assets | 30,000 | 15,654 | 8.75 | October 2007 |
| Acquisition and other obligations | Various Office and Other Assets | 13,416 | 13,416 | 6.60 to 6.63 | February 2008 to December 2012 |
| ***Secured Variable Rate Construction Debt:*** | | | | | |
| KeyBank I [4] | Ritz-Carlton Dallas Construction | 169,000 | 80,296 | 7.60 | July 2008 |
| JP Morgan Chase | Northstar Big Horn Construction | 84,918 | 56,342 | 7.75 | October 2007 |
| Societe Generale I [8] | 3883 Hughes Construction | 52,250 | 30,587 | 7.22 | September 2008 |
| FirstBank of Vail | Village Walk Construction | 41,782 | 14,041 | 7.75 | February 2008 |
| US Bank II | Northstar Trailside Construction | 36,000 | 1,991 | 8.10 | March 2009 |
| US Bank I [9] | Beaver Creek Landing Construction | 33,400 | 16,446 | 7.10 | February 2008 |
| California Bank & Trust[10] | One Riverfront Construction | 27,500 | 13,861 | 8.38 | March 2008 |
| JP Morgan Chase Bank | Old Greenwood Construction | 20,999 | 16,150 | 8.25 | March 2007 |
| Construction, Acquisition and other obligations | Various Office and Resort Residential Assets | 73,077 | 40,792 | 7.45 to 9.25 | June 2007 to December 2010 |
| Subtotal/Weighted Average | | $ 1,022,342 | $ 571,887 | 7.39% | |
| ***Unsecured Variable Rate Debt:*** | | | | | |
| Credit Facility [11] | | $ 366,759 | $ 118,000 | 6.95% | February 2008 |
| Junior Subordinated Notes | | 51,547 | 51,547 | 7.38 | June 2035 |
| Junior Subordinated Notes | | 25,774 | 25,774 | 7.38 | July 2035 |
| | | $ 444,080 | $ 195,321 | 7.12% | |

| | | | |
|---|---|---|---|
| Subtotal/Weighted Average | | | |
| **Total/Weighted Average** | $ 2,995,572 | $ 2,296,358 | 7.29%(12) |
| **Average remaining term** | | | 3.1 years |

(1) For more information regarding the terms of our debt financing arrangements and the method of calculation of the interest rate for our variable rate debt, see Note 12, Notes Payable and Borrowings under Credit Facility, included in Item 8, Financial Statements and Supplementary Data.

(2) Includes a portion of total premiums of $2.2 million reflecting market value of debt acquired with the purchase of Hughes Center portfolio.

(3) We purchased U.S. Treasuries and government sponsored agency securities, or defeasance

investments, to substitute as collateral for these loans. The cash flow from defeasance investments (principal and interest) matches the total debt service payment of the loans.

(4) This loan has three one-year extension options.

(5) The investments can be financed through March 2008, after which four equal payments are due quarterly. The loan has a provision for a one-year extension which is subject to Morgan Stanley s approval.

(6) The loans supporting these facilities are subject to daily valuations by Morgan Stanley and Goldman Sachs, respectively. We are subject to a margin call if the overall leverage of the facility exceeds certain

thresholds.

(7) The investments can be financed through May 2009. The financing and maturity can be extended one year subject to Goldman Sachs approval.

(8) This loan has two one-year extension options.

(9) This loan has one six-month extension option.

(10) This loan has one one-year extension option.

(11) The Credit Facility has a maximum borrowing capacity of $366.8 million. The $118.0 million outstanding at December 31, 2006, excludes letters of credit issued under the facility of $9.5 million. We are also subject to financial covenants, which include minimum debt service ratios, maximum

leverage ratios and, in the case of the Operating Partnership, a minimum tangible net worth limitation and a fixed charge coverage ratio.

(12) The overall weighted average interest rate does not include the effect of our cash flow hedge agreements. Including the effect of these agreements, the overall weighted average interest rate would have been 7.27%.

We are generally obligated by our debt agreements to comply with financial covenants, affirmative covenants and negative covenants, or some combination of these types of covenants. The financial covenants to which we are subject include, among others, leverage ratios, debt service coverage ratios and limitations on total indebtedness. The affirmative covenants to which we are subject under our debt agreements include, among others, provisions requiring us to comply with all laws relating to operation of any Properties securing the debt, maintenance of those Properties in good repair and working order, maintaining adequate insurance and providing timely financial information. The negative covenants under our debt agreements generally restrict our ability to transfer or pledge assets or incur additional debt at a subsidiary level, limit our ability to engage in transactions with affiliates and place conditions on our or our subsidiaries ability to make distributions.

Failure to comply with covenants generally will result in an event of default under that debt instrument. Any uncured or unwaived events of default under our loans can trigger an increase in interest rates, an acceleration of payment on the loan in default, and for our secured debt, foreclosure on the property securing the debt, and could cause the credit facility to become unavailable to us. In addition, an event of default by us or any of our subsidiaries with respect to any indebtedness in excess of $5.0 million generally will result in an event of default the Credit Facility, the 2007 Notes, 2009 Notes, KeyBank I Loan, Morgan Stanley II Loan, Goldman Sachs Loan, Societe Generale I Construction Loan and KeyBank II Loan, after the notice and cure periods for the other indebtedness have passed. As a result, any uncured or unwaived event of default could have an adverse effect on our business, financial condition, or liquidity.

As of December 31, 2006, no event of default had occurred. Our secured debt facilities generally prohibit loan prepayment for an initial period, allow prepayment with a penalty during a following specified period and allow prepayment without penalty after the expiration of that period. During the year ended December 31, 2006, there were no circumstances that required prepayment penalties or increased collateral related to our existing debt.

**Warehouse Facilities**

We finance certain of our mezzanine loans through the use of warehouse facilities governed by repurchase agreements. A repurchase agreement is a financing under which we pledge one or more of our mezzanine investments as collateral to secure a loan with the repurchase agreement counterparty (i.e. lender). The amount borrowed under a repurchase agreement is limited to a specified percentage, generally not more than 80%, of the estimated market value of the pledged collateral. Repurchase agreements take the form of a sale of the pledged collateral to a lender at an agreed upon price in return for such lender s simultaneous agreement to resell the same securities back to the borrower at a future date (i.e. the maturity of the borrowing), with periodic interest payments during the term of the sale. The cost of borrowings under repurchase agreements generally corresponds to LIBOR plus a margin. Under our repurchase agreements, we retain beneficial ownership of the pledged collateral, while the lender maintains custody of such collateral. At the maturity of a repurchase agreement, we are required to repay the loan, which may be due in installments over a one-year period, and receive back our pledged collateral from the lender or, at the sole discretion of the lender, we may renew such agreement. Under repurchase agreements, a lender may require us to pledge additional assets to such lender (i.e. a margin call) in the event that the lender determines the estimated fair value of our existing pledged collateral has declined below a specified percentage. Our pledged collateral fluctuates in value due to, among other things, market changes in interest rates and matters affecting the real estate underlying certain pledged collateral.

In order to reduce our exposure to counterparty-related risk, our goal is to enter into repurchase agreements with multiple financial institutions, all of whom have investment-grade long-term debt ratings. As of December 31, 2006, we had outstanding repurchase obligations under two repurchase agreements totaling $32.3 million with a weighted average borrowing rate of 7.17%.

Table of Contents

**Derivative Instruments and Hedging Activities**

We use derivative financial instruments to convert a portion of our variable rate debt to fixed rate debt and to manage the fixed to variable rate debt ratio. As of December 31, 2006, we had interest rate swaps and interest rate caps designated as cash flow hedges, which are accounted for in conformity with SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended by SFAS No. 138, *Accounting for Certain Derivative Instruments and Certain Hedging Activities an Amendment of FASB Statement No. 133* and SFAS No. 149, *Amendment of Statement 133 on Derivative Instruments and Hedging Activities.*

The following table shows information regarding the fair value of our interest rate swaps and caps designated as cash flow hedge agreements, which are included in the Other assets, net and Accounts payable, accrued expenses and other liabilities line items in the Consolidated Balance Sheets, and additional interest expense and unrealized gains (losses) recorded in Accumulated other comprehensive income, or OCI, for the year ended December 31, 2006.

| Effective Date | Notional Amount | Maturity Date | Reference Rate | Fair Market Value | Additional (Reduction) Interest Expense | Change in Unrealized Gains (Losses) in OCI |
|---|---|---|---|---|---|---|
| (in thousands) | | | | | | |
| ***Interest rate swaps*** | | | | | | |
| 2/15/03 | $ 100,000 | 2/15/06 | 3.26% | $ | $ (147) | $ (138) |
| 2/15/03 | 100,000 | 2/15/06 | 3.25% | | (148) | (139) |
| 9/02/03 | 200,000 | 9/01/06 | 3.72% | | (1,603) | (1,264) |
| 1/17/05 | | 10/16/06 | 3.74% | | (1) | (205) |
| 4/25/06 | 79,761 | 12/26/07 | 5.20% | 3 | (1) | 3 |
| 9/29/06 | 200,000 | 9/4/07 | 5.20% | 56 | (66) | 56 |
| | | | | $ 59 | $ (1,964) | $ (1,687) |
| ***Interest rate caps*** | | | | | | |
| 1/07/05 | $ 7,800 | 2/01/08 | 6.00% | | 4 | (1) |
| | | | | $ 59 | $ (1,960) | $ (1,688) |

(1) A portion of the interest on the debt that this swap is hedging is capitalized.

In addition, three of our unconsolidated companies have interest rate caps and swaps designated as cash flow hedges of which our portion of change in unrealized losses reflected in OCI was $0.1 million for the year ended December 31, 2006.

**Unconsolidated Debt Arrangements**

As of December 31, 2006, the total debt of the unconsolidated joint ventures and investments in which we have ownership interests was $2.3 billion, of which our share was $705.6 million. We guaranteed $1.0 million of this debt as of December 31, 2006. Additional information relating to our unconsolidated debt financing arrangements is contained in Note 10, Investments in Unconsolidated Companies, of Item 1, Financial Statements and Supplementary Data.

**Share Repurchase Program**

We commenced our share repurchase program in March 2000. On October 15, 2001, our Board of Trust Managers increased from $500.0 million to $800.0 million the amount of outstanding common shares that can be repurchased from time to time in the open market or through privately negotiated transactions. There were no share repurchases under the program for the year ended December 31, 2006. As of December 31, 2006, we had repurchased 20,256,423 common shares under the share repurchase program, at an aggregate cost of approximately $386.9 million, resulting in an average repurchase price of $19.10 per common share. All repurchased shares were recorded as treasury shares.

**Shelf Registration Statement**

On October 29, 1997, we filed a shelf registration statement with the SEC relating to the future offering of up to an aggregate of $1.5 billion of common shares, preferred shares and warrants exercisable for common shares. Management believes the shelf registration statement will provide us with more efficient and immediate access to capital markets when considered appropriate. As of March 5, 2007, approximately $510.0 million was available under the shelf registration statement for the issuance of securities.

Table of Contents

### Unconsolidated Investments

The following is a summary of our ownership in significant unconsolidated joint ventures and investments as of December 31, 2006.

| Entity | Classification | Our Ownership as of December 31, 2006 |
|---|---|---|
| Crescent Irvine, LLC | Office (2211 Michelson Office Development Irvine) | 40.0% (1) |
| Crescent Miami Center, LLC | Office (Miami Center Miami) | 40.0% (2) (3) |
| Crescent One Buckhead Plaza, L.P. | Office (One Buckhead Plaza Atlanta) | 35.0% (4) (3) |
| Crescent POC Investors, L.P. | Office (Post Oak Central Houston) | 23.9% (5) (3) |
| Crescent HC Investors, L.P. | Office (Houston Center Houston) | 23.9% (5) (3) |
| Crescent TC Investors, L.P. | Office (The Crescent Dallas) | 23.9% (5) (3) |
| Crescent Ross Avenue Mortgage Investors, L.P. | Office (Trammell Crow Center, Mortgage Dallas) | 23.9% (6) (3) |
| Crescent Ross Avenue Realty Investors, L.P. | Office (Trammell Crow Center, Ground Lessor Dallas) | 23.9% (6) (3) |
| Crescent Fountain Place, L.P. | Office (Fountain Place Dallas) | 23.9% (6) (3) |
| Crescent Five Post Oak Park L.P. | Office (Five Post Oak Park Houston) | 30.0% (7) (3) |
| Crescent One BriarLake Plaza, L.P. | Office (One BriarLake Plaza Houston) | 30.0% (8) (3) |
| Crescent 1301 McKinney, L.P. | Office (Fulbright Tower Houston) | 23.9% (9) (3) |
| AmeriCold Realty Trust | Temperature-Controlled Logistics | 31.7% (10) |
| CR Operating, LLC | Resort/Hotel | 48.0% (11) |
| CR Spa, LLC | Resort/Hotel | 48.0% (11) |
| East West Resort Development XIV, L.P., L.L.L.P. | Resort Residential Development | 26.8% (12) |
| Blue River Land Company, LLC | Resort Residential Development | 33.2% (13) |
| EW Deer Valley, LLC | Resort Residential Development | 35.7% (14) |
| SunTx Fulcrum Fund, L.P. (SunTx) | Other | 26.5% (15) |
| Redtail Capital Partners, L.P. (Redtail) | Other | 25.0% (16) (3) |
| Fresh Choice, LLC | Other | 40.0% (17) |
| G2 Opportunity Fund, L.P. (G2) | Other | 12.5% (18) |

(1) The remaining 60% interest is owned by an affiliate of Hines.

(2) The remaining 60% interest is owned by an affiliate of a fund managed by JP Morgan Investment Management, Inc., or JPM.

(3) We have negotiated performance

based incentives, which we refer to as promoted interest, which allow for additional equity to be earned if return targets are exceeded.

(4) The remaining 65% interest is owned by Metzler US Real Estate Fund, L.P.

(5) Each limited partnership is owned by Crescent Big Tex I, L.P., which is owned 60% by a fund advised by JPM and 16.1% by affiliates of General Electric, or GE.

(6) Each limited partnership is owned by Crescent Big Tex II, L.P., which is owned 76.1% by a fund advised by JPM.

(7) The remaining 70% interest is owned by an affiliate of GE.

(8) The remaining 70% interest is owned by affiliates of JPM.

(9) The partnership is owned by Crescent Big Tex III, L.P., which is owned 60% by a fund advised by JPM and 16.1% by affiliates of GE.

(10) Of the remaining 68.3% interest, 47.6% is owned by Vornado Realty, L.P. and 20.7% is owned by The Yucaipa Companies.

(11) The remaining 52% interest is owned by the founders of Canyon Ranch and their affiliates. CR Spa, LLC operates three resort spas which offer guest programs and services and sells Canyon Ranch branded skin care products exclusively at the destination health resorts and the resort spas. CR Operating, LLC operates and manages the two Canyon Ranch destination health resorts, Tucson and

Lenox, and collaborates with select real estate developers in developing residential lifestyle communities.

(12) We provided 41.9% of the initial capitalization and the venture is structured such that we own a 26.8% interest after we receive a preferred return on our invested capital and return of our capital. The remaining 73.2% economic interest is owned by parties unrelated to us. East West Resort Development XIV, L.P., L.L.L.P. was formed to co-develop a hotel and condominiums in Avon, Colorado.

(13) The remaining 66.8% interest is owned by parties unrelated to us. Blue River Land Company, LLC was formed to

acquire, develop and sell certain real estate property in Summit County, Colorado.

(14) The remaining 64.3% interest is owned by parties unrelated to us. EW Deer Valley, LLC was formed to acquire, hold and dispose of its 3.3% ownership interest in Empire Mountain Village, L.L.C. Empire Mountain Village, LLC was formed to acquire, develop and sell certain real estate property at Deer Valley Ski Resort next to Park City, Utah.

(15) Of the remaining 73.5%, approximately 42.5% is owned by SunTx Capital Partners, L.P. and the remaining 31.0% is owned by a group of individuals unrelated to us. Of our limited partnership interest in SunTx, 6.3% is

through an unconsolidated investment in SunTx Capital Partners, L.P., the general partner of SunTx. SunTx Fulcrum Fund, L.P. s objective is to invest in a portfolio of entities that offer the potential for substantial capital appreciation.

(16) The remaining 75% interest is owned by Capstead Mortgage Corporation. Redtail was formed to invest up to $100.0 million in equity in select mezzanine loans on commercial real estate over a two-year period.

(17) The remaining 60% interest is owned by Cedarlane Natural Foods, Inc. Fresh Choice is a restaurant owner, operator and developer.

(18) G2 was formed for the purpose of investing in

commercial mortgage backed securities and other commercial real estate investments. The remaining 87.5% interest is owned by Goff-Moore Strategic Partners, L.P., or GMSPLP, and by parties unrelated to us. G2 is managed and controlled by an entity that is owned equally by GMSPLP and GMAC Commercial Mortgage Corporation, or GMACCM. The ownership structure of GMSPLP consists of an approximately 92% limited partnership interest owned directly and indirectly by Richard E. Rainwater, Chairman of our Board of Trust Managers, of which approximately 6% is owned by Darla Moore, who is married to Mr. Rainwater. Approximately

6% general partner interest is owned by John C. Goff, Vice-Chairman of our Board of Trust Managers and our Chief Executive Officer. The remaining approximately 2% general partnership interest is owned by unrelated parties.

Table of Contents

## Significant Accounting Policies

### Critical Accounting Policies

Our discussion and analysis of financial condition and results of operations is based on our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, and contingencies as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. We evaluate our assumptions and estimates on an ongoing basis. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. These estimates form the basis for making judgments about the carrying values of assets and liabilities where that information is available from other sources. Certain estimates are particularly sensitive due to their significance to the financial statements. Actual results may differ significantly from management s estimates.

We believe that the most significant accounting policies that involve the use of estimates and assumptions as to future uncertainties and, therefore, may result in actual amounts that differ from estimates are the following:

Impairments,

Acquisition of operating properties,

Relative sales method and percentage of completion (Resort Residential Development entities),

Gain recognition on sale of real estate assets,

Consolidation of variable interest entities, and

Allowance for doubtful accounts.

**Impairments.** Real estate, leasehold improvements and intangible assets are classified as long-lived assets held for sale or long-lived assets to be held and used. Assets classified as held and used are evaluated for impairment when events or circumstances indicate that the carrying amount may not be recoverable. When expected undiscounted cash flows are less than the carrying value of a Property and we do not expect to recover our carrying costs, an impairment loss is recognized. For Properties classified as held for use, we reduce carrying costs to fair value. For Properties held for disposition, we reduce carrying costs to the fair value less estimated selling costs in accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. Our estimates of cash flows of the Properties requires us to make assumptions related to future rental rates, occupancies, operating expenses, the ability of our tenants to perform pursuant to their lease obligations and proceeds to be generated from the eventual sale of our Properties. Any changes in estimated future cash flows due to changes in our plans or views of market and economic conditions could result in recognition of additional impairment losses.

Goodwill is reviewed for impairment at least annually, using the fair value based test prescribed by SFAS No. 142, *Goodwill and Other Intangible Assets*. Our impairment review is judgmental and involves the use of significant estimates and assumptions. Estimates of fair value are primarily determined using discounted cash flow methods and are dependent upon assumptions of future sales trends, market conditions, future cash flow and applicable discount rates. A change in these underlying assumptions could cause a change in the results of our analysis and, as such, could cause the fair value to be less than the respective carrying amount. Such an event would result in recognition of impairment losses.

If events or circumstances indicate that the fair value of an investment accounted for using the equity method has declined below its carrying value and we consider the decline to be other than temporary, the investment is written down to fair value and an impairment loss is recognized. The evaluation of impairment for an investment would be based on a number of factors, including financial condition and operating results for the investment, inability to remain in compliance with provisions of any related debt agreements, and recognition of impairments by other investors. Impairment recognition would negatively impact the recorded value of our investment and reduce net income.

**Acquisition of operating properties.** We allocate the purchase price of acquired properties to tangible and identified intangible assets acquired based on their fair values in accordance with SFAS No. 141, *Business Combinations*. We initially record the allocation based on a preliminary purchase price allocation with adjustments recorded during the allocation period, not to exceed one year from the acquisition.

In making estimates of fair value for purposes of allocating purchase price, management utilizes sources, including, but not limited to, independent value consulting services, independent appraisals that may be obtained in connection with financing the respective property, and other market data. Management also considers information obtained about each property as a result of its pre-acquisition due diligence, marketing and leasing activities in estimating the fair value of the tangible and intangible assets acquired.

The aggregate value of the tangible assets acquired is measured based on the sum of (i) the value of the property and (ii) the present value of the unamortized in-place tenant improvement allowances. Management s estimates of the value of the property are made using models similar to those used by independent appraisers. Factors considered by management in its analysis include an estimate of carrying costs such as real estate taxes, insurance, and other operating expenses and estimates of lost rentals during the expected lease-up period assuming current market conditions. The value of the property is then allocated among building, land, site improvements, and equipment. The value of tenant improvements is separately estimated due to the different depreciable lives.

Table of Contents

The aggregate value of intangible assets acquired is measured based on the difference between (i) the purchase price and (ii) the value of the tangible assets acquired as defined above. This value is then allocated among above-market and below-market in-place lease values, costs to execute similar leases (including leasing commissions, legal expenses and other related expenses), in-place lease values and customer relationship values.

Above-market and below-market in-place lease values for acquired properties are calculated based on the present value (using a market interest rate which reflects the risks associated with the leases acquired) of the difference between (i) the contractual amounts to be paid pursuant to the in-place leases and (ii) management s estimate of fair market lease rates for the corresponding in-place leases, measured over a period equal to the remaining non-cancelable term of the lease for above-market leases and the initial term plus the term of the below-market fixed rate renewal option, if any, for below-market leases. We perform this analysis on a lease by lease basis. The capitalized above-market lease values are amortized as a reduction to rental income over the remaining non-cancelable terms of the respective leases. The capitalized below-market lease values are amortized as an increase to rental income over the initial term plus the term of the below-market fixed rate renewal option, if any, of the respective leases.

Management estimates costs to execute leases similar to those acquired at the property at acquisition based on current market conditions. These costs are recorded based on the present value of the amortized in-place leasing costs on a lease by lease basis over the remaining term of each lease.

The in-place lease values and customer relationship values are based on management s evaluation of the specific characteristics of each customer s lease and our overall relationship with that respective customer. Characteristics considered by management in allocating these values include the nature and extent of our existing business relationships with the customer, growth prospects for developing new business with the customer, the customer s credit quality, and the expectation of lease renewals, among other factors. The in-place lease value and customer relationship value are both amortized to expense over the initial term of the respective leases and projected renewal periods, but in no event does the amortization period for the intangible assets exceed the remaining depreciable life of the building.

Should a tenant terminate its lease, the unamortized portion of the costs to execute similar leases, in-place lease value and the customer relationship value and above-market and below-market lease values would be charged to expense.

**Relative sales method and percentage of completion.** We use the accrual method to recognize earnings from the sale of Resort Residential Development Properties after closing has taken place, title has been transferred, sufficient cash has been received to demonstrate the buyer s commitment to pay for the property and collection of the balance of the sales price, if any, is reasonably assured. If a sale does not qualify for the accrual method of recognition, deferral methods are used as appropriate including the percentage-of-completion method. In certain cases, when we receive an inadequate cash down payment and take a promissory note for the balance of the sales price, revenue recognition is deferred until such time as sufficient cash is received to meet minimum down payment requirements. The cost of resort residential property sold is defined based on the type of product being purchased. The cost of sales for resort residential lots is generally determined as a specific percentage of the sales revenues recognized for each Resort Residential Development project. The percentages are based on total estimated development costs and sales revenue for each Resort Residential Development project. These estimates are revised annually and are based on the then-current development strategy and operating assumptions utilizing internally developed projections for product type, revenue and related development costs. The cost of sales for resort residential units (such as townhomes and condominiums) is determined using the relative sales value method. If the resort residential unit has been sold prior to the completion of infrastructure cost, and those uncompleted costs are not significant in relation to total costs, the full accrual method is utilized. Under this method, 100% of the revenue is recognized, and a commitment liability is established to reflect the allocated estimated future costs to complete the resort residential unit. If our estimates of costs or the percentage of completion is incorrect, it could result in either an increase or decrease in cost of sales expense or revenue recognized and therefore, an increase or decrease in net income.

**Gain recognition on sale of real estate assets.** In accordance with SFAS No. 66, *Accounting for Sales of Real Estate,* we perform evaluations of each real estate sale to determine if full gain recognition is appropriate and of each sale or contribution of a property to a joint venture to determine if partial gain recognition is appropriate. The application of SFAS No. 66 can be complex and requires us to make assumptions including an assessment of whether the risks and rewards of ownership have been transferred, the extent of the purchaser s investment in the property being sold, whether our receivables, if any, related to the sale are collectible and are subject to subordination, and the degree of our continuing involvement with the real estate asset after the sale. If full gain recognition is not appropriate, we account for the sale under an appropriate deferral method.

**Consolidation of Variable Interest Entities.** We perform evaluations of each of our investments, investment partnerships, real estate partnerships, mezzanine investments and joint ventures to determine if the associated entities constitute a Variable Interest Entity, or VIE, as defined under Interpretations 46 and 46R, Consolidation of Variable Interest Entities, or FIN 46 and 46R, respectively. In general, a VIE is an entity that has (i) an insufficient amount of equity for the entity to carry on its principal operations, without additional subordinated financial support from other parties, (ii) a group of equity owners that are unable to make decisions about the entity s activities, or (iii) equity that does not absorb the entity s losses or receive the benefits of the entity. If any one of these characteristics is present, the entity is subject to FIN 46R s variable interests consolidation model.

Quantifying the variability of VIEs is complex and subjective, requiring consideration and estimates of a significant number of possible future outcomes as well as the probability of each outcome occurring. The results of each possible outcome are allocated to the parties holding interests in the VIE and based on the allocation, a calculation is performed to determine which party, if any, has a majority of the potential negative outcomes (expected losses) or a majority of the potential positive outcomes (expected residual returns). That party, if any, is the VIE s primary beneficiary and is required to consolidate the VIE. Calculating expected losses and expected residual returns requires modeling potential future results of the entity, assigning probabilities to each potential outcome, and allocating those potential outcomes to the VIE s interest holders. If our estimates of possible outcomes and probabilities are incorrect, it could result in the inappropriate consolidation or deconsolidation of the VIE.

For entities that do not constitute VIE s, we consider other GAAP, as required, determining (i) consolidation of the entity if our ownership interests comprise a majority of its outstanding voting stock or otherwise control the entity, or (ii) application of the equity method of accounting if we do not have direct or indirect control of the entity, with the initial investment carried at cost and subsequently adjusted for our share of net income or loss and cash contributions and distributions to and from these entities. Further, we evaluate, under EITF 04-5, *Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights,* entities for which we have a general partner interest to determine the nature of limited partners rights in assessing whether those rights overcome the presumption that we control the limited partnership entity.

**Allowance for doubtful accounts/credit losses.** Our accounts receivable balance is reduced by an allowance for amounts that may become uncollectible in the future. Our receivable balance is composed primarily of rents and operating cost recoveries due from tenants, receivables associated with club memberships at our Resort Residential Development properties and guest receivables at our Resort/Hotel properties. We also maintain an allowance for deferred rent receivables which arise from the straight-lining of rents. The allowance for doubtful accounts is reviewed at least quarterly for adequacy by reviewing such factors as the credit quality of our tenants or members, any delinquency in payment, historical trends and current economic conditions. If the assumptions regarding the collectibility of accounts receivable prove incorrect, we could experience write-offs in excess of allowance for doubtful accounts, which would result in a decrease in net income.

Mezzanine notes are reviewed for potential impairment at each balance sheet date. A mezzanine note is considered impaired when it becomes probable, based on current information, that we will be unable to collect all amounts due according to the mezzanine note contractual terms. The amount of impairment, if any, is measured by comparing the recorded amount of the mezzanine note to the present value of the expected cash flows or the fair value of the collateral. If a mezzanine note was deemed to be impaired, we would record a reserve for loan losses through a charge to income for any shortfall. To date, no such impairment charges have been recognized.

**Impact of New Accounting Standards**

**SFAS No. 123R.** In December 2004, the Financial Accounting Standards Board, or FASB, issued Statement of Financial Accounting Standards, or SFAS, No. 123R (Revised 2004), *Share-Based Payment*. The new FASB rule requires that the compensation cost relating to share-based payment transactions be recognized in financial statements. That cost will be measured based on the fair value of the equity or liability instruments issued. We were required to apply SFAS No. 123R beginning January 1, 2006. The scope of SFAS No. 123R includes a wide range of share-based compensation arrangements including share options, restricted share plans, performance-based awards, share appreciation rights, and employee share purchase plans. SFAS No. 123R replaces SFAS No. 123, *Accounting for*

*Stock-Based Compensation*, and supersedes Accounting Principles Board, or APB, Opinion No. 25, *Accounting for Stock Issued to Employees*. SFAS No. 123, as originally issued in 1995, established as preferable a fair-value-based method of accounting for share-based payment transactions with employees. However, that statement permitted entities the option of continuing to apply the guidance in Opinion No. 25, as long as the footnotes to the financial statements disclosed what net income would have been had the preferable fair-value-based method been used. Effective January 1, 2003, we adopted the fair value expense recognition provisions of SFAS No. 123 on a prospective basis. We adopted SFAS No. 123R using the modified prospective application method which requires, among other things, that we recognize compensation cost for all awards outstanding at January 1, 2006, for which the requisite service has not yet been rendered. Additionally, our prior interim periods and fiscal years do not reflect any restated amounts due to the adoption of SFAS No. 123R. We estimate an additional

$0.2 million of expense will be recorded for the year ended December 31, 2007, for stock and unit options due to the adoption of SFAS No. 123R.

**EITF 04-5.** In June 2005, the EITF ratified the consensus in Issue No. 04-5, *Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights* (EITF 04-5), which states that the general partner in a limited partnership is presumed to control that limited partnership. This presumption may be overcome if the limited partners have either (1) the substantive ability to dissolve the limited partnership or otherwise remove the general partner without cause or (2) substantive participating rights, which provide the limited partners with the ability to effectively participate in significant decisions that would be expected to be made in the ordinary course of business and thereby preclude the general partner from exercising unilateral control over the partnership. EITF 04-5 is effective June 30, 2005 for new or modified limited partnership arrangements and effective January 1, 2006 for existing limited partnership arrangements. There was no impact to our financial condition or results of operations from the adoption of EITF 04-5.

**EITF 06-3.** At its June 2006 meeting, the EITF ratified the consensus regarding Issue No. 06-3 (EITF 06-3), *How Taxes Collected from Customers and Remitted to Governmental Authorities Should be Presented in the Income Statement (That Is, Gross versus Net Presentation)*. EITF 06-3 is effective for interim and annual periods beginning after December 15, 2006, with earlier application permitted. The scope of EITF 06-3 includes any tax assessed by a governmental authority that is both imposed on and concurrent with a specific revenue-producing transaction between a seller and a customer, and may include, but is not limited to, sales, use, value added, and certain excise taxes. The consensus indicates that gross vs. net income statement classification of those taxes within its scope is an accounting policy decision. In addition, for taxes within its scope, the consensus requires the following disclosures: the accounting policy elected for these taxes and the amounts of the taxes reflected gross (as revenue) in the income statement on an interim and annual basis. We do not believe there will be an impact to our financial condition or results of operations from the adoption of EITF 06-3.

**FASB Interpretation 48.** In July 2006, the FASB issued Interpretation 48, *Accounting for Uncertainty in Income Taxes An Interpretation of FASB Statement No. 109,* (FIN 48), which clarifies the accounting for uncertainty in income taxes recognized in a company s financial statements in accordance with SFAS No. 109, *Accounting for Income Taxes.* FIN 48 also prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The standard also provides guidance on derecognizing, classification, interest and penalties, accounting in interim periods, disclosure, and transition. The provisions of FIN 48 are effective for fiscal years beginning after December 15, 2006, and are to be applied to all tax positions upon initial adoption of this standard. Only tax positions that meet a more-likely-than-not recognition threshold at the effective date may be recognized or continue to be recognized upon adoption of FIN 48. We expect to record less than $1.0 million as a cumulative effect adjustment to beginning Accumulated Deficit as of January 1, 2007 from the adoption of FIN 48.

**SFAS No. 157.** In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*. The new FASB rule defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, or GAAP, and expands disclosures about fair value measurements. The statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We are currently evaluating the impact, if any, to our financial condition or results of operations from the adoption of SFAS No. 157.

**SAB No. 108.** In September 2006, the Securities and Exchange Commission, or SEC, issued Staff Accounting Bulletin No. 108, *Financial Statements Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements*, (SAB 108), which is effective for fiscal years ending after November 15, 2006. SAB No. 108 provides guidance on the consideration of the effects of prior year misstatements in quantifying current year misstatements. The adoption of SAB No. 108 did not have an impact to our financial condition or results of operations.

**EITF 06-8.** At its November 2006 meeting, the EITF ratified the consensus regarding Issue No. 06-8 (EITF 06-8), *Applicability of the Assessment of a Buyer s Continuing Investment under FASB Statement No. 66 for Sales Of Condominiums*. EITF 06-8 is effective for annual periods beginning after March 15, 2007. The scope of EITF 06-8 is limited to the sale of individual units in a condominium project and requires an entity to evaluate the adequacy of the buyer s initial and continuing investment for purposes of determining whether the sales price is collectible as required to recognize profit using the percentage-of-completion method under paragraph 37 of Statement 66. If the buyer does not meet the initial and continuing investment criteria, the guidance requires use of the deposit method to recognize profit. We do not believe there will be an impact to our financial condition or results of operations from the adoption of EITF 06-8.

Table of Contents

## Funds from Operations

FFO, as used in this document, means:

- Net Income (Loss) determined in accordance with GAAP;
- excluding gains (or losses) from sales of depreciable operating property;
- excluding extraordinary items (as defined by GAAP);
- plus depreciation and amortization of real estate assets; and
- after adjustments for unconsolidated partnerships and joint ventures.

We calculate FFO available to common shareholders diluted in this manner, except that Net Income (Loss) is replaced by Net Income (Loss) Available to Common Shareholders and we include the effect of operating partnership unitholder minority interests.

The National Association of Real Estate Investment Trusts, or NAREIT, developed FFO as a relative measure of performance and liquidity of an equity REIT to recognize that income-producing real estate historically has not depreciated on the basis determined under GAAP. We consider FFO available to common shareholders diluted and FFO appropriate measures of performance for an equity REIT and for its investment segments. However, FFO available to common shareholders diluted and FFO should not be considered an alternative to net income determined in accordance with GAAP as an indication of our operating performance.

Accordingly, we believe that to facilitate a clear understanding of our consolidated historical operating results, FFO available to common shareholders diluted should be considered in conjunction with our net income and cash flows reported in the consolidated financial statements and notes to the financial statements. However, our measure of FFO available to common shareholders diluted may not be comparable to similarly titled measures of other REITs because these REITs may apply the definition of FFO in a different manner than we apply it.

## Consolidated Statements of Funds from Operations

| | For the years ended December 31, 2006 | 2005 |
|---|---|---|
| (dollars in thousands) | | (Restated) |
| Net income | $ 33,433 | $ 101,585 |
| Adjustments to reconcile net income to funds from operations available to common shareholders diluted: | | |
| Depreciation and amortization of real estate assets | 132,139 | 131,392 |
| Gain on property sales | (28,847) | (102,803) |
| Gain from sale of development operating property | (16,221) | (13,369) |
| Gain from promoted interest | (22,575) | (13,579) |
| Adjustment for investments in unconsolidated companies: | | |
| Office Properties | 21,217 | 18,872 |
| Resort Residential Development Properties | (10,616) | (5,543) |
| Resort/Hotel Properties | 4,773 | 3,881 |
| Temperature-Controlled Logistics Properties | 17,917 | 18,210 |
| Unitholder minority interest | 266 | 12,379 |
| Series A Preferred Share distributions | (23,963) | (23,963) |
| Series B Preferred Share distributions | (8,075) | (8,075) |
| Funds from operations available to common shareholders diluted[(1) (2)] | $ 99,448 | $ 118,987 |
| Investment Segments: | | |
| Office Properties | $ 231,248 | $ 209,715 |
| Resort Residential Development Properties | 12,422 | 45,486 |
| Resort/Hotel Properties | 36,150 | 34,440 |
| Temperature-Controlled Logistics Properties | 2,249 | 18,444 |
| Other: | | |
| Corporate general and administrative | (44,918) | (50,363) |
| Interest expense | (135,457) | (136,664) |
| Series A Preferred Share distributions | (23,963) | (23,963) |
| Series B Preferred Share distributions | (8,075) | (8,075) |
| Income from mezzanine loans and other loans | 29,674 | 10,618 |
| Other[(3)] | 118 | 19,349 |
| Funds from operations available to common shareholders diluted[(1) (2)] | $ 99,448 | $ 118,987 |
| Basic weighted average shares outstanding | 102,055 | 100,179 |
| Diluted weighted average shares and units outstanding[(4)] | 122,980 | 118,836 |

(1) To calculate basic funds from operations available to

common shareholders, deduct unitholder minority interest.

(2) In addition to presenting FFO in accordance with the NAREIT definition, we also disclose FFO available to common shareholders as adjusted, which includes adjustments to exclude extinguishment of debt and impairment charges related to real estate assets and include the impact of gain on sale of developed properties and promoted interest. We provide this additional information because management utilizes it, in addition to FFO available to common shareholders diluted, in making operating decisions and assessing performance, and because we

believe that it also is useful to investors in assessing our operating performance.

| (dollars in thousands) | For the years ended December 31, 2006 | 2005 |
|---|---|---|
| FFO available to common shareholders diluted NAREIT | $ 99,448 | $ 118,987 |
| Debt extinguishment charges related to the sale of real estate assets | | 729 |
| Impairment charges related to real estate assets | 125 | 1,047 |
| Promoted interests related to the sale of investment in unconsolidated companies | 22,575 | 13,579 |
| Gain from sale of development operating property | 16,221 | 13,369 |
| FFO available to common shareholders diluted as adjusted | $ 138,369 | $ 147,711 |

(3) Includes income from investment land sales, interest and other income, extinguishment of debt, income/loss from other unconsolidated companies, other expenses, depreciation and amortization of non-real estate assets, and amortization of deferred financing costs.

(4) See calculations for the amounts presented in the reconciliation following this table.

Table of Contents

The following schedule reconciles our basic weighted average shares to the diluted weighted average shares/units in share equivalents presented above:

| (shares/units in share equivalents in thousands) | For the years ended December 31, 2006 | 2005 |
|---|---|---|
| Basic weighted average shares: | 102,055 | 100,179 |
| Add: Weighted average units in share equivalents | 19,461 | 17,833 |
| Restricted shares and share and unit options in share equivalents | 1,464 | 824 |
| Diluted weighted average shares and units | 122,980 | 118,836 |

The following table reconciles the As Previously Reported to the As Restated Consolidated Statement of Funds from Operations for the year ended December 31, 2005. This table reflects the impact of the restated financial data discussed in Item 8., Financial Statements and Supplementary Data, Note 1, Organization and Basis of Presentation, associated with the Calculation of Minority Interest, the Redeemable Fees for Club Member Services and the Classification of Club Membership Intangible Asset matters.

**Consolidated Statement of Funds from Operations**

| | For the year ended December 31, 2005 | | | | |
|---|---|---|---|---|---|
| (in thousands) | As Previously Reported | Discontinued Operations | As Reported with Discontinued Operations | Restatement Adjustments | As Restated |
| Net income | $ 95,307 | $ | $ 95,307 | $ 6,278 | $ 101,585 |
| Adjustments to reconcile net income to funds from operations available to common shareholders diluted: | | | | | |
| Depreciation and amortization of real estate assets | 131,392 | | 131,392 | | 131,392 |
| Gain on property sales | (102,803) | | (102,803) | | (102,803) |
| Gain from sale of development operating property | (13,369) | | (13,369) | | (13,369) |
| Gain from promoted interest | (13,579) | | (13,579) | | (13,579) |
| Office Properties | 18,872 | | 18,872 | | 18,872 |
| Resort Residential Development Properties | (5,468) | | (5,468) | (75) | (5,543) |
| Resort/Hotel Properties | 3,881 | | 3,881 | | 3,881 |
| Temperature-Controlled Logistics Properties | 18,210 | | 18,210 | | 18,210 |
| Unitholder minority interest | 16,964 | | 16,964 | (4,585) | 12,379 |
| Series A Preferred Share distributions | (23,963) | | (23,963) | | (23,963) |
| Series B Preferred Share distributions | (8,075) | | (8,075) | | (8,075) |
| Funds from operations available to common shareholders diluted | $ 117,369(1) | $ | $ 117,369 | $ 1,618 | $ 118,987 |
| Investment Segments: | | | | | |
| Office Properties | $ 209,715 | $ | $ 209,715 | $ | $ 209,715 |

| | | | | |
|---|---|---|---|---|
| Resort Residential Development Properties | 43,868 | 43,868 | 1,618 | 45,486 |
| Resort/Hotel Properties | 34,440 | 34,440 | | 34,440 |
| Temperature-Controlled Logistics Properties | 18,444 | 18,444 | | 18,444 |
| Other: | | | | |
| Corporate general and administrative | (50,363) | (50,363) | | (50,363) |
| Interest expense | (136,664) | (136,664) | | (136,664) |
| Series A Preferred Share distributions | (23,963) | (23,963) | | (23,963) |
| Series B Preferred Share distributions | (8,075) | (8,075) | | (8,075) |
| Income from mezzanine loans and other loans | 10,618 | 10,618 | | 10,618 |
| Other[3] | 19,349 | 19,349 | | 19,349 |
| Funds from operations available to common shareholders diluted | $ 117,369[1] $ | $ 117,369 | $ 1,618 | $ 118,987 |
| Basic weighted average shares outstanding | 100,179 | 100,179 | | 100,179 |
| Diluted weighted average shares and units outstanding | 118,836 | 118,836 | | 118,836 |

(1) Amount represents FFO available to common shareholders presented in accordance with the NAREIT definition. The 2005 Form 10-K amount reported of $144,317 represented FFO, as adjusted, and included $26,948 gain on sale of developed property (inclusive of $13,579 promoted interest).

Table of Contents

## Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Our use of financial instruments, such as debt instruments and mezzanine notes receivable, subjects us to market risk which may affect our future earnings and cash flows as well as the fair value of its assets. Market risk generally refers to the risk of loss from changes in interest rates and market prices. We manage our market risk by attempting to match anticipated inflow of cash from our operating, investing and financing activities with anticipated outflow of cash to fund debt payments, distributions to shareholders, investments, capital expenditures and other cash requirements. We also enter into derivative financial instruments such as interest rate swaps to mitigate our interest rate risk on a related financial instrument or to effectively lock the interest rate on a portion of our variable rate debt.

The following discussion of market risk is based solely on hypothetical changes in interest rates related to our variable rate debt and variable rate mezzanine notes receivable. This discussion does not purport to take into account all of the factors that may affect the financial instruments discussed in this section.

### Interest Rate Risk

### Debt

Our interest rate risk is most sensitive to fluctuations in interest rates on our short-term variable rate debt. We had total outstanding debt of approximately $2.3 billion at December 31, 2006, of which approximately $479.6 million, or approximately 21%, was unhedged variable rate debt. The variable rate debt is based on an index (LIBOR or Prime) plus a credit spread. The weighted average interest rate on such unhedged variable rate debt was 7.3% as of December 31, 2006. A 10% increase in the underlying index would cause an increase of 62.1 basis points to the weighted average interest rate on such variable rate debt, which would result in an annual decrease in net income and cash flows of approximately $3.0 million. Conversely, a 10% decrease in the underlying index would cause a decrease of 62.1 basis points to the weighted average interest rate on such unhedged variable rate debt, which would result in an annual increase in net income and cash flows of approximately $3.0 million based on the unhedged variable rate debt outstanding as of December 31, 2006.

### Mezzanine Notes

Our mezzanine notes receivable are sensitive to fluctuations in interest rates on our variable loans. We had total outstanding mezzanine loans of approximately $124.3 million at December 31, 2006, of which approximately $106.8 million, or approximately 86%, were variable rate loans. The variable rate is based on an index (LIBOR) plus a credit spread. The weighted average interest rate on such variable rate loans was 14.0% as of December 31, 2006. A 10% increase in the underlying index would cause an increase of 53.6 basis points to the weighted average interest rate on such variable rate loans, which would result in an annual increase in net income and cash flows of approximately $0.6 million. Conversely, a 10% decrease in the underlying index would cause a decrease of 53.6 basis points to the weighted average interest rate on such variable rate loans, which would result in an annual decrease in net income and cash flows of approximately $0.6 million based on the variable rate loans outstanding as of December 31, 2006.

### Cash Flow Hedges

We use derivative financial instruments to convert a portion of our variable rate debt to fixed rate debt and to manage the fixed to variable rate debt ratio. As of December 31, 2006, total variable rate debt was $767.2 million, of which $287.6 million was hedged. A description of these derivative financial instruments is contained in Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Equity and Debt Financing Derivative Instruments and Hedging Activities.

Table of Contents

**Item 8. Financial Statements and Supplementary Data**

**INDEX TO CONSOLIDATED FINANCIAL STATEMENTS**

**Table of Contents**

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

Board of Trust Managers and Shareholders of
Crescent Real Estate Equities Company

We have audited the accompanying consolidated balance sheets of Crescent Real Estate Equities Company (the Company ) as of December 31, 2006 and 2005, and the related consolidated statements of operations, shareholders equity, and cash flows for each of the three years in the period ended December 31, 2006. Our audits also included the financial statement schedules listed in the Index at Item 15(a). These financial statements and schedules are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements and schedules based on our audits. The financial statements of AmeriCold Realty Trust (AmeriCold), a corporation in which the Company has a 31.7% interest for 2006, have been audited by other auditors whose report has been furnished to us, and our opinion on the consolidated financial statements, insofar as it relates to the amounts included for AmeriCold, is based solely on the report of the other auditors. In the consolidated financial statements, the Company s investment in AmeriCold is stated at $87,069,000 at December 31, 2006, and the Company s equity in the net loss of AmeriCold is stated at $15,669,000 for the year then ended.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the report of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and, for 2006, the report of other auditors, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Crescent Real Estate Equities Company at December 31, 2006 and 2005, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2006, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedules, when considered in relation to the basic financial statements taken as a whole, present fairly, in all material respects, the information set forth therein.

As discussed in Note 1 to the consolidated financial statements, the 2005 and 2004 consolidated financial statements have been restated to correct errors in recording minority interests, membership deposits and intangible assets, including the related tax impact. Additionally, as discussed in Note 2 to the consolidated financial statements, in 2006 the Company changed its method of accounting for stock-based compensation.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Crescent Real Estate Equities Company s internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 13, 2007, expressed an unqualified opinion on management s assessment and an adverse opinion on the effectiveness of internal control over financial reporting.

ERNST & YOUNG LLP
Dallas, Texas
March 13, 2007

**CRESCENT REAL ESTATE EQUITIES COMPANY**
**CONSOLIDATED BALANCE SHEETS**
**(dollars in thousands)**

| | December 31, 2006 | December 31, 2005 (As Restated See Note 1) |
|---|---|---|
| ASSETS: | | |
| Investments in real estate: | | |
| Land | $ 186,779 | $ 183,228 |
| Land improvements, net of accumulated depreciation of $36,421 and $29,784 at December 31, 2006 and 2005, respectively | 70,630 | 70,494 |
| Buildings and improvements, net of accumulated depreciation of $533,311 and $456,628 at December 31, 2006 and 2005, respectively | 1,851,770 | 1,734,131 |
| Furniture, fixtures and equipment, net of accumulated depreciation of $39,118 and $34,129 at December 31, 2006 and 2005, respectively | 43,270 | 37,018 |
| Land held for investment or development | 750,970 | 513,040 |
| Properties held for disposition, net | 2,400 | 118,205 |
| Net investment in real estate | $ 2,905,819 | $ 2,656,116 |
| Cash and cash equivalents | 77,550 | 86,228 |
| Restricted cash and cash equivalents | 93,471 | 84,699 |
| Defeasance investments | 111,014 | 274,134 |
| Accounts receivable, net | 63,996 | 56,356 |
| Deferred rent receivable | 61,096 | 70,074 |
| Investments in unconsolidated companies | 280,870 | 393,535 |
| Notes receivable, net | 174,867 | 219,016 |
| Income tax asset current and deferred, net | 3,274 | 10,732 |
| Other assets, net | 275,014 | 312,366 |
| Total assets | $ 4,046,971 | $ 4,163,256 |
| LIABILITIES: | | |
| Borrowings under Credit Facility | $ 118,000 | $ 234,000 |
| Notes payable | 2,101,037 | 1,933,546 |
| Notes payable, accounts payable, accrued expenses and other liabilities, properties held for disposition | | 19,306 |
| Junior subordinated notes | 77,321 | 77,321 |
| Accounts payable, accrued expenses and other liabilities | 502,014 | 495,918 |
| Current tax liability | 610 | |
| Total liabilities | $ 2,798,982 | $ 2,760,091 |
| COMMITMENTS AND CONTINGENCIES | | |
| MINORITY INTERESTS: | | |
| Operating partnership, 11,320,798 and 11,416,173 units, at December 31, 2006 and 2005, respectively | $ 75,865 | $ 98,659 |

| | | | | |
|---|---|---|---|---|
| Consolidated real estate partnerships | | 49,838 | | 52,880 |
| Total minority interests | $ | 125,703 | $ | 151,539 |
| SHAREHOLDERS EQUITY: | | | | |
| Preferred shares, $0.01 par value, authorized 100,000,000 shares: | | | | |
| Series A Convertible Redeemable Cumulative Preferred Shares, liquidation preference of $25.00 per share, 14,200,000 shares issued and outstanding at December 31, 2006 and 2005 respectively | $ | 319,166 | $ | 319,166 |
| Series B Cumulative Redeemable Preferred Shares, liquidation preference of $25.00 per share, 3,400,000 shares issued and outstanding at December 31, 2006 and 2005 | | 81,923 | | 81,923 |
| Common shares, $0.01 par value, authorized 250,000,000 shares, 127,875,571 and 126,562,980 shares issued and 102,754,654 and 101,442,063 shares outstanding at December 31, 2006 and 2005, respectively | | 1,279 | | 1,266 |
| Additional paid-in capital | | 2,294,827 | | 2,271,888 |
| Deferred compensation on restricted shares | | | | (1,182) |
| Accumulated deficit | | (1,114,553) | | (962,688) |
| Accumulated other comprehensive (loss) income | | (224) | | 1,385 |
| | $ | 1,582,418 | $ | 1,711,758 |
| Less shares held in treasury, at cost, 25,120,917 common shares at December 31, 2006 and 2005 | | (460,132) | | (460,132) |
| Total shareholders equity | $ | 1,122,286 | $ | 1,251,626 |
| Total liabilities and shareholders equity | $ | 4,046,971 | $ | 4,163,256 |

The accompanying notes are an integral part of these consolidated financial statements.

75

Table of Contents

**CRESCENT REAL ESTATE EQUITIES COMPANY**
**CONSOLIDATED STATEMENTS OF OPERATIONS**
**(dollars in thousands, except per share data)**

| | For the Years Ended December 31, 2006 | 2005 | 2004 |
|---|---|---|---|
| | | (As Restated see Note 1) | |
| REVENUE: | | | |
| Office Property | $ 414,343 | $ 372,759 | $ 475,797 |
| Resort Residential Development Property | 372,148 | 502,723 | 309,945 |
| Resort/Hotel Property | 142,205 | 142,618 | 214,531 |
| Total Property Revenue | $ 928,696 | $ 1,018,100 | $ 1,000,273 |
| EXPENSE: | | | |
| Office Property real estate taxes | $ 41,674 | $ 38,062 | $ 57,393 |
| Office Property operating expenses | 164,965 | 157,719 | 176,768 |
| Resort Residential Development Property expense | 342,994 | 432,203 | 271,310 |
| Resort/Hotel Property expense | 108,391 | 111,277 | 179,825 |
| Total Property Expense | $ 658,024 | $ 739,261 | $ 685,296 |
| Income from Property Operations | $ 270,672 | $ 278,839 | $ 314,977 |
| OTHER INCOME (EXPENSE): | | | |
| Income from sale of investment in unconsolidated company | $ 47,709 | $ 29,934 | $ |
| Income from investment land sales | | 8,622 | 18,879 |
| (Loss) gain on joint venture of properties | | (2,743) | 265,772 |
| Interest and other income | 47,428 | 29,250 | 18,005 |
| Corporate general and administrative | (44,918) | (50,363) | (38,889) |
| Interest expense | (134,273) | (136,664) | (176,771) |
| Amortization of deferred financing costs | (7,605) | (8,108) | (13,056) |
| Extinguishment of debt | | (2,161) | (42,608) |
| Depreciation and amortization | (147,407) | (141,366) | (159,898) |
| Impairment charges related to real estate assets | | | (4,094) |
| Other expenses | (12,997) | (3,964) | (725) |
| Equity in net income (loss) of unconsolidated companies: | | | |
| Office Properties | 9,231 | 11,464 | 6,262 |
| Resort Residential Development Properties | (355) | (491) | (2,266) |
| Resort/Hotel Properties | (5,109) | (1,541) | (245) |
| Temperature-Controlled Logistics Properties | (15,669) | 234 | 6,153 |
| Other | 12,157 | 17,885 | (280) |
| Total other income (expense) | $ (251,808) | $ (250,012) | $ (123,761) |
| INCOME FROM CONTINUING OPERATIONS BEFORE MINORITY INTERESTS AND INCOME TAXES | $ 18,864 | $ 28,827 | $ 191,216 |
| Minority interests | (2,661) | (11,067) | (32,706) |

| | | | |
|---|---|---|---|
| Income tax benefit (expense) | 3,475 | (8,462) | 12,231 |
| INCOME BEFORE DISCONTINUED OPERATIONS AND CUMULATIVE EFFECT OF A CHANGE IN ACCOUNTING PRINCIPLE | $ 19,678 | $ 9,298 | $ 170,741 |
| (Loss) income from discontinued operations, net of minority interests and taxes | (502) | 4,006 | 10,407 |
| Impairment charges related to real estate assets from discontinued operations, net of minority interests | (105) | (953) | (2,978) |
| Gain on sale of real estate from discontinued operations, net of minority interest and taxes | 14,362 | 89,234 | 1,052 |
| Cumulative effect of a change in accounting principle, net of minority interests | | | (363) |
| NET INCOME | $ 33,433 | $ 101,585 | $ 178,859 |
| Series A Preferred Share distributions | (23,963) | (23,963) | (23,723) |
| Series B Preferred Share distributions | (8,075) | (8,075) | (8,075) |
| NET INCOME AVAILABLE TO COMMON SHAREHOLDERS | $ 1,395 | $ 69,547 | $ 147,061 |
| BASIC EARNINGS PER SHARE DATA: | | | |
| (Loss) income available to common shareholders before discontinued operations and cumulative effect of a change in accounting principle | $ (0.12) | $ (0.23) | $ 1.40 |
| (Loss) Income from discontinued operations, net of minority interests and taxes | (0.01) | 0.04 | 0.11 |
| Impairment charges related to real estate assets from discontinued operations, net of minority interests | | (0.01) | (0.03) |
| Gain on sale of real estate from discontinued operations, net of minority interests and taxes | 0.14 | 0.89 | 0.01 |
| Cumulative effect of a change in accounting principle, net of minority interests | | | |
| Net income available to common shareholders basic | $ 0.01 | $ 0.69 | $ 1.49 |
| DILUTED EARNINGS PER SHARE DATA: | | | |
| (Loss) income available to common shareholders before discontinued operations and cumulative effect of a change in accounting principle | $ (0.12) | $ (0.23) | $ 1.40 |
| (Loss) Income from discontinued operations, net of minority interests and taxes | (0.01) | 0.04 | 0.10 |
| Impairment charges related to real estate assets from discontinued operations, net of minority interests | | (0.01) | (0.03) |
| Gain on sale of real estate from discontinued operations, net of minority interests and taxes | 0.14 | 0.89 | 0.01 |
| Cumulative effect of a change in accounting principle, net of minority interests | | | |

| | | | | | | |
|---|---|---|---|---|---|---|
| Net income available to common shareholders diluted | $ | 0.01 | $ | 0.69 | $ | 1.48 |

The accompanying notes are an integral part of these consolidated financial statements.

**Table of Contents**

**CRESCENT REAL ESTATE EQUITIES COMPANY**
**CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY**
**(dollars in thousands, except share data)**

| Series A Preferred Shares | | Series B Preferred Shares | | Treasury Shares | | Common Shares | | Additional Paid-in | Deferred Compensation on Restricted | Accumulated | Acc Com |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Shares | Net Value | Shares | Net Value | Shares | Net Value | Shares | Par Value | Capital | Shares | (Deficit) | I |
| 0,800,000 | $ 248,160 | 3,400,000 | $ 81,923 | 25,121,861 | $ (460,148) | 124,396,168 | $ 1,237 | $ 2,245,683 | $ (4,102) | $ (877,120) | $ |
| | | | | | | | | | | (2,570) | |
| 0,800,000 | $ 248,160 | 3,400,000 | $ 81,923 | 25,121,861 | $ (460,148) | 124,396,168 | $ 1,237 | $ 2,245,683 | $ (4,102) | $ (879,690) | $ |
| | | | | | | | | | | 178,859 | |