

UNITED STATE
SECURITIES EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2001

or

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

For the transition period from _____ to _____

Commission File Number 1-10709

PS BUSINESS PARKS, INC.

(Exact name of registrant as specified in its charter)

California

(State or Other Jurisdiction
of Incorporation)

95-4300881

(I.R.S. Employer
Identification Number)

701 Western Avenue, Glendale, California 91201-2397

(Address of principal executive offices) (Zip Code)

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes X No _____

Number of shares outstanding of each of the issuer's classes of common stock, as of November 13, 2001:

Common Stock, \$0.01 par value, 21,527,967 shares outstanding

PS BUSINESS PARKS, INC.

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PS BUSINESS PARKS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

	September 30, 2001 (unaudited)	December 31, 2000
<u>ASSETS</u>		
Cash and cash equivalents.....	\$ 66,291,000	\$ 49,295,000
Marketable securities	8,657,000	6,065,000
Real estate facilities, at cost:		
Land	240,635,000	214,020,000
Buildings and equipment	805,415,000	709,328,000
	1,046,050,000	923,348,000
Accumulated depreciation.....	(113,224,000)	(83,841,000)
	932,826,000	839,507,000
Property held for disposition, net	3,343,000	-
Land held for development	5,829,000	5,737,000
Construction in progress.....	-	19,467,000
	941,998,000	864,711,000
Receivables	514,000	461,000
Deferred rent receivables	8,868,000	7,697,000
Intangible assets, net	755,000	981,000
Other assets	1,422,000	1,546,000
Total assets	\$1,028,505,000	\$ 930,756,000
<u>LIABILITIES AND SHAREHOLDERS' EQUITY</u>		
Accrued and other liabilities	\$ 35,202,000	\$ 28,964,000
Mortgage notes payable	30,354,000	30,971,000
Total liabilities	65,556,000	59,935,000
Minority interest:		
Preferred units.....	197,750,000	144,750,000
Common units.....	162,338,000	161,728,000
Shareholders' equity:		
Preferred stock, \$0.01 par value, 50,000,000 shares authorized, 4,840 shares issued and outstanding at September 30, 2001 (2,200 shares issued and outstanding at December 31, 2000)	121,000,000	55,000,000
Common stock, \$0.01 par value, 100,000,000 shares authorized, 21,704,067 shares issued and outstanding at September 30, 2001 (23,044,635 shares issued and outstanding at December 31, 2000)	217,000	230,000
Paid-in capital.....	426,546,000	464,855,000
Cumulative net income.....	162,134,000	124,990,000
Other comprehensive loss.....	(740,000)	-
Cumulative distributions.....	(106,296,000)	(80,732,000)
Total shareholders' equity.....	602,861,000	564,343,000
Total liabilities and shareholders' equity.....	\$1,028,505,000	\$ 930,756,000

See accompanying notes.

PS BUSINESS PARKS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2001	2000	2001	2000
Revenues:				
Rental income	\$ 43,290,000	\$ 36,798,000	\$121,964,000	\$107,265,000
Facility management fees primarily from affiliates	170,000	131,000	499,000	383,000
Business services	75,000	82,000	308,000	349,000
Interest income.....	346,000	1,035,000	1,659,000	3,046,000
Dividend income.....	4,000	439,000	12,000	1,297,000
	<u>43,885,000</u>	<u>38,485,000</u>	<u>124,442,000</u>	<u>112,340,000</u>
Expenses:				
Cost of operations.....	12,006,000	9,762,000	32,852,000	29,432,000
Cost of facility management.....	38,000	27,000	111,000	77,000
Cost of business services.....	147,000	78,000	460,000	142,000
Depreciation and amortization	10,679,000	9,449,000	30,058,000	26,723,000
General and administrative.....	1,037,000	995,000	3,157,000	2,859,000
Interest expense.....	538,000	502,000	932,000	1,246,000
	<u>24,445,000</u>	<u>20,813,000</u>	<u>67,570,000</u>	<u>60,479,000</u>
Income before gain on investment and minority interest	19,440,000	17,672,000	56,872,000	51,861,000
Gain on disposition of real estate	-	159,000	-	256,000
Gain on investment in Pacific Gulf Properties Inc.	-	-	15,000	-
Income before minority interest.....	<u>19,440,000</u>	<u>17,831,000</u>	<u>56,887,000</u>	<u>52,117,000</u>
Minority interest in income – preferred units ...	(3,323,000)	(3,157,000)	(9,696,000)	(8,998,000)
Minority interest in income – common units....	(3,268,000)	(3,203,000)	(10,047,000)	(9,393,000)
	<u>(6,591,000)</u>	<u>(6,360,000)</u>	<u>(19,743,000)</u>	<u>(18,391,000)</u>
Net income.....	<u>\$ 12,849,000</u>	<u>\$ 11,471,000</u>	<u>\$ 37,144,000</u>	<u>\$ 33,726,000</u>
Net income allocation:				
Allocable to preferred shareholders.....	\$ 2,839,000	\$ 1,272,000	\$ 6,014,000	\$ 3,816,000
Allocable to common shareholders	10,010,000	10,199,000	31,130,000	29,910,000
	<u>\$ 12,849,000</u>	<u>\$ 11,471,000</u>	<u>\$ 37,144,000</u>	<u>\$ 33,726,000</u>
Net income per common share:				
Basic.....	<u>\$ 0.45</u>	<u>\$ 0.44</u>	<u>\$ 1.38</u>	<u>\$ 1.28</u>
Diluted.....	<u>\$ 0.45</u>	<u>\$ 0.44</u>	<u>\$ 1.37</u>	<u>\$ 1.28</u>
Weighted average common shares outstanding:				
Basic.....	<u>22,210,000</u>	<u>23,117,000</u>	<u>22,610,000</u>	<u>23,354,000</u>
Diluted.....	<u>22,295,000</u>	<u>23,216,000</u>	<u>22,685,000</u>	<u>23,426,000</u>

See accompanying notes.

PS BUSINESS PARKS, INC.
CONDENSED CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2001
(Unaudited)

	Preferred Stock		Common Stock		Paid-in Capital
	Shares	Amount	Shares	Amount	
Balances at December 31, 2000	2,200	\$55,000,000	23,044,635	\$ 230,000	\$464,855,000
Issuance of preferred stock.....	2,640	66,000,000	-	-	(1,663,000)
Exercise of stock options.....	-	-	82,443	1,000	1,397,000
Unrealized loss – depreciation in marketable securities	-	-	-	-	-
Repurchase of common stock	-	-	(1,423,011)	(14,000)	(38,961,000)
Net income	-	-	-	-	-
Distributions paid:					
Preferred stock	-	-	-	-	-
Common stock	-	-	-	-	-
Adjustment to reflect minority interest to underlying ownership interest	-	-	-	-	918,000
Balances at September 30, 2001	<u>4,840</u>	<u>\$121,000,000</u>	<u>21,704,067</u>	<u>\$ 217,000</u>	<u>\$426,546,000</u>

	Cumulative	Other	Cumulative	Shareholders'
	Net Income	Comprehensive Loss	Distributions	Equity
Balances at December 31, 2000	\$124,990,000	-	\$ (80,732,000)	\$ 564,343,000
Issuance of preferred stock.....	-	-	-	64,337,000
Exercise of stock options.....	-	-	-	1,398,000
Unrealized loss – depreciation in marketable securities	-	(740,000)	-	(740,000)
Repurchase of common stock	-	-	-	(38,975,000)
Net income	37,144,000	-	-	37,144,000
Distributions paid:				
Preferred stock	-	-	(6,014,000)	(6,014,000)
Common stock	-	-	(19,550,000)	(19,550,000)
Adjustment to reflect minority interest to underlying ownership interest	-	-	-	918,000
Balances at September 30, 2001	<u>\$162,134,000</u>	<u>\$ (740,000)</u>	<u>\$(106,296,000)</u>	<u>\$ 602,861,000</u>

See accompanying notes.

PS BUSINESS PARKS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	For the Nine Months Ended September 30,	
	2001	2000
Cash flows from operating activities:		
Net income	\$ 37,144,000	\$ 33,726,000
Adjustments to reconcile net income to net cash provided by operating activities:		
Gain on investment in Pacific Gulf Properties Inc.	(15,000)	-
Depreciation and amortization expense.....	30,058,000	26,723,000
Minority interest in income.....	19,743,000	18,391,000
Increase in receivables and other assets	(1,056,000)	(1,768,000)
Increase in accrued and other liabilities	6,233,000	5,823,000
Total adjustments	54,978,000	49,169,000
Net cash provided by operating activities.....	92,107,000	82,895,000
Cash flows from investing activities:		
Investment in marketable securities	(9,440,000)	(1,732,000)
Sale of marketable securities.....	6,079,000	-
Acquisition of real estate facilities	(90,239,000)	(56,407,000)
Disposition of real estate facilities	-	23,634,000
Capital improvements to real estate facilities	(7,346,000)	(7,598,000)
Development of real estate facilities	(9,534,000)	(13,790,000)
Net cash used in investing activities.....	(110,480,000)	(55,893,000)
Cash flows from financing activities:		
Principal payments on mortgage notes payable.....	(617,000)	(5,898,000)
Net proceeds from the issuance of preferred stock	64,337,000	-
Net proceeds from the issuance of preferred operating partnership units.....	51,650,000	11,700,000
Exercise of stock options	1,398,000	193,000
Repurchase of common stock	(38,975,000)	(14,781,000)
Redemption of common operating partnership units.....	(808,000)	-
Distributions paid to preferred shareholders.....	(6,014,000)	(3,816,000)
Distributions paid to minority interests – preferred units	(9,696,000)	(8,998,000)
Distributions paid to common shareholders	(19,550,000)	(17,480,000)
Distributions paid to minority interests – common units.....	(6,356,000)	(5,529,000)
Net cash provided by (used in) financing activities.....	35,369,000	(44,609,000)
Net increase (decrease) in cash and cash equivalents	16,996,000	(17,607,000)
Cash and cash equivalents at the beginning of the period.....	49,295,000	74,220,000
Cash and cash equivalents at the end of the period.....	\$ 66,291,000	\$ 56,613,000

See accompanying notes.

PS BUSINESS PARKS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

For the Nine Months
 Ended September 30,

	2001	2000
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Supplemental schedule of non cash investing and financing activities:

Conversion of common OP units into shares of common stock:		
Minority interest – common units.....	\$ -	\$ (2,531,000)
Common stock.....	-	1,000
Paid-in capital.....	-	2,530,000
Adjustment to reflect minority interest to underlying ownership interest:		
Minority interest – common units.....	(918,000)	1,540,000
Paid-in capital.....	918,000	(1,540,000)
Reclassification of developed properties:		
Real estate facilities.....	(28,507,000)	(3,228,000)
Construction in progress.....	28,507,000	3,228,000
Unrealized gain/loss:		
Marketable securities.....	740,000	(6,480,000)
Other comprehensive (loss) income.....	(740,000)	6,480,000

See accompanying notes.

PS BUSINESS PARKS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2001

1. Organization and description of business

PS Business Parks, Inc. ("PSB") was incorporated in the state of California in 1990. As of September 30, 2001, PSB owned an approximate 75% general and limited partnership interest in PS Business Parks, L.P. (the "Operating Partnership" or "OP"). PSB, as the sole general partner of the Operating Partnership, has full, exclusive and complete responsibility and discretion in managing and controlling the Operating Partnership. PSB and the Operating Partnership are collectively referred to as the "Company."

The company is a fully integrated, self-advised and self-managed real estate investment trust ("REIT") that acquires, develops, owns and operates commercial properties containing commercial and industrial rental space. As of September 30, 2001, the Company owned and operated approximately 13.6 million net rentable square feet located in 9 states. The Company also managed approximately 1.3 million net rentable square feet on behalf of Public Storage, Inc. ("PSI"), affiliated entities and a third party owner.

2. Summary of significant accounting policies

Basis of presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principals generally accepted in the United States for interim financial information and with instructions to Form 10-Q and Article 10 or Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. The preparation of the condensed consolidated financial statements in conformity with accounting principals generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements and accompanying notes. Actual results could differ from estimates. In the opinion of management, all adjustments (consisting of normal recurring accruals) necessary for a fair presentation have been included. Operating results for the three and nine months ended September 30, 2001 are not necessarily indicative of the results that may be expected for the year ended December 31, 2001. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2000.

The condensed consolidated financial statements include the accounts of PSB and the Operating Partnership. All significant intercompany balances and transactions have been eliminated in the condensed consolidated financial statements.

Financial instruments

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

PS BUSINESS PARKS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2001

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

Financial assets that are exposed to credit risk consist primarily of cash and cash equivalents and accounts receivable. Cash and cash equivalents, which consist primarily of short-term investments, including commercial paper, are only invested in entities with an investment grade rating. Accounts receivable are not a significant portion of total assets and are comprised of a large number of customers.

Marketable securities

Marketable securities are classified as "available-for-sale" in accordance with Statement of Financial Accounting Standards ("SFAS") No. 115, Accounting for Certain Investments in Debt and Equity Securities. Investments are reflected on the balance sheet at fair market value based upon the quoted market price. The unrealized loss of \$740,000 is excluded from earnings and reported in a separate component of shareholders' equity. Dividend income is recognized when earned.

The Company sold its investment in Pacific Gulf Properties Inc. during the nine months ended September 30, 2001 and recognized a gain of \$15,000.

Real estate facilities

Real estate facilities are recorded at cost. Costs related to the renovation or improvement of the properties are capitalized. Expenditures for repairs and maintenance are expensed as incurred. Buildings and equipment are depreciated on the straight-line method over the estimated useful lives, which are generally 30 and 5 years, respectively.

Interest cost and property taxes incurred during the period of construction of real estate facilities are capitalized. The Company capitalized \$1,001,000 and \$996,000 of interest expense during the nine months ended September 30, 2001 and 2000, respectively.

Intangible assets

Intangible assets consist of property management contracts for properties managed, but not owned, by the Company. The intangible assets are being amortized over seven years. Intangible assets are net of accumulated amortization of \$1,401,000 and \$1,175,000 at September 30, 2001 and December 31, 2000, respectively.

Evaluation of asset impairment

The Company evaluates its assets used in operations by identifying indicators of impairment and by comparing the sum of the estimated undiscounted future cash flows for each asset to the asset's carrying amount. When indicators of impairment are present and the sum of the undiscounted future cash flows is less than the carrying value of such asset, an impairment loss is recorded equal to the difference between the asset's current carrying value and its value based on discounting its estimated future cash flows. At September 30, 2001, no such indicators of impairment have been identified.

PS BUSINESS PARKS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2001

Loans to affiliate

The Company loaned an aggregate of \$77 million to PSI and received \$153,000 in interest income during the period of January 5, 2000 through March 20, 2000. The notes bore interest at 5.9% (per annum) and were repaid as of March 20, 2000.

Revenue and expense recognition

All leases are classified as operating leases. Rental income is recognized on a straight-line basis over the terms of the leases. Reimbursements from tenants for real estate taxes and other recoverable operating expenses are recognized as revenues in the period the applicable costs are incurred.

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

Property management fees are recognized in the period earned.

General and administrative expense

General and administrative expense includes executive compensation, office expense, professional fees, state income taxes, cost of acquisition personnel and other such administrative items. Such amounts include amounts incurred by PSI on behalf of the Company, which were subsequently charged to the Company in accordance with the allocation methodology set forth in the cost allocation and administrative service agreement between the Company and PSI.

Acquisition costs

In March 1998, the Emerging Issues Task Force ("EITF") of the Financial Accounting Standards Board issued guidance (the "97-11 Guidance") with respect to Issue No. 97-11, "Accounting for Internal Acquisition Costs Relating to Real Estate Property Acquisitions." The 97-11 Guidance provides that a company shall expense internal pre-acquisition costs (such as costs of an internal acquisitions department) related to the purchase of an operating property. The Company does not capitalize such internal pre-acquisition costs with respect to the acquisition of operating real estate facilities. Accordingly, the 97-11 Guidance had no impact upon the consolidated financial statements and would have had no impact upon financial statements for periods prior to the issuance of the 97-11 Guidance.

Income taxes

The Company qualified and intends to continue to qualify as a REIT, as defined in Section 856 of the Internal Revenue Code. As a REIT, the Company is not subject to federal income tax to the extent that it distributes its taxable income to its shareholders. A REIT must distribute at least 90% of its taxable income each year. In addition, REIT's are subject to a number of organizational and operating requirements. If the Company fails to qualify as a REIT in any taxable year, the Company will be subject to federal income tax (including any applicable alternative minimum tax) based on its taxable income using corporate income tax rates. Even if the Company qualifies for taxation as a REIT, the Company may be subject to certain state and local taxes on its income and property and to federal income and excise taxes on its undistributed taxable income. The Company believes it met all organization and operating requirements to maintain its REIT status during 2000 and intends to continue to meet such requirements for 2001. Accordingly, no provision for income taxes has been made in the accompanying financial statements.

PS BUSINESS PARKS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2001

Net income per common share

Per share amounts are computed using the number of weighted average common shares outstanding. "Diluted" weighted average common shares outstanding includes the dilutive effect of stock options under the treasury stock method. "Basic" weighted average common shares outstanding excludes such effect. Earnings per share have been calculated as follows:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2001	2000	2001	2000
Net income allocable to common shareholders	\$ 10,010,000	\$ 10,199,000	\$ 31,130,000	\$ 29,910,000
Weighted average common shares outstanding:				
Basic weighted average common shares outstanding	22,210,000	23,117,000	22,610,000	23,354,000
Net effect of dilutive stock options - based on treasury stock method using average market price.....	85,000	99,000	75,000	72,000
Diluted weighted average common shares outstanding	22,295,000	23,216,000	22,685,000	23,426,000
Basic earnings per common share	\$ 0.45	\$ 0.44	\$ 1.38	\$ 1.28
Diluted earnings per common share	\$ 0.45	\$ 0.44	\$ 1.37	\$ 1.28

Reclassifications

Certain reclassifications have been made to the condensed consolidated financial statements for 2000 in order to conform to the 2001 presentation.

3. Real estate facilities

The activity in real estate facilities for the nine months ended September 30, 2001 is as follows:

	Land	Buildings	Accumulated Depreciation	Total
Balances at December 31, 2000	\$ 214,020,000	\$ 709,328,000	\$ (83,841,000)	\$ 839,507,000
Property acquisitions	23,147,000	67,092,000	-	90,239,000
Developed projects.....	4,397,000	24,512,000	-	28,909,000
Capital improvements.....	-	7,346,000	-	7,346,000
Properties held for disposition.....	(929,000)	(2,863,000)	449,000	(3,343,000)
Depreciation expense	-	-	(29,832,000)	(29,832,000)
Balances at September 30, 2001....	\$ 240,635,000	\$ 805,415,000	\$(113,224,000)	\$ 932,826,000

During the nine months ended September 30, 2001, the Company incurred \$9,534,000 in development costs.

PS BUSINESS PARKS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2001

One property has been identified as not meeting the Company's ongoing investment strategy and has been designated as a property held for disposition at September 30, 2001. This property is currently being marketed and the Company anticipates a gain on the sale during this fiscal year. The following summarizes the condensed results of operations of the property held for disposition which is also included in the condensed consolidated statements of income:

	For the Nine Months Ended September 30,	
	2001	2000
Rental income	\$ 1,036,000	\$ 863,000
Cost of operations	(470,000)	(379,000)
Depreciation	(67,000)	(60,000)
Net operating income	\$ 499,000	\$ 424,000

4. Leasing activity

The Company leases space in its real estate facilities to tenants under non-cancelable leases generally ranging from one to ten years. Future minimum rental revenues excluding recovery of expenses as of September 30, 2001 under these leases are as follows:

2001 (October – December)	\$ 36,300,000
2002	127,433,000
2003	101,246,000
2004	74,409,000
2005	54,560,000
Thereafter	85,416,000
	\$ 479,364,000

In addition to minimum rental payments, tenants pay reimbursements for their pro rata share of specified operating expenses, which amounted to \$16,846,000 and \$14,277,000 for the nine months ended September 30, 2001 and 2000, respectively. These amounts are included as rental income and cost of operations in the accompanying condensed consolidated statements of income.

5. Revolving line of credit

In September 2000, the Company extended its unsecured line of credit (the "Credit Facility") with Wells Fargo Bank. The Credit Facility has a borrowing limit of \$100 million and an expiration date of August 6, 2003. The expiration date may be extended by one year on each anniversary of the Credit Facility. Interest on outstanding borrowings is payable monthly. At the option of the Company, the rate of interest charged is equal to (i) the prime rate or (ii) a rate ranging from the London Interbank Offered Rate ("LIBOR") plus 0.75% to LIBOR plus 1.35% depending on the Company's credit ratings and coverage ratios, as defined (currently LIBOR plus 1.00%). In addition, the Company is required to pay an annual commitment fee of 0.25% of the borrowing

PS BUSINESS PARKS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2001

limit. The Company had no outstanding balance and \$100 million available on its line of credit at September 30, 2001 and December 31, 2000.

The Credit Facility requires the Company to meet certain covenants including (i) maintaining a balance sheet leverage ratio (as defined) of less than 0.50 to 1.00, (ii) maintaining interest and fixed charge coverage ratios (as defined) of not less than 2.25 to 1.0 and 1.75 to 1.0, respectively, (iii) maintaining a minimum total shareholders' equity (as defined) and (iv) limiting distributions to 95% of funds from operations. In addition, the Company is limited in its ability to incur additional borrowings (the Company is required to maintain unencumbered assets with an aggregate book value equal to or greater than two times the Company's unsecured recourse debt) or sell assets. The Company was in compliance with the covenants of the Credit Facility at September 30, 2001.

6. Mortgage notes payable

Mortgage notes consist of the following:	September 30, 2001	December 31, 2000
7.050% mortgage note, principal and interest payable monthly, due May 2006.....	\$ 8,424,000	\$ 8,570,000
8.190% mortgage note, principal and interest payable monthly, due March 2007.....	6,334,000	6,482,000
7.290% mortgage note, principal and interest payable monthly, due February 2009.....	6,192,000	6,272,000
7.280% mortgage note, principal and interest payable monthly, due February 2003.....	4,092,000	4,186,000
8.000% mortgage note, principal and interest payable monthly, due April 2003.....	1,954,000	2,022,000
8.500% mortgage note, principal and interest payable monthly, due July 2007	1,811,000	1,850,000
8.000% mortgage note, principal and interest payable monthly, due April 2003.....	1,547,000	1,589,000
	\$30,354,000	\$30,971,000

At September 30, 2001, approximate principal maturities of mortgage notes payable are as follows:

2001 (October - December).....	\$ 214,000
2002.....	898,000
2003.....	7,874,000
2004.....	699,000
2005.....	755,000
Thereafter	19,914,000
	\$ 30,354,000

PS BUSINESS PARKS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2001

7. Minority interests

Common partnership units

The Company presents the accounts of PSB and the Operating Partnership on a consolidated basis. Ownership interests in the Operating Partnership, other than PSB's interest, are classified as minority interest in the condensed consolidated financial statements. Minority interest in income consists of the minority interests' share of the condensed consolidated operating results.

Beginning one year from the date of admission as a limited partner and subject to certain limitations described below, each limited partner other than PSB has the right to require the redemption of its partnership interest.

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

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

On January 12, 2001, the Company redeemed 30,484 common units from unaffiliated third parties for an aggregate cost of \$808,000.

At September 30, 2001, there were 7,305,355 OP units owned by PSI and affiliated entities. On a fully converted basis, assuming all 7,305,355 minority interest OP units were converted into shares of common stock of PSB at September 30, 2001, the minority interest units would convert into approximately 25% of the common shares outstanding. At the end of each reporting period, the Company determines the amount of equity (book value of net assets) which is allocable to the minority interest based upon the ownership interest and an adjustment is made to the minority interest, with a corresponding adjustment to paid-in capital, to reflect the minority interest's equity in the Company.

Preferred partnership units

On April 23, 1999, the Operating Partnership completed a private placement of 510,000 preferred units with a preferred distribution rate of 8 7/8%. The net proceeds from the placement of preferred units were approximately \$12.5 million and were used to repay borrowings from an affiliate.

On September 3, 1999, the Operating Partnership completed a private placement of 3,200,000 preferred units with a preferred distribution rate of 8 3/4%. The net proceeds from the placement of preferred units were approximately \$78 million and part of the proceeds was used to prepay a mortgage note payable of approximately \$8.5 million.

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On September 7 and 23, 1999, the Operating Partnership completed private placements of 1,200,000 and 400,000 preferred units, respectively, with a preferred distribution rate of 8 7/8%. The net proceeds from the placements of preferred units were approximately \$39.2 million.

On July 12, 2000, the Operating Partnership completed a private placement of 480,000 preferred units with a preferred distribution rate of 8 7/8%. The net proceeds from the placement of preferred units were approximately \$11.7 million.

On September 21, 2001, the Operating Partnership completed a private placement of 2,120,000 preferred units with a preferred distribution rate of 9 1/4%. The net proceeds from the placement of preferred units were approximately \$51.6 million.

The Operating Partnership has the right to redeem preferred units on or after the fifth anniversary of the applicable issuance date at the original capital contribution plus the cumulative priority return, as defined, to the redemption date to the extent not previously distributed. The preferred units are exchangeable for Cumulative Redeemable Preferred Stock of the respective series of PS Business Parks, Inc. on or after the tenth anniversary of the date of issuance at the option of the Operating Partnership or a majority of the holders of the respective preferred units. The Preferred Stock will have the same distribution rate and par value as the respective units and will have equivalent terms to those described in Note 9.

8. Property management contracts

The Operating Partnership manages industrial, office and retail facilities for PSI and affiliated entities. These facilities, all located in the United States, operate under the "Public Storage" or "PS Business Parks" names. In addition, the Operating Partnership manages an office building for a third party owner.

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

The property management contract with PSI is for a seven year term with the term being extended one year on each anniversary. The property management contracts with affiliates of PSI are cancelable by either party upon sixty days notice.

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9. Shareholders' equity

Preferred stock

As of September 30, 2001 and December 31, 2000, the Company had the following series of preferred stock outstanding:

Series	Dividend Rate	September 30, 2001		December 31, 2000	
		Shares Outstanding	Carrying Amount	Shares Outstanding	Carrying Amount
Series A	9.250%	2,200	\$ 55,000,000	2,200	\$ 55,000,000
Series D	9.500%	2,640	66,000,000	-	-
		<u>4,840</u>	<u>\$ 121,000,000</u>	<u>2,200</u>	<u>\$ 55,000,000</u>

On April 30, 1999, the Company issued 2,200,000 depositary shares, each representing 1/1,000 of a share of 9 1/4% Cumulative Preferred Stock, Series A. Net proceeds from the public perpetual preferred stock offering were approximately \$53.1 million and were used to repay borrowings from an affiliate and a mortgage note payable of approximately \$11 million. The remaining proceeds were used for investment in real estate.

On May 10, 2001, the Company issued 1,840,000 depositary shares, each representing 1/1,000 of a share of 9 1/2% Cumulative Preferred Stock, Series D in a public offering. On June 18, 2001, the Company issued 800,000 depositary shares, each representing 1/1,000 of a share of 9 1/2% Cumulative Preferred Stock, Series D in a directed placement. Net proceeds from the offerings were approximately \$64.3 million and were used for investment in real estate and general corporate purposes.

Holders of the Company's preferred stock will not be entitled to vote on most matters, except under certain conditions. In the event of a cumulative arrearage equal to six quarterly dividends, the holders of the preferred stock will have the right to elect two additional members to serve on the Company's Board of Directors until all events of default have been cured. At September 30, 2001, there were no dividends in arrears.

Except under certain conditions relation to the Company's qualification as a REIT, the preferred stock is not redeemable prior to the following dates: Series A - April 30, 2004 and Series D - May 10, 2006. On or after the respective dates, the respective series of preferred stock will be redeemable, at the option of the Company, in whole or in part, at \$25 per depositary share, plus any accrued and unpaid dividends.

The Company paid \$6,014,000 and \$3,816,000 in distributions to its preferred shareholders for the nine months ended September 30, 2001 and 2000, respectively.

Common Stock

The Company's Board of Directors has authorized the repurchase from time to time of up to 2,500,000 shares of the Company's common stock on the open market or in privately negotiated transactions. Purchases will be made subject to market conditions and other investment opportunities available to the Company. As of December 31, 2000, the Company had repurchased 722,600 shares of common stock at an aggregate cost of approximately \$16.6 million. The Company repurchased an additional 1,423,011 shares of common stock at an aggregate cost of approximately \$39.0 million for the nine months ended September 30, 2001.

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On March 31, 2000, a holder of common OP units exercised its option and converted its 107,517 common OP units into an equal number of shares of PSB common stock. The conversion resulted in an increase in shareholders' equity and a corresponding decrease in minority interest of approximately \$2,531,000, representing the book value of the OP units at the time of conversion.

The Company paid \$19,550,000 (\$0.87 per common share) and \$17,480,000 (\$0.75 per common share) in distributions to its common shareholders for the nine months ended September 30, 2001 and 2000, respectively. Pursuant to restrictions on the Credit Facility, distributions may not exceed 95% of funds from operations, as defined.

Equity stock

In addition to common and preferred stock, the Company is authorized to issue 100,000,000 shares of Equity Stock. The Articles of Incorporation provide that the Equity Stock may be issued from time to time in one or more series and give the Board of Directors broad authority to fix the dividend and distribution rights, conversion and voting rights, redemption provisions and liquidation rights of each series of Equity Stock.

10. Recent accounting pronouncements

In June 1998, the Financial Accounting Standards Board issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," which is required to be adopted by the Company on January 1, 2001. This statement provides a comprehensive and consistent standard for the recognition and measurements of derivatives and hedging activities. The Company adopted SFAS No. 133 on January 1, 2001. This adoption had no material impact on the Company's consolidated financial statements.

In October 2001, the Financial Accounting Standards Board issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." This statement addresses financial accounting and reporting for the disposal of long-lived assets and becomes effective for financial statements issued for fiscal years beginning after December 15, 2001. The Company is studying this statement to determine its effect on the consolidated financial statements and will adopt this statement in the year ending December 31, 2002.

11. Commitments and contingencies

Substantially all of the Company's properties have been subjected to Phase I environmental reviews. Such reviews have not revealed, nor is management aware of, any probable or reasonably possible environmental costs that management believes would have a material adverse effect on the Company's business, assets or results of operations, nor is the Company aware of any potentially material environmental liability, except as discussed below.

The Company acquired a property in Beaverton, Oregon ("Creekside Corporate Park") in May 1998. A portion of Creekside Corporate Park, as well as properties adjacent to Creekside Corporate Park, are currently the subject of an environmental remedial investigation/feasibility study ("RI/FS") that is being conducted by two current and past owner/operators of an industrial facility on adjacent property, pursuant to an order issued by the Oregon Department of Environmental Quality ("ODEQ"). As part of that study, ODEQ ordered the owner/operators of the industrial facility to sample soil and groundwater on the Company's property to determine the nature and extent of contamination resulting from past operations at the industrial facility. The Company, which is not a party to the Order on Consent, executed separate Access Agreements with the two owner/operators to allow access to portions of Creekside Corporate Park to conduct the required sampling and

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testing. The sampling and testing is ongoing; results to date indicate that the contamination from the industrial facility has migrated onto portions of Creekside Corporate Park owned by the Company.

There is no evidence that the Company's past or current use of the Creekside Corporate Park property contributed in any way to the contamination that is the subject of the current investigation. Nevertheless, upon completion of the RI/FS, it is likely that removal or remedial measures will be required to address contamination detected during the current investigation, including any contamination on or under the Creekside Corporate Park property. Because of the preliminary nature of the investigation, the Company cannot predict the outcome of the investigation, nor can it estimate the costs of any remediation or removal activities that may be required.

One of the two owner/operators that are conducting the RI/FS pursuant to the Order on Consent recently filed for Chapter 11 bankruptcy protection. It is not clear at this point what impact, if any, this filing will have on the completion of the RI/FS, or on any removal or remedial activities ordered by the ODEQ. It is possible that the ODEQ could require the Company to participate in completing the RI/FS and implementing removal or remedial actions that may be required on the Company's property, or to pay a portion of the costs to do so. In the event the Company is ultimately deemed responsible for any costs relating to this matter, the Company believes that the party from whom the property was purchased will be responsible for any expenses or liabilities that the Company may incur as a result of this contamination. In addition, the Company believes it may have recourse against other potentially responsible parties, including, but not limited to, one or both of the owner/operators of the adjacent industrial facility.

On November 3, 1999, the Company filed an action entitled *PS Business Parks, Inc. v. Larry Howard et al.* (Case No. BC219580) in Los Angeles Superior court seeking damages in excess of \$1 million. The complaint alleges that Mr. Howard and entities controlled by him engaged in unfair trade practices. The Company subsequently amended its complaint to add Mary Jayne Howard, a former officer of the Company as a defendant. Mr. Howard filed a cross-complaint which the Company intends to vigorously contest. The litigation is proceeding.

On November 27, 2000, Mary Jayne Howard, a former officer of the Company, filed a demand for arbitration with the American Arbitration alleging claims against the Company for breach of contract, gender discrimination, marital discrimination, and wrongful termination based on public policy. The demand seeks damages of approximately \$2 million. The Company plans to vigorously contest these claims.

On February 2, 2000, the Company filed an action against Mary Piper, its former Vice President of operations, in Riverside County Superior Court, alleging claims for breach of fiduciary duties, fraud and deceit, constructive fraud, negligent misrepresentation, violation of Section 17000 of Business and Professions Code, violation of Section 17200 of the Business and Professions Code and culpable negligence. The Company's claims arose from Ms. Piper's alleged participation in a plan that resulted in the payment of improper kickbacks to Larry Howard, a former vendor of the Company and the husband of Mary Jayne Howard, a former officer of the Company. Ms. Piper subsequently filed a cross-complaint which the Company intends to vigorously contest.

The Company currently is neither subject to any other material litigation nor, to management's knowledge, is any material litigation currently threatened against the Company other than routine litigation and administrative proceedings arising in the ordinary course of business. Management believes that these items will not have a material adverse impact on the Company's condensed consolidated financial position or results of operations.

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

Forward-Looking Statements: Forward-looking statements are made throughout this Quarterly Report on Form 10-Q. For this purpose, any statements contained herein that are not statements of historical fact may be deemed to be forward-looking statements. Without limiting the foregoing, the words "believes," "anticipates," "plans," "expects," "seeks," "estimates," and similar expressions are intended to identify forward-looking statements. There are a number of important factors that could cause the results of the Company to differ materially from those indicated by such forward-looking statements, including those detailed under the heading "Item 2A. Risk Factors." In light of the significant uncertainties inherent in the forward-looking statements included herein, the inclusion of such information should not be regarded as a representation by us or any other person that our objectives and plans will be achieved. Moreover, we assume no obligation to update these forward-looking statements to reflect actual results, changes in assumptions or changes in other factors affecting such forward-looking statements.

Overview

Effect of Economic Conditions on the Company's Operations: During 2001, the Company has been affected by the slowdown in economic activity in the United States which has affected most of the Company's primary markets. These effects were exacerbated by the terrorist attacks of September 11, 2001 and the related aftermath. These effects include a decline in occupancy rates and a reduction in market rates throughout the portfolio, slower than expected lease-up of our development properties, lower interest rates on invested cash and the expectation that insurance costs will rise upon expiration of our policies in March 2002.

The reduction in occupancies and market rental rates has been the result of several factors related to general economic conditions. There are more businesses contracting than expanding, more businesses failing than starting-up and businesses are uncertain, resulting in slower decision-making and requests for shorter term leases. There is also more competing vacant space including substantial amounts of sub-lease space in many of the Company's markets. An extended economic slowdown will put additional downward pressure on occupancies and market rental rates and may lead to an upward pressure on higher rent concessions, tenant improvements and broker commissions.

The Company's developments are 63% leased, but behind the Company's original expectations. There is a 102,000 square foot development in the Las Colinas submarket of Dallas, Texas that is 100% leased, a 141,000 square foot flex development in Northern Virginia that is 60% leased, with increasing activity from government contractors. Finally, the Company completed a 94,000 square foot development in the Beaverton submarket of Portland, Oregon that is 27% leased, but activity has been severely impacted by the economic slowdown.

Historically, the Company has raised capital prior to identifying opportunities to deploy the capital. This has generally resulted in some short-term earnings dilution. Interest rates on cash investments have declined 350 basis points over the past twelve months, resulting in a significantly greater cost of capital awaiting to be deployed. The Company is evaluating whether this strategy continues to be viable in this interest rate environment.

The Company also anticipates a 25%-50% increase in insurance costs when our current policies expire in 2002 due to the terrorist attacks of September 11, 2001. The Company does not expect the increase to materially impact its results since insurance expense represents less than 3% of the Company's operating costs and most of the cost will be passed along to the Company's customers in accordance with the lease agreements.

Growth of the Company's Operations: During 2000 and the nine months ended September 30, 2001, the Company focused on increasing cash flow from its existing core portfolio of properties, expanding its presence in existing markets through strategic acquisitions and developments and strengthening its balance sheet primarily through the issuance of preferred stock/units. The Company has maintained low debt and overall leverage levels including preferred stock/units to facilitate future growth.

During the nine months ended September 30, 2001, the Company expanded its presence in Northern Virginia. The Company acquired 12 buildings known as the Prosperity Business Campus in Fairfax County, Virginia at a cost of \$88.4 million. The acquisition was funded with the Company's existing cash, including proceeds from the issuance of depositary shares. The 12 buildings consist of four office buildings (355,000 square feet) and eight flex-space buildings (302,000 square feet). The Company plans to continue to build its presence in existing markets by acquiring high quality facilities in selected markets. The Company targets properties with below market rents which offer the Company the ability to raise rents to market as leases expire in addition to achieving economies of scale resulting in more efficient operations. In addition, the Company began to collect rent on three developments totaling 340,000 square feet. The developments are in the lease-up phase and net operating income for the nine months ending September 30, 2001 was \$741,000.

During 2000, the Company added approximately 842,000 square feet to its portfolio at an aggregate cost of approximately \$82 million. These acquisitions increased the Company's presence in its existing markets, which the Company believes have the characteristics necessary for long-term growth. The Company acquired 454,000 square feet in Southern California for \$40 million, 178,000 square feet in Northern California for \$23 million, 210,000 square feet in Northern Virginia for approximately \$19 million. In addition, the Company completed development of a property totaling 22,000 square feet in Oregon for approximately \$3 million. The Company also sold five properties aggregating 627,000 square feet for approximately \$23.8 million in non-core markets.

Results of Operations

Results of Operations: Net income for the three months ended September 30, 2001 was \$12,849,000 compared to \$11,471,000 for the same period in 2000. Net income allocable to common shareholders (net income less preferred stock dividends) for the three months ended September 30, 2001 was \$10,010,000 compared to \$10,199,000 for the same period in 2000. Net income per common share on a diluted basis was \$0.45 for the three months ended September 30, 2001 compared to \$0.44 for the same period in 2000 (based on weighted average diluted common shares outstanding of 22,295,000 and 23,216,000, respectively). Net income for the nine months ended September 30, 2001 was \$37,144,000 compared to \$33,726,000 for the same period in 2000. Net income allocable to common shareholders (net income less preferred stock dividends) for the nine months ended September 30, 2001 was \$31,130,000 compared to \$29,910,000 for the same period in 2000. Net income per common share on a diluted basis was \$1.37 for the nine months ended September 30, 2001 compared to \$1.28 for the same period in 2000 (based on weighted average diluted common shares outstanding of 22,685,000 and 23,426,000, respectively).

The Company's property operations account for almost all of the net operating income earned by the Company. The following table presents the pre-depreciation operating results of the properties:

	Three Months Ended September 30,		Change
	2001	2000	
Rental income:			
“Same Park” facilities (11.5 million net rentable square feet).....	\$35,719,000	\$34,455,000	3.7%
Other facilities	7,571,000	2,343,000	223.1%
Total rental income	<u>\$43,290,000</u>	<u>\$36,798,000</u>	17.6%
Cost of operations (excluding depreciation):			
“Same Park” facilities.....	\$9,395,000	\$8,960,000	4.9%
Other facilities	2,611,000	802,000	225.6%
Total cost of operations	<u>\$12,006,000</u>	<u>\$9,762,000</u>	23.0%
Net operating income (rental income less cost of operations):			
“Same Park” facilities.....	\$26,324,000	\$25,495,000	3.3%
Other facilities	4,960,000	1,541,000	221.9%
Total net operating income	<u>\$31,284,000</u>	<u>\$27,036,000</u>	15.7%

	Nine Months Ended September 30,		Change
	2001	2000	
Rental income:			
“Same Park” facilities (11.5 million net rentable square feet).....	\$106,528,000	\$100,731,000	5.8%
Other facilities	15,436,000	6,534,000	136.2%
Total rental income	<u>\$121,964,000</u>	<u>\$107,265,000</u>	13.7%
Cost of operations (excluding depreciation):			
“Same Park” facilities.....	\$28,290,000	\$27,210,000	4.0%
Other facilities	4,562,000	2,222,000	105.3%
Total cost of operations	<u>\$32,852,000</u>	<u>\$29,432,000</u>	11.6%
Net operating income (rental income less cost of operations):			
“Same Park” facilities.....	\$78,238,000	\$73,521,000	6.4%
Other facilities	10,874,000	4,312,000	152.2%
Total net operating income	<u>\$89,112,000</u>	<u>\$77,833,000</u>	14.5%

Rental income and rental income less cost of operations or net operating income ("NOI") prior to depreciation are summarized for the three months ended September 30, 2001 by major geographic region below:

Region	Square Footage	Percent of Total	Rental Income	Percent of Total	NOI	Percent of Total
Southern California	3,548,000	26.1%	\$11,228,000	27.2%	\$8,426,000	26.9%
Northern California	1,495,000	11.0%	4,989,000	11.8%	3,742,000	12.0%
Southern Texas	1,032,000	7.6%	2,883,000	7.3%	1,682,000	5.4%
Northern Texas	1,951,000	14.3%	5,049,000	11.8%	3,367,000	10.8%
Virginia	2,621,000	19.3%	10,119,000	19.9%	7,336,000	23.5%
Maryland	866,000	6.4%	2,494,000	6.1%	1,917,000	6.1%
Oregon	1,288,000	9.5%	4,727,000	11.4%	3,907,000	12.5%
Other	797,000	5.8%	1,801,000	4.6%	907,000	2.9%
	<u>13,598,000</u>	<u>100.0%</u>	<u>\$43,290,000</u>	<u>100.0%</u>	<u>\$31,284,000</u>	<u>100.0%</u>

Rental income and rental income less cost of operations or net operating income ("NOI") prior to depreciation are summarized for the nine months ended September 30, 2001 by major geographic region below:

Region	Square Footage	Percent of Total	Rental Income	Percent of Total	NOI	Percent of Total
Southern California	3,548,000	26.1%	\$33,085,000	27.1%	\$24,726,000	27.7%
Northern California	1,495,000	11.0%	14,500,000	11.9%	11,043,000	12.4%
Southern Texas	1,032,000	7.6%	8,846,000	7.3%	5,359,000	6.0%
Northern Texas	1,951,000	14.3%	14,382,000	11.8%	9,867,000	11.1%
Virginia	2,621,000	19.3%	24,258,000	19.9%	17,885,000	20.1%
Maryland	866,000	6.4%	7,393,000	6.1%	5,650,000	6.3%
Oregon	1,288,000	9.5%	14,032,000	11.5%	11,429,000	12.8%
Other	797,000	5.8%	5,468,000	4.5%	3,153,000	3.5%
	<u>13,598,000</u>	<u>100.0%</u>	<u>\$121,964,000</u>	<u>100.0%</u>	<u>\$89,112,000</u>	<u>100.0%</u>

Supplemental Property Data and Trends: In order to evaluate the performance of the Company's overall portfolio, management analyzes the operating performance of a consistent group of properties (11.5 million net rentable square feet). These properties in which the Company currently has an ownership interest (herein referred to as the "Same Park" facilities) have been owned and operated by the Company for the comparable periods. The square footage has been reduced since the end of the first quarter of 2001 for planned dispositions. The "Same Park" facilities represent approximately 85% of the square footage of the Company's portfolio at September 30, 2001.

The following table summarizes the pre-depreciation historical operating results of the "Same Park" facilities excluding the effects of accounting for rental income on a straight-line basis.

"Same Park" Facilities (11.5 million square feet)

	Three Months Ended September 30,		Change
	2001	2000	
Rental income ⁽¹⁾	\$ 35,481,000	\$ 33,774,000	5.1%
Cost of operations	9,395,000	8,960,000	4.9%
Net operating income.....	<u>\$ 26,086,000</u>	<u>\$ 24,814,000</u>	5.1%
Gross margin ⁽²⁾	73.5%	73.5%	0.0%
<u>Weighted average for period:</u>			
Occupancy	95.0%	96.6%	(1.6%)
Annualized realized rent per occupied sq. ft. ⁽³⁾	\$12.93	\$12.11	6.8%

	Nine Months Ended September 30,		Change
	2001	2000	
Rental income ⁽¹⁾	\$105,505,000	\$ 98,899,000	6.7%
Cost of operations	28,290,000	27,210,000	4.0%
Net operating income.....	<u>\$ 77,215,000</u>	<u>\$ 71,689,000</u>	7.7%
Gross margin ⁽²⁾	73.3%	72.5%	0.7%
<u>Weighted average for period:</u>			
Occupancy	95.6%	96.6%	(1.0%)
Annualized realized rent per occupied sq. ft. ⁽³⁾	\$12.74	\$11.82	7.8%

(1) Rental income does not include the effect of straight-line accounting.

(2) Gross margin is computed by dividing property net operating income by rental income.

(3) Realized rent per square foot represents the actual revenues earned per occupied square foot.

The following tables summarize the "Same Park" operating results by major geographic region for the three months ended September 30, 2001 and 2000:

Region	Revenues 2001	Revenues 2000	Increase (Decrease)	NOI 2001	NOI 2000	Increase (Decrease)
Southern California....	\$9,458,000	\$8,862,000	6.7%	\$7,400,000	\$6,863,000	7.8%
Northern California....	4,314,000	4,016,000	7.4%	3,259,000	3,068,000	6.2%
Southern Texas	2,880,000	2,747,000	4.8%	1,741,000	1,791,000	(2.8%)
Northern Texas	4,678,000	4,393,000	6.5%	3,175,000	3,033,000	4.7%
Virginia.....	5,782,000	5,601,000	3.2%	4,189,000	4,021,000	4.2%
Maryland.....	2,491,000	2,508,000	(0.7%)	1,944,000	1,845,000	5.4%
Oregon	4,076,000	3,862,000	5.5%	3,427,000	3,084,000	11.1%
Other	1,802,000	1,785,000	1.0%	951,000	1,109,000	(14.2%)
	<u>\$35,481,000</u>	<u>\$33,774,000</u>	5.1%	<u>\$26,086,000</u>	<u>\$24,814,000</u>	5.1%

Northern and Southern California and Oregon continue to benefit from the expirations of leases with below market rents. The remaining markets (excluding Southern Texas) grew to a lesser extent. The peripheral markets were affected primarily by the drop in Arizona occupancies.

The following tables summarize the "Same Park" operating results by major geographic region for the nine months ended September 30, 2001 and 2000:

Region	Revenues 2001	Revenues 2000	Increase	NOI 2001	NOI 2000	Increase
Southern California....	\$27,843,000	\$26,108,000	6.6%	\$21,422,000	\$20,003,000	7.1%
Northern California....	12,333,000	11,215,000	10.0%	9,302,000	8,286,000	12.3%
Southern Texas	8,821,000	7,917,000	11.4%	5,370,000	4,762,000	12.8%
Northern Texas	13,775,000	13,011,000	5.9%	9,454,000	8,795,000	7.5%
Virginia.....	17,540,000	16,585,000	5.8%	12,697,000	11,971,000	6.1%
Maryland.....	7,373,000	7,369,000	0.1%	5,647,000	5,452,000	3.6%
Oregon	12,229,000	11,325,000	8.0%	10,076,000	9,134,000	10.3%
Other	5,591,000	5,369,000	4.1%	3,247,000	3,286,000	(1.2%)
	<u>\$105,505,000</u>	<u>\$98,899,000</u>	6.7%	<u>\$77,215,000</u>	<u>\$71,689,000</u>	7.7%

Northern and Southern California and Oregon continue to benefit from the expirations of leases with below market rents. Southern Texas revenues increased in comparison to 2000 primarily due to increased occupancy and rental rate increases at certain Austin facilities. The remaining markets grew to a lesser extent.

Facility Management Operations: The Company's facility management accounts for a small portion of the Company's net operating income. During the three months ended September 30, 2001, \$132,000 in net operating income was recognized from facility management operations compared to \$104,000 for the same period in 2000. During the nine months ended September 30, 2001, \$388,000 in net operating income was recognized from facility management operations compared to \$306,000 for the same period in 2000. Facility management fees have increased due to the increase in rental rates of the properties managed by the Company and an additional property brought under management during 2000.

Business Services: Business services include construction management fees and fees from telecommunications service providers. During the three months ended September 30, 2001, Business Services generated a net operating loss of \$72,000 compared to net operating income of \$4,000 for the same period in 2000. During the nine months ended September 30, 2001, Business Services generated a net operating loss of \$152,000 compared to net operating income of \$207,000 for the same period in 2000.

Interest Income: Interest income reflects earnings on cash balances. Interest income was \$346,000 for the three months ended September 30, 2001 compared to \$1,035,000 for the same period in 2000. Interest income was \$1,659,000 for the nine months ended September 30, 2001 compared to \$3,046,000 for the same period in 2000. The decreases are attributable to lower average cash balances and interest rates. Average cash balances and effective interest rates for the three months ended September 30, 2001 were approximately \$39 million and 3.5% compared to \$64 million and 6.5% for the same period in 2000. Average cash balances and effective interest rates for the nine months ended September 30, 2001 were approximately \$51 million and 4.4% compared to \$68 million and 6.3% for the same period in 2000.

Dividend Income: Dividend income reflects dividends received from marketable securities. Dividend income was \$4,000 for the three months ended September 30, 2001 compared to \$439,000 for the same period in 2000. Dividend income was \$12,000 for the nine months ended September 30, 2001 compared to \$1,297,000 for the same period in 2000. No dividend income was received from Pacific Gulf Properties, Inc. during the three and nine months ended September 30, 2001.

Cost of Operations: Cost of operations for the three months ended September 30, 2001 was \$12,006,000 compared to \$9,762,000 for the same period in 2000. Cost of operations for the nine months ended September 30, 2001 was \$32,852,000 compared to \$29,432,000 for the same period in 2000. The increases are due primarily to increased utilities, repairs and maintenance and payroll costs and the growth in the total square footage of the Company's portfolio of properties. Cost of operations for the three months ended September 30, 2001 consisted primarily of property taxes (\$3,695,000), property maintenance (\$2,461,000), utilities (\$2,241,000) and direct payroll (\$1,660,000). Cost of operations for the nine months ended September 30, 2001 consisted primarily of property taxes (\$10,556,000), property maintenance (\$6,481,000), utilities (\$5,788,000) and direct payroll (\$4,881,000). Cost of operations as a percentage of rental income increased from 26.5% to 27.7% for the three months ended September 30, 2001 due primarily to the hiring of additional regional and divisional officers. Cost of operations as a percentage of rental income decreased from 27.4% to 26.9% for the nine months ended September 30, 2001 as a result of economies of scale achieved through the acquisition and development of properties in core markets and the disposition of properties outside of the Company's core markets in addition to revenue increases in excess of expense increases at the Company's "Same Park" facilities.

Depreciation and Amortization Expense: Depreciation and amortization expense for the three months ended September 30, 2001 was \$10,679,000 compared to \$9,449,000 for the same period in 2000. Depreciation and amortization expense for the nine months ended September 30, 2001 was \$30,058,000 compared to \$26,723,000 for the same period in 2000. The increase is primarily due to the acquisition and development of real estate facilities during 2000 and 2001.

General and Administrative Expense: General and administrative expense was \$1,037,000 for the three months ended September 30, 2001 compared to \$995,000 for the same period in 2000. General and administrative expense was \$3,157,000 for the nine months ended September 30, 2001 compared to \$2,859,000 for the same period in 2000. The increases are due primarily to the increased size and activities of the Company. Included in general and administrative costs are acquisition costs and abandoned transaction costs. Acquisition expenses were \$136,000 and \$130,000 for the three months ended September 30, 2001 and 2000, respectively. There was no abandoned transaction costs for the three months ended September 30, 2001 and 2000. Acquisition expenses were \$453,000 and \$378,000 for the nine months ended September 30, 2001 and 2000, respectively. Abandoned transaction costs were \$7,000 and \$7,000 for the nine months ended September 30, 2001 and 2000, respectively.

Interest Expense: Interest expense was \$538,000 for the three months ended September 30, 2001 compared to \$502,000 for the same period in 2000. The increase is attributable to a reduction in capitalized interest in 2001 as a result of completed developments. Interest expense was \$932,000 for the nine months ended September 30, 2001 compared to \$1,246,000 for the same period in 2000. The decrease is primarily attributable to lower average debt balances during the period. Interest expense of \$103,000 and \$308,000 was capitalized as part of building costs associated with properties under development during the three months ended September 30, 2001 and 2000, respectively. Interest expense of \$1,001,000 and \$996,000 was capitalized as part of building costs associated with properties under development during the nine months ended September 30, 2001 and 2000, respectively.

Gain on Investment in Pacific Gulf Properties Inc. ("PAG"): The Company sold its investment in PAG during the nine months ended September 30, 2001 and recognized a gain of \$15,000.

Minority Interest in Income: Minority interest in income reflects the income allocable to equity interest in the Operating Partnership that is not owned by the Company. Minority interest in income for the three months ended September 30, 2001 was \$6,591,000 (\$3,323,000 allocated to preferred unitholders and \$3,268,000 allocated to common unitholders) compared to \$6,360,000 (\$3,157,000 allocated to preferred unitholders and \$3,203,000 allocated to common unitholders) for the same period in 2000. Minority interest in income for the nine months ended September 30, 2001 was \$19,743,000 (\$9,696,000 allocated to preferred unitholders and \$10,047,000 allocated to common unitholders) compared to \$18,391,000 (\$8,998,000 allocated to preferred unitholders and \$9,393,000 allocated to common unitholders) for the same period in 2000. The increases in minority interest in income are due primarily to the issuance of preferred operating partnership units during 2000 and 2001 and higher earnings at the operating partnership level, partially offset by a conversion of units to common stock during 2000.

Liquidity and Capital Resources

Net cash provided by operating activities for the nine months ended September 30, 2001 and 2000 was \$92,107,000 and \$82,895,000, respectively. Management believes that the Company's internally generated net cash provided by operating activities will continue to be sufficient to enable it to meet its operating expenses, capital improvements and debt service requirements and to maintain the current level of distributions to shareholders.

The following table summarizes the Company's cash flow from operating activities:

	Nine Months Ended September 30,	
	2001	2000
Net income.....	\$37,144,000	\$33,726,000
Gain on investment in Pacific Gulf Properties, Inc.....	(15,000)	-
Depreciation and amortization.....	30,058,000	26,723,000
Minority interest in income.....	19,743,000	18,391,000
Change in working capital.....	5,177,000	4,055,000
Net cash provided by operating activities.....	92,107,000	82,895,000
Maintenance capital expenditures.....	(2,589,000)	(2,301,000)
Tenant improvements.....	(3,091,000)	(3,058,000)
Capitalized lease commissions.....	(1,666,000)	(2,239,000)
Funds available for distributions to shareholders, minority interests, acquisitions and other corporate purposes.....	84,761,000	75,297,000
Cash distributions to shareholders and minority interests.....	(41,616,000)	(35,823,000)
Excess funds available for principal payments on debt, investments in real estate and other corporate purposes.....	<u>\$ 43,145,000</u>	<u>\$ 39,474,000</u>

The Company's capital structure is characterized by a low level of leverage. As of September 30, 2001, the Company had seven fixed rate mortgage notes payable totaling \$30,354,000, which represented 3.1% of its total capitalization (based on book value, including minority interest and debt). The weighted average interest rate for the mortgage notes is 7.56%.

The Company expects to fund its growth strategies with permanent capital, including issuances of common and preferred stock, and retained internally generated cash flows. In addition, the Company may sell properties that no longer meet its investment criteria. The Company may finance acquisitions on a temporary basis with borrowings from its unsecured line of credit (the "Credit Facility"). The Company intends to repay amounts borrowed under the Credit Facility from undistributed cash flow or, as market conditions permit and as determined to be advantageous, from the public or private placement of preferred and common stock/OP units of the Company or Operating Partnership or the formation of joint ventures. As of September 30, 2001 and for the nine months then ended, the leverage ratio was 30% (defined as debt and preferred equity as a percentage of market capitalization) and the Funds From Operations ("FFO") to combined fixed charges and preferred distributions coverage ratio was 4.9 to 1.0.

On September 21, 2001, the Operating Partnership completed a private placement of 2,120,000 preferred units with a preferred distribution rate of 9 1/4%. The net proceeds from the placement of preferred units were approximately \$51.6 million.

On May 10, 2001, the Company issued 1,840,000 depositary shares, each representing 1/1,000 of a share of 9 1/2% Cumulative Preferred Stock, Series D in a public offering. On June 18, 2001, the Company issued 800,000 depositary shares, each representing 1/1,000 of a share of 9 1/2% Cumulative Preferred Stock, Series D in a directed placement. Net proceeds from the offerings were approximately \$64.3 million and were used for investment in real estate and general corporate purposes.

In September 2000, the Company extended its Credit Facility with Wells Fargo Bank. The Credit Facility has a borrowing limit of \$100 million and an expiration date of August 6, 2003. The expiration date may be extended by one year on each anniversary of the Credit Facility. Interest on outstanding borrowings is payable monthly. At the option of the Company, the rate of interest charged is equal to (i) the prime rate or (ii) a rate ranging from the London Interbank Offered Rate ("LIBOR") plus 0.75% to LIBOR plus 1.35% depending on the Company's credit ratings and coverage ratios, as defined (currently LIBOR plus 1.00%). In addition, the Company is required to pay an annual commitment fee of 0.25% of the borrowing limit. As of September 30, 2001, the Company had no balance outstanding on the Credit Facility.

Funds from Operations: FFO is defined as net income, computed in accordance with accounting principles generally accepted in the United States, before depreciation, amortization, minority interest in income, straight-line rent adjustments and extraordinary or non-recurring items. FFO is presented because the Company considers FFO to be a useful measure of the operating performance of a REIT which, together with net income and cash flows, provides investors with a basis to evaluate the operating and cash flow performances of a REIT. FFO does not represent net income or cash flows from operations as defined by accounting principles generally accepted in the United States. FFO does not take into consideration scheduled principal payments on debt or capital improvements. Accordingly, FFO is not necessarily a substitute for cash flow or net income as a measure of liquidity or operating performance or ability to make acquisitions and capital improvements or ability to pay distributions or debt principal payments. Also, FFO as computed and disclosed by the Company may not be comparable to FFO computed and disclosed by other REITs.

FFO for the Company is computed as follows:

	Nine Months Ended September 30,	
	2001	2000
Net income allocable to common shareholders	\$ 31,130,000	\$ 29,910,000
Less: Gain on investment in Pacific Gulf Properties Inc.	(15,000)	-
Less: Gain on disposition of real estate.....	-	(256,000)
Depreciation and amortization	30,058,000	26,723,000
Minority interest in income – common units	10,047,000	9,393,000
Less: Straight-line rent adjustment	(1,171,000)	(1,951,000)
Consolidated FFO allocable to common shareholders and minority interests	70,049,000	63,819,000
FFO allocated to common minority interest – common units.....	(17,092,000)	(15,253,000)
FFO allocated to common shareholders	<u>\$ 52,957,000</u>	<u>\$ 48,566,000</u>

Capital Expenditures: During the nine months ended September 30, 2001, the Company incurred \$7.3 million in maintenance capital expenditures, tenant improvements and capitalized lease commissions. On a recurring annual basis, the Company expects \$0.90 to \$1.20 per square foot in recurring capital expenditures (\$12-\$16 million based on square footage at September 30, 2001). In addition, the Company expects to make \$1.0 million in renovations on a property in Southern California during the remainder of 2001.

Stock Repurchase: On November 7, 2001, the Board of Directors increased the number of common shares authorized to be repurchased from 2,500,000 to 4,500,000. The shares may be repurchased periodically on the open market or in privately negotiated transactions. The Company repurchased 1,423,011 shares of common stock and 30,484 common units at an aggregate cost of approximately \$39.8 million during the nine months ended September 30, 2001. Since inception of the program (March 2000) through September 30, 2001, the Company has repurchased 2,145,611 shares of common stock and 30,484 common units at an aggregate cost of approximately \$56.4 million.

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

ITEM 2A. RISK FACTORS

In addition to the other information in this Form 10-Q, the following factors should be considered in evaluating our company and our business.

PSI has significant influence over us.

PSI owns a substantial number of our shares: At September 30, 2001, PSI owned 25% of the outstanding shares of our common stock (44% upon conversion of its interest in our operating partnership). Consequently, PSI has the ability to significantly influence all matters submitted to a vote of our shareholders, including electing directors, changing our articles of incorporation, dissolving and approving other extraordinary transactions. In addition, PSI's ownership may make it more difficult for another party to take over our company without PSI's approval.

PSI has a voting agreement with another large shareholder: PSI and an institutional shareholder owning 27% of our common stock as of September 30, 2001 have both agreed to vote their shares to support specified nominees to our board of directors until the voting agreement expires, which is not before December 2001. This voting agreement may further increase PSI's influence over our company.

Provisions in our organizational documents may prevent changes in control.

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

Our board can set the terms of certain securities without shareholder approval: Our board of directors is authorized, without shareholder approval, to issue up to 50,000,000 shares of preferred stock and up to 100,000,000 shares of equity stock, in each case in one or more series. Our board has the right to set the terms of each of these series of stock. Consequently, the board could set the terms of a series of stock that could make it difficult (if not impossible) for another party to take over our company even if it might be favorable to our public shareholders. Our articles of incorporation also contain other provisions that could have the same effect. We can also cause our operating partnership to issue additional interest for cash or in exchange for property.

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

Our operating partnership poses additional risks to us.

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

We cannot sell certain properties without PSI's approval.

Before 2007, we may not sell 13 specified properties without PSI's approval. Since PSI would be taxed on a sale of these properties, the interests of PSI and our shareholders may differ as to the best time to sell.

Certain institutional investors have special rights.

Certain institutional investors have rights, such as the right to approve nominees to our board of directors, the right to purchase our securities in certain circumstances and the right to require registration of their shares, not available to our public shareholders.

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

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

Our cash flow would be reduced if our predecessor failed to qualify as a REIT: For us to qualify to be taxed as a REIT, our predecessor, American Office Park Properties, also needed to qualify to be taxed as a REIT. We believe American Office Park Properties qualified as a REIT beginning in 1997 until its March 1998 merger with us. If it is determined that it did not qualify as a REIT, we could also lose our REIT qualification. Before 1997, our predecessor was a taxable corporation and, to qualify as a REIT, was required to distribute all of its profits before the end of 1996. While we believe American Office Park Properties qualified as a REIT since 1997, we did not obtain an opinion of an outside expert at the time of its merger with us.

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

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

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

- the national, state and local economic climate and real estate conditions, such as oversupply of or reduced demand for space and changes in market rental rates;
- how prospective tenants perceive the attractiveness, convenience and safety of our properties;
- our ability to provide adequate management, maintenance and insurance;
- our ability to collect rent from tenants on a timely basis;
- the expense of periodically renovating, repairing and reletting spaces;
- increasing operating costs, including real estate taxes and utilities, if these increased costs cannot be passed through to tenants, and
- changes in tax, real estate and zoning laws.

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

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

We may encounter significant delays in reletting vacant space, resulting in losses of income: When leases expire, we will incur expenses and we may not be able to release the space on the same terms. Certain leases provide tenants with the right to terminate early if they pay a fee. While we have estimated our cost of renewing leases that expire in 2001, our estimates could be wrong. If we are unable to release space promptly, if the terms are significantly less favorable than anticipated or if the costs are higher, we may have to reduce our distributions to shareholders.

Tenant defaults and bankruptcies may reduce our cash flow and distributions: We may have difficulty in collecting from tenants in default, particularly if they declare bankruptcies. This could reduce our cash flow and distributions to shareholders.

We may be adversely affected by significant competition among commercial properties: Many other commercial properties compete with our properties for tenants and we expect that new properties will be built in our markets. Also, we compete with other buyers, many of whom are larger than us, in seeking to acquire commercial properties. Therefore, we may not be able to grow as rapidly as we would like.

We may be adversely affected if losses on our properties are not covered by insurance: We carry insurance on our properties that we believe is comparable to the insurance carried by other operators for similar properties. However, we could suffer uninsured losses that adversely affect us or even result in loss of properties. We might still remain liable on any mortgage debt related to that property.

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

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

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

We acquired a property in Beaverton, Oregon in May 1998 know as Creekside Corporate Park. A portion of Creekside Corporate Park, as well as properties adjacent to Creekside Corporate Park, are currently the subject of an environment remedial investigation/feasibility study, or RI/FS, that is being conducted by two current and past owner/operators of an industrial facility on adjacent property, pursuant to a consent order issued by the Oregon Department of Environmental Quality, or ODEQ. As part of that study, ODEQ ordered the owner/operators of the industrial facility to sample soil and groundwater on our property to determine the nature and extent of contamination resulting from past operations at the industrial facility. Because we are not a party to the consent order, we executed separate agreements with the two owner/operators to allow them access to portions of Creekside Corporate Park to conduct the required sampling and testing. The sampling and testing is ongoing; results to date indicate that the contamination from the industrial facility has migrated onto portions of Creekside Corporate Park owned by us.

There is no evidence that our past or current use of the Creekside Corporate Park property contributed in any way to the contamination that is the subject of the current investigation. Nevertheless, upon completion of the RI/FS, it is likely that removal or remedial measures will be required to address contamination detected during the current investigation, including any contamination on or under the Creekside Corporate Park property. Because of the preliminary nature of the investigation, we cannot predict the outcome of the investigation, nor can we estimate the costs of any remediation or removal activities that may be required.

One of the two owner/operators that are conducting the RI/FS pursuant to the consent order recently filed for Chapter 11 bankruptcy protection. It is not clear at this point what impact, if any, this filing will have on the completion of RI/FS, or on any removal or remedial activities ordered by the ODEQ. It is possible that the ODEQ could require us to participate in completing the RI/FS and implementing removal or remedial actions that may be required on our property, or to pay a portion of the costs to do so. In the event we are ultimately deemed responsible for any costs relating to this matter, we believe that the party from whom the property was purchased will be responsible for any expenses or liabilities that we may incur as a result of this contamination. In addition, we believe that we may have recourse against other potentially responsible parties, including, but not limited to, one or both of the owner/operators of the adjacent industrial facility. However, if we are deemed responsible for any expenses related to removal or remedial actions on the property, and we are not successful in obtaining reimbursement from one or more third parties, our operations and financial condition could be harmed.

We may be affected by the Americans with Disabilities Act: The Americans with Disabilities Act of 1990 requires that access and use by disabled persons of all public accommodations and commercial properties be facilitated. Existing commercial properties must be made accessible to disabled persons. While we have not estimated the cost of complying with this act, we do not believe the cost will be material.

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

We own most of our properties through our operating partnership. Our organizational documents do not limit our ability to invest funds with other in partnerships or joint ventures. This type of investment may present additional risks. For example, our partners may have interests that differ from ours or that conflict with ours, or our partners may become bankrupt.

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

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

We can issue additional securities without shareholder approval.

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

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

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

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

Substantial sales of our common stock, or the perception that substantial sales may occur, could adversely affect the market price of our common stock. Certain of our shareholders hold significant numbers of shares of our common stock and, subject to compliance with applicable securities laws, could sell their shares.

We depend on key personnel.

We depend on our executive officers, including Ronald L. Havner, Jr., our chief executive officer and president. The loss of Mr. Havner could adversely affect our operations. We maintain no key person insurance on him.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

To limit the Company's exposure to market risk, the Company principally finances its operations and growth with permanent equity capital consisting of either common or preferred stock. At September 30, 2001, the Company's debt as a percentage of shareholders' equity (based on book values) was 5.0%.

The Company's market risk sensitive instruments include mortgage notes payable which totaled \$30,354,000 at September 30, 2001. All of the Company's mortgage notes payable bear interest at fixed rates. See Note 6 of the Notes to Consolidated Financial Statements for terms, valuations and approximate principal maturities of the mortgage notes payable as of September 30, 2001. Based on borrowing rates currently available to the Company, the carrying amount of debt approximates fair value.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

On February 2, 2000, the Company filed an action against Mary Piper, its former Vice President of operations, in Riverside County Superior Court, alleging claims for breach of fiduciary duties, fraud and deceit, constructive fraud, negligent misrepresentation, violation of Section 17000 of the Business and Professions Code, violation of Section 17200 of the Business and Professions Code and culpable negligence. The Company's claims arose from Ms. Piper's alleged participation in a plan that resulted in the payment of improper kickbacks to Larry Howard, a former vendor of the Company and the husband of Mary Jayne Howard, a former officer of the Company. Ms. Piper subsequently filed a cross-complaint which the Company intends to vigorously contest.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

- 3.1 Amendment to Certificate of Determination of Preferences of 9 1/8% Series D Cumulative Redeemable Preferred Stock of PS Business Parks, Inc. Filed herewith.
- 3.2 Certificate of Determination of Preferences of 9 1/4% Series E Cumulative Redeemable Preferred Stock of PS Business Parks, Inc. Filed herewith.
- 10.1 Amendment No. 1 to Amendment to Agreement of Limited Partnership of PS Business Parks, L.P. Relating to 9 1/8% Series D Cumulative Redeemable Preferred Units. Filed herewith.
- 10.2 Amendment to Agreement of Limited Partnership of PS Business Parks, L.P. Relating to 9 1/4% Series E Cumulative Redeemable Preferred Units. Filed herewith.
- 12 Statement re: Computation of Ratio of Earnings to Fixed Charges. Filed herewith.

(b) Reports on Form 8-K

The Registrant filed a Current Report on Form 8-K dated July 20, 2001 (filed July 24, 2001) pursuant to Item 9, relating to Regulation FD Disclosure.

The Registrant filed a Current Report on Form 8-K dated September 21, 2001 (filed September 24, 2001) pursuant to Item 9, relating to Regulation FD Disclosure.

SIGNATURES

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

Dated: November 13, 2001

PS BUSINESS PARKS, INC.

BY: /s/ Jack Corrigan

Jack Corrigan

Vice President and Chief Financial Officer

AMENDMENT TO
CERTIFICATE OF DETERMINATION OF PREFERENCES
OF
9.500% CUMULATIVE PREFERRED STOCK, SERIES D
OF
PS BUSINESS PARKS, INC.

The undersigned, David Goldberg and Jack E. Corrigan, Vice President and Secretary, respectively, of PS BUSINESS PARKS, INC., a California corporation (the "Corporation"), do hereby certify:

FIRST: Pursuant to and in accordance with the provisions of Section 401(c) of the California Corporations Code and the Articles of Incorporation of the Corporation, the Board of Directors of the Corporation has duly adopted the recitals and resolutions attached hereto as Exhibit A and incorporated herein by reference authorizing and increasing the authorized number of shares of the Corporation's 9.500% Cumulative Preferred Stock Series D, from 1,840 to 2,640 for a net increase of 800 shares.

SECOND: The number of share of the Corporation's 9.500% Cumulative Preferred Stock, Series D, that are currently outstanding is 1,840.

We further declare under penalty of perjury under the laws of the State of California that the matters set forth in the foregoing certificate are true and correct of our own knowledge.

IN WITNESS WHEREOF, the undersigned has executed this certificate on June 1, 2001.

/s/ David Goldberg
David Goldberg
Vice President

/s/ Jack E. Corrigan
Jack E. Corrigan
Secretary

CERTIFICATE OF DETERMINATION OF PREFERENCES
OF
9¼% SERIES E CUMULATIVE REDEEMABLE
PREFERRED STOCK
OF
PS BUSINESS PARKS, INC.

The undersigned, David Goldberg and Jack E. Corrigan, Vice President and Secretary, respectively, of PS BUSINESS PARKS, INC., a California corporation, do hereby certify:

FIRST: The Restated Articles of Incorporation of the Corporation authorize the issuance of 50,000,000 shares of stock designated "preferred shares," issuable from time to time in one or more series, and authorize the Board of Directors to fix the number of shares constituting any such series, and to determine or alter the dividend rights, dividend rate, conversion rights, voting rights, right and terms of redemption (including sinking fund provisions), the redemption price or prices and the liquidation preference of any wholly unissued series of such preferred shares, and the number of shares constituting any such series.

SECOND: The Board of Directors of the Corporation did duly adopt the resolutions attached hereto as Exhibit A and incorporated herein by reference authorizing and providing for the creation of a series of preferred shares to be known as "9¼% Series E Cumulative Redeemable Preferred Stock" consisting of 2,120,000 shares, none of the shares of such series having been issued.

We further declare under penalty of perjury under the laws of the State of California that the matters set forth in this certificate are true and correct of our own knowledge.

IN WITNESS WHEREOF, the undersigned have executed this certificate this 21st day of September, 2001.

/s/ David Goldberg
David Goldberg, Vice President

/s/ Jack E. Corrigan
Jack E. Corrigan, Secretary

EXHIBIT A

RESOLUTION OF THE BOARD OF DIRECTORS
OF PS BUSINESS PARKS, INC.

ESTABLISHING A SERIES OF 9¼% SERIES E
CUMULATIVE REDEEMABLE PREFERRED STOCK

RESOLVED that pursuant to the authority conferred upon the Board of Directors by Article III of the Restated Articles of Incorporation of this Corporation, there is hereby established a series of the authorized preferred shares of this Corporation having a par value of \$.01 per share, which series shall be designated "9¼% Series E Cumulative Redeemable Preferred Stock," shall consist of 2,120,000 shares and shall have the following rights, preferences and privileges:

1. Rank. The 9¼% Series E Cumulative Redeemable Preferred Stock (the "Series E Preferred Stock") will, with respect to distributions and rights upon voluntary or involuntary liquidation, winding-up or dissolution of the Corporation, or both, rank senior to all classes or series of Common Shares and to all classes or series of equity securities of the Corporation now or hereafter authorized, issued or outstanding, other than any class or series of equity securities of the Corporation expressly designated as ranking on a parity with or senior to the Series E Preferred Stock as to distributions and rights upon voluntary or involuntary liquidation, winding-up or dissolution of the Corporation. For purposes of this Certificate of Determination, the term "Parity Preferred Stock" shall be used to refer to any class or series of capital stock of the Corporation now or hereafter authorized, issued or outstanding expressly designated by the Corporation to rank on a parity with Series E Preferred Stock with respect to distributions and rights upon voluntary or involuntary liquidation, winding-up or dissolution of the Corporation (including the Corporation's 9¼% Cumulative Preferred Stock, Series A, the ⅞ Series B Cumulative Redeemable Preferred Stock, the 8¾% Series C Cumulative Redeemable Preferred Stock, the 9.500% Cumulative Preferred % Series X Cumulative Redeemable Preferred Stock and the ⅞ Series Redeemable Preferred Stock). For purposes of the preceding sentence, "capital stock" means any equity securities (including Common Shares and Preferred Stock), shares, participation or other ownership interests (however any rights (other than debt securities convertible into or exchangeable for equity securities) or options to purchase any of the foregoing.

Distribution Rights. (a) _____. Subject to the rights of holders of Parity Preferred Stock
Priority Return, when, as and if declared by the Board of Directors of the Corporation, out of funds legally available for the payment of dis
issuance of the Series E Preferred Stock and will be payable (A)
September 30 and December 31 of each year commencing on the first such date following the date of issuance of
in the event of a redemption, on the redemption date (each a "Distribution Payment Date"). If any Series E Preferred Stock Distribution Payment Date is no
defined herein), then payment of the distribution to be made on such date shall be made on the Business Day
immediately preceding such Series E Preferred Stock Distribution Payment Date in each case with the same force
made on such date. Distributions on the Series E Preferred Stock will be made to the holders of
record of the Series E Preferred Stock on the relevant record dates to be fixed by the Board of Directors of the
ent be more than 45 days or less than 15 days prior to the relevant
Series E Preferred Stock Distribution Payment Date (each, a "_____").

For purposes of this Certificate of Determination, the following terms shall have the meanings set
herein: (i) "Liquidation Preference

Series E Preferred Stock, plus the amount of any accumulated and unpaid Series E Priority Return (as hereinafter defined) with respect to such share, whether or not declared, minus any distributions in excess of the Series E Priority Return that has accrued with respect to such Series E Preferred Units, to the date of payment; (ii) “Series E Priority Return” shall mean an amount equal to 9¼% per annum of the Liquidation Preference per share of Series E Preferred Stock, commencing on the date of issuance of such share of Series E Preferred Stock, determined on the basis of a 360-day year of twelve 30-day months (and for any period shorter than a full quarterly period for which distributions are computed, the amount of the distribution payable will be computed based on the ratio of the actual number of days elapsed in such period to ninety (90) days), cumulative to the extent not distributed on any Series E Preferred Stock Distribution Payment Date plus the per share amount accrued on each share of Series E Preferred Stock on the date of issuance of such shares in exchange of Series E Preferred Units of PS Business Parks, L.P. corresponding to the accrued and unpaid priority return on such Preferred Units, if any; and (iii) “Business Day” shall mean each day, other than a Saturday or a Sunday, which is not a day on which banking institutions in New York, New York are authorized or required by law, regulation or executive order to close.

(b) Prohibition on Distributions. No distributions on Series E Preferred Stock shall be authorized by the Board of Directors of the Corporation or paid or set apart for payment by the Corporation at any such time as the terms and provisions of any agreement of the Corporation including any agreement relating to indebtedness, prohibits such authorization, payment or setting apart for payment or provides that such authorization, payment or setting apart for payment would constitute a breach thereof or a default thereunder, or to the extent that such authorization or payment shall be restricted or prohibited by law.

(c) Distributions Cumulative. Distributions on the Series E Preferred Stock will accrue whether or not the terms and provisions of any agreement of the Corporation, including any agreement relating to its indebtedness at any time prohibits the current payment of distributions, whether or not the Corporation has earnings, whether or not there are funds legally available for the payment of such distributions and whether or not such distributions are authorized or declared. Accrued but unpaid distributions on the Series E Preferred Stock will accumulate as of the Series E Preferred Stock Distribution Payment Date on which they first become payable. Distributions on account of arrears for any past distribution periods may be declared and paid at any time, without reference to a regular Series E Preferred Stock Distribution Payment Date to holders of record of the Series E Preferred Stock on the record date fixed by the Board of Directors which date shall not exceed fifteen (15) business days prior to the payment date. Accumulated and unpaid distributions will not bear interest.

(d) Priority as to Distributions. (i) So long as any Series E Preferred Stock is outstanding, no distribution of cash or other property shall be authorized, declared, paid or set apart for payment on or with respect to any class or series of Common Shares or any class or series of other stock of the Corporation ranking junior as to the payment of distributions or rights upon voluntary or involuntary dissolution, liquidation or winding-up of the Corporation to the Series E Preferred Stock (such Common Shares or other junior stock, collectively, “Junior Stock”), nor shall any cash or other property be set aside for or applied to the purchase, redemption or other acquisition for consideration of any Series E Preferred Stock, any Parity Preferred Stock or any Junior Stock, unless, in each case, all distributions accumulated on all Series E Preferred Stock and all classes and series of outstanding Parity Preferred Stock have been paid in full. The foregoing sentence shall not prohibit (i) distributions payable solely in Junior Stock, and (ii) the conversion of Series E Preferred Stock, Junior Stock or Parity Preferred Stock into stock of the Corporation ranking junior to the Series E Preferred Stock as to distributions.

(ii) So long as distributions have not been paid in full (or a sum sufficient for such full payment is not irrevocably deposited in trust for payment) upon the Series E Preferred Stock, all distributions authorized and declared on the Series E Preferred Stock and all classes or series of outstanding Parity Preferred Stock with respect to distributions shall be authorized and declared so that the amount of distributions authorized and declared per share of Series E Preferred Stock and such other classes or series of Parity Preferred Stock shall in all cases bear to each other the same ratio that accrued distributions per share on the Series E Preferred Stock and such other classes or series of Parity Preferred Stock (which shall not include any accumulation in respect of unpaid distributions for prior

distribution periods
to each other.

- (e) No Further Rights. Holders of Series E Preferred Stock shall not be entitled to any distributions, parity or otherwise, in excess of the full cumulative distributions described herein.

3. _____ (a) Payment of Liquidating Distributions
Preferred Stock with respect to rights upon any voluntary or involuntary liquidation, dissolution or winding up of the Corporation and subject to any series of capital stock ranking senior to the Series E Preferred Stock with respect to winding up of the Corporation, all payments of Series E Preferred Stock shall be made so that the payments on the Series E Preferred Stock and such Parity Preferred Stock shall in all cases bear to each other the same ratio as the Series E Preferred Stock (which shall not include any accumulation in respect of unpaid distributions for prior distribution periods if such Parity Preferred Stock) to the total of the assets of the Corporation available for distribution at the time of liquidation, dissolution or winding up of the Corporation. If upon such voluntary or involuntary liquidation, dissolution or winding up of the Corporation, all payments of Series E Preferred Stock and any Parity Preferred Stock shall be made so that the payments on the Series E Preferred Stock and such Parity Preferred Stock shall in all cases bear to each other the same ratio as the Series E Preferred Stock (which shall not include any accumulation in respect of unpaid distributions for prior distribution periods if such Parity Preferred Stock) to the total of the assets of the Corporation available for distribution at the time of liquidation, dissolution or winding up of the Corporation.

(b) Notice. Written notice of any such voluntary or involuntary liquidation, dissolution or winding up of the Corporation, stating the payment date or dates when, and the place or places where, the amounts distributable in such circumstances shall be payable, shall be given by (i) fax and (ii) by first class mail, postage prepaid, not less than 10 and not more than 60 days prior to the payment date stated therein, to each record holder of the Series E Preferred Stock at the time of the distribution.

(c) No Further Rights. After payment of the full amount of the liquidating distributions to which they are entitled, the Series E Preferred Stock will have no right or claim to any of the remaining assets of the Corporation.

Consolidation, Merger or Certain Other Transactions
exchange or transfer (for cash, shares of stock, securities or other consideration) of all or substantially all of the assets of the Corporation with or into, any corporation, trust or other entity (or of any corporation, trust or other entity with or without assets) or the winding up of the Corporation.

4. _____ (a) Right of Optional Redemption. The Series E Preferred Stock may not be redeemed prior to September 21, 2006. On or after such date, the Corporation shall have the right to redeem the Series E Preferred Stock upon written notice, at a redemption price, payable in cash, equal to the Liquidation Preference (the "Redemption Price").

Limitation on Redemption
solely to the extent such payment would be permitted as a distribution under the California Corporations Code.

(c) Procedures for Redemption. (i) Notice of redemption will be (i) faxed, and (ii) mailed by the Corporation, postage prepaid, not less than 30 nor more than 60 days prior to the redemption date, addressed to the respective holders of record of the Series E Preferred Stock to be redeemed at their respective addresses as they appear on the transfer records of the Corporation. No failure to give or defect in such notice shall affect the validity of the proceedings for the redemption of any Series E Preferred Stock except as to the holder to whom such notice was defective or not given. In addition to any information required by law or by the applicable rules of any exchange upon which the Series E Preferred Stock may be listed or admitted to trading, each such notice shall state: (i) the redemption date, (ii) the redemption price, (iii) the number of shares of Series E Preferred Stock to be redeemed, (iv) the place or places where such shares of Series E Preferred Stock are to be surrendered for payment of the redemption price, (v) that distributions on the Series E Preferred Stock to be redeemed will cease to accumulate on such redemption date and (vi) that payment of the redemption price and any accumulated and unpaid distributions will be made upon presentation and surrender of such Series E Preferred Stock.

(ii) If the Corporation gives a notice of redemption in respect of Series E Preferred Stock (which notice will be irrevocable) then, by 12:00 noon, New York City time, on the redemption date, the Corporation will deposit irrevocably in trust for the benefit of the Series E Preferred Stock being redeemed funds sufficient to pay the applicable Series E Redemption Price, and will give irrevocable instructions and authority to pay such Series E Redemption Price to the holders of the Series E Preferred Stock upon surrender of the certificate evidencing the Series E Preferred Stock by such holders at the place designated in the notice of redemption. On and after the date of redemption, distributions will cease to accumulate on the Series E Preferred Stock called for redemption, unless the Corporation defaults in the payment thereof. If any date fixed for redemption of Series E Preferred Stock is not a Business Day, then payment of the redemption price payable on such date will be made on the next succeeding day that is a Business Day (and without any interest or other payment in respect of any such delay) except that, if such Business Day falls in the next calendar year, such payment will be made on the immediately preceding Business Day, in each case with the same force and effect as if made on such date fixed for redemption. If payment of the Series E Redemption Price or any accumulated or unpaid distributions in respect of the Series E Preferred Stock is improperly withheld or refused and not paid by the Corporation, distributions on such Series E Preferred Stock will continue to accumulate from the original redemption date to the date of payment, in which case the actual payment date will be considered the date fixed for redemption for purposes of calculating the applicable Series E Redemption Price.

(d) Status of Redeemed Stock. Any Series E Preferred Stock that shall at any time have been redeemed shall after such redemption, have the status of authorized but unissued Preferred Stock, without designation as to class or series until such shares are once more designated as part of a particular class or series by the Board of Directors.

5. Voting Rights. (a) General. Holders of the Series E Preferred Stock will not have any voting rights, except as set forth below.

(b) Right to Elect Directors. If the Corporation shall fail to pay full cumulative dividends on the shares of Series E Preferred Stock or any of its preferred shares for six quarterly dividend payment periods, whether or not consecutive (a "Dividend Default"), the holders of all outstanding preferred shares, voting as a single class without regard to series, will be entitled to elect two Directors until full cumulative dividends for all past dividend payment periods on all preferred shares have been paid or declared and funds therefor set apart for payment. Such right to vote separately as a class to elect Directors shall, when vested, be subject, always, to the same provisions for the vesting of such right to elect Directors separately as a class in the case of future Dividend Defaults. At any time when such right to elect Directors separately as a class shall have so vested, the Corporation may call, and, upon the written request of the holders of record of not less than 20% of the total number of preferred shares of the Corporation then outstanding, shall call, a special meeting of stockholders for the election of Directors. In the case of such a written request, such special meeting shall be held within 90 days after the delivery of such request and, in either case, at the place and upon the notice provided by law and in the Bylaws of the Corporation; provided that the Corporation shall not be required to call such a special meeting if such request is received less than 120 days before

the date fixed for the next ensuing Annual Meeting of Shareholders of the Corporation and the holders of all classes of outstanding preferred shares are afforded the opportunity to elect such Directors (or fill any vacancy) at such Annual Meeting of Shareholders. Directors elected as aforesaid shall serve until the next Annual Meeting of Shareholders of the Corporation or until their respective successors shall be elected and qualified. If, prior to the end of the term of any Director elected as aforesaid, a vacancy in the office of such Director shall occur during the continuance of a Dividend Default by reason of death, resignation, or disability, such vacancy shall be filled for the unexpired term by the appointment of a new Director for the unexpired term of such former Director, such appointment to be made by the remaining Director elected as aforesaid.

(c) Certain Voting Rights. So long as any Series E Preferred Stock or Series E Preferred Units exchangeable into Series E Preferred Stock remain outstanding, the Corporation shall not, without the affirmative vote of the holders of a majority of the Series E Preferred Stock outstanding at the time (i) designate or create, or increase the authorized or issued amount of, any class or series of shares ranking prior to the Series E Preferred Stock with respect to payment of distributions or rights upon liquidation, dissolution or winding-up or reclassify any authorized shares of the Corporation into any such shares, or create, authorize or issue any obligations or security convertible into or evidencing the right to purchase any such shares, (ii) designate or create, or increase the authorized or issued amount of, any Parity Preferred Stock or reclassify any authorized shares of the Corporation into any such shares, or create, authorize or issue any obligations or security convertible into or evidencing the right to purchase any such shares, but only to the extent such Parity Preferred Stock is issued to an Affiliate of the Corporation on terms that differ from the terms of such series of Parity Preferred Stock issued to the public or non-Affiliates of the Corporation, (iii) increase the authorized number of shares of Series E Preferred Stock, or (iv) either (A) consolidate, merge into or with, or convey, transfer or lease its assets substantially as an entirety, to any corporation or other entity, or (B) amend, alter or repeal the provisions of the Corporation's Articles of Incorporation (including this Certificate of Determination) or By-laws, whether by merger, consolidation or otherwise, in each case that would materially and adversely affect the powers, special rights, preferences, privileges or voting power of the Series E Preferred Stock or the holders thereof; provided, however, that with respect to the occurrence of a merger, consolidation or a sale or lease of all of the Corporation's assets as an entirety, so long as (a) the Corporation is the surviving entity and the Series E Preferred Stock remains outstanding with the terms thereof unchanged, or (b) the resulting, surviving or transferee entity is a corporation organized under the laws of any state and substitutes the Series E Preferred Stock for other preferred stock having substantially the same terms and same rights as the Series E Preferred Stock, including with respect to distributions, voting rights and rights upon liquidation, dissolution or winding-up, then the occurrence of any such event shall not be deemed materially and adversely affect such rights, privileges or voting powers of the holders of the Series E Preferred Stock; and provided, further, that any increase in the amount of authorized Preferred Stock or the creation or issuance of any other class or series of Preferred Stock, or any increase in an amount of authorized shares of each class or series, in each case ranking either (a) junior to the Series E Preferred Stock with respect to payment of distributions and the distribution of assets upon liquidation, dissolution or winding-up, or (b) on a parity with the Series E Preferred Stock with respect to payment of distributions or the distribution of assets upon liquidation, dissolution or winding-up to the extent such Preferred Stock is not issued to an Affiliate of the Corporation on terms that differ from the terms of any Parity Preferred Stock issued to the public or non-Affiliates of the Corporation, shall not be deemed to materially and adversely affect such rights, preferences, privileges or voting powers.

The affirmative vote or consent of the holders of at least 66 2/3% of the outstanding shares of this Series and any other series of preferred shares ranking on a parity with this Series as to dividends and upon liquidation, voting as a single class without regard to series, will be required to issue, authorize or increase the authorized amount of any class or series of shares ranking prior to this Series as to dividends or upon liquidation or to issue or authorize any obligation or security convertible into or evidencing a right to purchase any such security, but subject to Section 5(c)(ii) hereof, the Articles of Incorporation may be amended to increase the number of authorized preferred shares ranking on a parity with or junior to this Series or to create another class of preferred shares ranking on a parity with or junior to this Series without the vote of the holders of outstanding shares of this Series.

6. Conversion. The holders of the Series E Preferred Stock shall not have any rights to convert such shares into shares of any other class or series of stock or into any other securities of, or interest in, the Corporation.

7. No Sinking Fund. No sinking fund shall be established for the retirement or redemption of Series E Preferred Stock.

8. No Preemptive Rights. No holder of the Series E Preferred Stock of the Corporation shall, as such holder, have any preemptive rights to purchase or subscribe for additional shares of stock of the Corporation or any other security of the Corporation which it may issue or sell.

PS BUSINESS PARKS, L.P.
AMENDMENT NO. 1 TO
PARTNERSHIP RELATING TO
9 1/2% SERIES D CUMULATIVE REDEEMABLE

June 18, 2001 (this "**Amendment**")
Agreement of Limited Partnership of PS Business Parks, L.P., a California limited partnership (the "**Partnership**"
dated as of May 10, 2001 (the "**Initial Amendment**" Limited Partnership of the
Partnership, dated as of March 17, 1998, as amended, by and among PS Business Parks, Inc. (the
Partner") and each of the limited partners described on Exhibit A to that partnership agreement (the
Agreement")

WHEREAS, on May 10, 2001 the General Partner issued 1,840,000 Depositary Shares each representing
Series D" (the "**Depositary Shares**" a price of \$25.00 per Depositary Share;
\$25.00 per Depositary Share; and

Amendment as of the
date first set forth above to increase the number of Series D Preferred Units (as defined in the Initial Amendment).

NOW, THEREFORE, the Initial Amendment is hereby amended as follows:

Section 2(a) of the Initial Amendment is
with the following:

Pursuant to Section 4.2(a) of the Partnership Agreement, a series of Partnership Units (as such
term is defined in the Partnership Agreement) in the Partnership designated as the "9 1/2% Seri
Cumulative Redeemable Preferred Units" (the "**Series D Preferred Units**"
effective as of May 10, 2001. The initial number of Series D Preferred Units shall be 1,840,000.
Effective June 18, 2001, the number of Series D Preferred
The Holders of Series D Preferred Units shall not have any Percentage Interest (as such term is
defined in the Partnership Agreement) in the Partnership.

Section 2. onal 800,000 Series D Preferred Units
provided for herein, the Initial Amendment is further amended pursuant to Section 12.3 of the Partnership
A to the Partnership Agreement) with the form of Exhibit C that is attached to this Amendment as Exhibit

IN WITNESS WHEREOF, this Amendment has been executed as of the date first above written.

PS BUSINESS PARKS, INC.

By: /s/ Jack E. Corrigan
Name: Jack E. Corrigan
Title: Chief Financial Officer

PS BUSINESS PARKS, L.P.

AMENDMENT TO AGREEMENT OF LIMITED
PARTNERSHIP RELATING TO
9¼% SERIES E CUMULATIVE REDEEMABLE
PREFERRED UNITS

This Amendment to the Agreement of Limited Partnership of PS Business Parks, L.P., a California limited partnership (the "**Partnership**"), dated as of the 21st day of September, 2001 (this "**Amendment**") amends the Agreement of Limited Partnership of the Partnership, dated as of March 17, 1998, by and among PS Business Parks, Inc. (the "**General Partner**") and each of the limited partners executing a signature page thereto, as amended by that certain Amendment to Agreement of Limited Partnership Relating to ⅙ Series B Cumulative Redeemable Preferred Units, dated as of April 23, 1999, an Amendment to Agreement of Limited Partnership Relating to 9¼% Series A Cumulative Redeemable Preferred Units, dated as of April 30, 1999, an Amendment Relating to the ⅙ Series X Cumulative Redeemable Preferred Units dated as of September 7, 1999, an Amendment to Agreement of Limited Partnership Relating to 8⅓% Series C Cumulative Redeemable Preferred Units, dated as of September 3, 1999, an Amendment to Agreement of Limited Partnership Relating to ⅙ of Series Y Cumulative Redeemable Preferred Units, dated as of July 12, 2000, and an Amendment to Agreement of Limited Partnership Relating to 9½% Series D Cumulative Redeemable Preferred Units, dated as of May 10, 2001, as amended by Amendment No. 1 to such Amendment to Agreement of Limited Partnership Relating to 9½% Series D Cumulative Redeemable Preferred Units, dated as of June 18, 2001 (collectively, the "**Partnership Agreement**"). Capitalized terms used herein and not otherwise defined shall have the meanings ascribed to such terms in the Partnership Agreement. Section references are (unless otherwise specified) references to sections in this Amendment.

WHEREAS, pursuant to Section 4.2(a) of the Partnership Agreement, the General Partner desires to cause the Partnership to issue additional Units of a new class and series, with the designations, preferences and relative, participating, optional or other special rights, powers and duties set forth herein;

WHEREAS, pursuant to Section 4.2(a) of the Partnership Agreement, the General Partner, without the consent of the Limited Partners, may amend the Partnership Agreement by executing a written instrument setting forth the terms of such amendment; and

WHEREAS, the General Partner desires by this Amendment to so amend the Partnership Agreement as of the date first set forth above to provide for the designation and issuance of such new class and series of Units.

NOW, THEREFORE, the Partnership Agreement is hereby amended by establishing and fixing the rights, limitations and preferences of a new class and series of Units as follows:

Section 1. Definitions. Capitalized terms not otherwise defined herein shall have their respective meanings set forth in the Partnership Agreement. Capitalized terms that are used in this Amendment shall have the meanings set forth below:

(a) "**Liquidation Preference**" means, with respect to the Series E Preferred Units, \$25.00 per Series E Preferred Unit, plus the amount of any accumulated and unpaid Priority Return with respect to such unit, whether or not declared, minus any distributions in excess of the Priority Return that has accrued with respect to such Series E Preferred Units to the date of payment.

(b) "**Parity Preferred Units**" means any class or series of Partnership Interests of the Partnership now or hereafter authorized, issued or outstanding and expressly designated by the Partnership to rank on a parity with the Series E Preferred Units (as hereinafter defined) with respect to distributions and rights upon voluntary or involuntary liquidation winding-up or dissolution of the Partnership, including the 9¼% Series A Cumulative

Redeemable Preferred Units (the “**Series A Preferred Units**”), the ⅞ Series B Cumulative Redeemable Preferred Units (the “**Series B Preferred Units**”), the 8¾% Series C Cumulative Redeemable Preferred Units (the “**Series C Preferred Units**”), the 9½% Series D Cumulative Redeemable Preferred Units (the “**Series D Preferred Units**”), the ⅞ Series X Cumulative Redeemable Preferred Units (the “**Series X Preferred Units**”) and the ⅞ Series Y Cumulative Redeemable Preferred Units (the “**Series Y Preferred Units**”). Notwithstanding the differing allocation rights set forth in Section 4 below that apply to the Series A, B, C and D Preferred Units (as compared to the Series E, X and Y Preferred Units), for purposes of this Amendment, those Series A, B, C and D Preferred Units and any future series of preferred units that rank in parity with those series also shall be considered Parity Preferred Units to the Series E, X and Y Preferred Units.

(c) “**Priority Return**” means an amount equal to 9¼% per annum of the Liquidation Preference per Series E Preferred Unit, commencing on the date of issuance of such Series E Preferred Unit, determined on the basis of a 360-day year of twelve 30-day months, and for any period shorter than a full quarterly period for which distributions are computed, the amount of the distributions payable will be based on the ratio of the actual number of days elapsed in such period to ninety (90) days, cumulative to the extent not distributed for any given distribution period pursuant to Section 3, hereof, commencing on the date of the issuance of such Series E Preferred Unit.

(d) “**PTP**” means a “publicly traded partnership” within the meaning of Section 7704 of the Code.

Section 2. Designation and Number. Pursuant to Section 4.2(a) of the Partnership Agreement, a series of Partnership Units in the Partnership designated as the “9¼% Series E Cumulative Redeemable Preferred Units” (the “**Series E Preferred Units**”) is hereby established. The number of Series E Preferred Units shall be 2,120,000. The Holders of Series E Preferred Units shall not have any Percentage Interest (as such term is defined in the Partnership Agreement) in the Partnership.

Section 3. Distributions. (a) **Payment of Distributions.** Subject to the rights of holders of Parity Preferred Units as to the payment of distributions pursuant to Section 5.1 of the Partnership Agreement, holders of Series E Preferred Units shall be entitled to receive, when, as and if declared by the Partnership acting through the General Partner, the Priority Return. Such Priority Return shall be cumulative, shall accrue from the original date of issuance of the Series E Preferred Units and, notwithstanding Section 5.1 of the Partnership Agreement, will be payable (i) quarterly in arrears on March 31, June 30, September 30 and December 31 of each year commencing on September 30, 2001, and (ii) in the event of (A) a redemption of Series E Preferred Units, or (B) an exchange of Series E Preferred Units into Series E Preferred Stock, on the redemption date or the exchange date, as applicable (each a “**Series E Preferred Unit Distribution Payment Date**”). The amount of the distribution payable for any period will be computed on the basis of a 360-day year of twelve 30-day months and for any period shorter than a full quarterly period for which distributions are computed, the amount of the distribution payable will be computed based on the ratio of the actual number of days elapsed in such period to ninety (90) days. If any date on which distributions are to be made on the Series E Preferred Units is not a Business Day (as defined herein), then payment of the distribution to be made on such date will be made on the Business Day immediately preceding such date with the same force and effect as if made on such date. Distributions on the Series E Preferred Units will be made to the holders of record of the Series E Preferred Units on the relevant record dates to be fixed by the Partnership acting through the General Partner, which record dates shall in no event exceed fifteen (15) Business Days prior to the relevant Series E Preferred Unit Distribution Payment Date (the “**Series E Preferred Unit Partnership Record Date**”).

(b) **Prohibition on Distribution.** No distributions on Series E Preferred Units shall be authorized by the General Partner or paid or set apart for payment by the Partnership at any such time as the terms and provisions of any agreement of the Partnership or the General Partner, including any agreement relating to their indebtedness, prohibits such authorization, payment or setting apart for payment or provides that such authorization, payment or setting apart for payment would constitute a breach thereof or a default thereunder, or to the extent that such authorization or payment shall be restricted or prohibited by law.

(c) Distributions Cumulative. Distributions on the Series E Preferred Units will accrue, whether or not declared, whether or not the terms and provisions of any agreement of the Partnership or the General Partner, including any agreement relating to its indebtedness at any time prohibit the current payment of distributions, whether or not the Partnership has earnings, whether or not there are funds legally available for the payment of such distributions and whether or not such distributions are authorized. Accrued but unpaid distributions on the Series E Preferred Units will accumulate as of the Series E Preferred Unit Distribution Payment Date on which they first become payable. Distributions on account of arrears for any past distribution periods may be declared and paid at any time, without reference to a regular Series E Preferred Unit Distribution Payment Date to holders of record of the Series E Preferred Units on the record date fixed by the Partnership acting through the General Partner which date shall not exceed fifteen (15) Business Days prior to the payment date. Accumulated and unpaid distributions will not bear interest.

(d) Priority as to Distributions. Subject to the provisions of Article 13 of the Partnership Agreement:

(i) so long as any Series E Preferred Units are outstanding, no distribution of cash or other property shall be authorized, declared, paid or set apart for payment on or with respect to any class or series of Partnership Interest ranking junior as to the payment of distributions or rights upon a voluntary or involuntary liquidation, dissolution or winding-up of the Partnership to the Series E Preferred Units (collectively, "**Junior Units**"), nor shall any cash or other property be set aside for or applied to the purchase, redemption or other acquisition for consideration of any Series E Preferred Units, any Parity Preferred Units or any Junior Units, unless, in each case, all distributions accumulated on all Series E Preferred Units and all classes and series of outstanding Parity Preferred Units have been paid in full. The foregoing sentence shall not prohibit (x) distributions payable solely in Junior Units, or (y) the conversion of Junior Units or Parity Preferred Units into Partnership Interests ranking junior to the Series E Preferred Units as to distributions and rights upon involuntary or voluntary liquidation, dissolution or winding up of the Partnership or (z) the redemption of Partnership Interests corresponding to Series E Preferred Stock, Parity Preferred Stock or Junior Stock to be purchased by the General Partner pursuant to the Articles of Incorporation of the General Partner with respect to the General Partner's common stock and comparable provisions in the Articles of Incorporation with respect to other classes or series of capital stock of the General Partner to preserve the General Partner's status as a real estate investment trust, provided that such redemption shall be upon the same terms as the corresponding purchase pursuant to the Articles of Incorporation.

(ii) So long as distributions have not been paid in full (or a sum sufficient for such full payment is not irrevocably deposited in trust for payment) upon the Series E Preferred Units, all distributions authorized and declared on the Series E Preferred Units and all classes or series of outstanding Parity Preferred Units shall be authorized and declared so that the amount of distributions authorized and declared per Series E Preferred Unit and such other classes or series of Parity Preferred Units shall in all cases bear to each other the same ratio that accrued distributions per Series E Preferred Unit and such other classes or series of Parity Preferred Units (which shall not include any accumulation in respect of unpaid distributions for prior distribution periods if such class or series of Parity Preferred Units do not have cumulative distribution rights) bear to each other.

(e) No Further Rights. Holders of Series E Preferred Units shall not be entitled to any distributions, whether payable in cash, other property, or otherwise, in excess of the full cumulative distributions described herein.

Section 4. Allocations. Section 6.1(a)(ii) of the Partnership Agreement is amended to read, in its entirety, as follows:

“(ii)(A) Notwithstanding anything to the contrary contained in this Agreement, in any taxable year: (1) the holders of Series A, B, C and D Preferred Units shall first be allocated an amount of gross income equal to the Priority Return distributed to such holders in such taxable year, and (2) subject to any prior allocation of Profit pursuant to the loss chargeback set forth in Section 6.1(a)(ii)(B) below, the holders of Series E, X and Y Preferred Units shall then be allocated an amount of Profit equal to the Priority Return

distributed to such holders either in such taxable year or in prior taxable years to the extent that such distributions have not previously been matched with an allocation of Profit pursuant to this Section 6.1(a)(ii)(A)(2).

(B) After the Capital Account balances of all Partners other than holders of any series of Preferred Units have been reduced to zero, Losses of the Partnership that otherwise would be allocated so as to cause deficit Capital Account balances for those other Partners shall be allocated to the holders of the Series A, B, C, D, E, X and Y Preferred Units in proportion to the positive balances of their Capital Accounts until those Capital Account balances have been reduced to zero. If Losses have been allocated to the holders of the Series A, B, C, D, E, X and Y Preferred Units pursuant to the preceding sentence, the first subsequent Profits shall be allocated to those preferred partners so as to recoup, in reverse order, the effects of the loss allocations.

(C) Upon liquidation of the Partnership or the interest of the holders of Series A, B, C, D, E, X or Y Preferred Units in the Partnership: (1) items of gross income or deduction shall first be allocated to the holders of Series A, B, C and D Preferred Units in a manner such that, immediately prior to such liquidation, the Capital Account balances of such holders shall equal the amount of their Liquidation Preferences, and (2) an amount of Profit or Loss shall then be allocated to the holders of Series E, X and Y Preferred Units in a manner such that, immediately prior to such liquidation, the Capital Account balances of such holders shall equal the amount of their Liquidation Preferences.”

Section 5. Optional Redemption. (a) **Right of Optional Redemption.** Except as otherwise provided herein, the Series E Preferred Units may not be redeemed prior to the fifth (5th) anniversary of the issuance date. On or after such date, the Partnership shall have the right to redeem the Series E Preferred Units, in whole (and not in part), at any time, upon not less than 30 nor more than 60 days written notice, at a redemption price, payable in cash, equal to the Liquidation Preference (the “**Series E Redemption Price**”). The Redemption Right given to Limited Partners in Section 8.6 of the Partnership Agreement shall not be available to the holders of the Series E Preferred Units and all references to Limited Partners in said Section 8.6 (and related provisions of the Partnership Agreement) shall not include holders of the Series E Preferred Units.

(b) **Procedures for Redemption.** (i) Notice of redemption will be (A) faxed, and (B) mailed by the Partnership, by certified mail, postage prepaid, not less than 30 nor more than 60 days prior to the redemption date, addressed to the respective holders of record of the Series E Preferred Units at their respective addresses as they appear on the records of the Partnership. No failure to give or defect in such notice shall affect the validity of the proceedings for the redemption of any Series E Preferred Units except as to the holder to whom such notice was defective or not given. In addition to any information required by law each such notice shall state: (m) the redemption date, (n) the Redemption Price, (o) the aggregate number of Series E Preferred Units to be redeemed, (p) as provided in Section 5(b)(ii) below, the place or places where evidence of the surrender of such Series E Preferred Units shall be delivered for payment of the Redemption Price, (q) that distributions on the Series E Preferred Units to be redeemed will cease to accumulate on such redemption date and (r) that payment of the Redemption Price will be made upon presentation of evidence of the surrender of such Series E Preferred Units as set forth in Section 5(b)(ii) below.

(ii) If the Partnership gives a notice of redemption in respect of Series E Preferred Units (which notice will be irrevocable) then, by 12:00 noon, New York City time, on the redemption date, the Partnership will deliver into escrow with an escrow agent acceptable to the Partnership and the holders of the Series E Preferred Units (the “**Escrow Agent**”) the Redemption Price and an executed Redemption Agreement, in the form attached hereto as **Exhibit A** (the “**Redemption Agreement**”), and an Amendment to the Agreement of Limited Partnership evidencing the Redemption, in the form attached hereto as **Exhibit B**. The holders of the Series E Preferred Units shall also, by 12:00 noon, New York City time, on the redemption date, deliver into escrow with the Escrow Agent an executed Redemption Agreement and an executed Amendment to the Agreement of Limited Partnership evidencing the Redemption. Upon delivery of all of the above-described items by both parties, Escrow Agent shall

release the Redemption Price to the holders of the Series E Preferred Units and the fully-executed Redemption Agreement and Amendment to Agreement of Limited Partnership to both parties. On and after the date of redemption, distributions will cease to accumulate on the Series E Preferred Units called for redemption, unless the Partnership defaults in the payment thereof. If any date fixed for redemption of Series E Preferred Units is not a Business Day, then payment of the Redemption Price payable on such date will be made on the next succeeding day that is a Business Day (and without any interest or other payment in respect of any such delay) except that, if such Business Day falls in the next calendar year, such payment will be made on the immediately preceding Business Day, in each case with the same force and effect as if made on such date fixed for redemption. If payment of the Redemption Price is improperly withheld or refused and not paid by the Partnership, distributions on such Series E Preferred Units will continue to accumulate from the original redemption date to the date of payment, in which case the actual payment date will be considered the date fixed for redemption for purposes of calculating the applicable Redemption Price.

Section 6. Voting Rights. (a) General. Holders of the Series E Preferred Units will not have any voting rights or right to consent to any matter requiring the consent or approval of the Limited Partners, except as set forth in Section 14.1 of the Partnership Agreement and in this Section 6. (Solely for purposes of Section 14.1 of the Partnership Agreement, each Series E Preferred Unit shall be treated as one Partnership Unit.) If and for so long as the General Partner holds any Series E Preferred Units, the General Partner shall not have any voting rights with respect to such Series E Preferred Units and such Series E Preferred Units shall not be counted in determining the number of such units outstanding for the purpose of determining whether the holders of such units have granted any approval called for hereunder.

(b) Certain Voting Rights. So long as any Series E Preferred Units remain outstanding, the Partnership shall not, without the affirmative vote of the holders of at least a majority of the Series E Preferred Units outstanding at the time:

(i) authorize or create, or increase the authorized or issued amount of, any class or series of Partnership Interests ranking senior to the Series E Preferred Units with respect to payment of distributions or rights upon liquidation, dissolution or winding-up or reclassify any Partnership Interests into any such Partnership Interest, or create, authorize or issue any obligations or security convertible into or evidencing the right to purchase any such Partnership Interests;

(ii) designate or create, or increase the authorized or issued amount of, any Parity Preferred Units or reclassify any authorized Partnership Interests into any such Parity Preferred Units, or create, authorize or issue any obligations or security convertible into or evidencing the right to purchase any such shares, but only to the extent such Parity Preferred Units are issued to an Affiliate of the Partnership on terms that differ from the terms of such series of Parity Preferred Units issued to the public or non-Affiliates of the Partnership (for purposes of this Section 6(b)(ii), an issuance to the General Partner shall not be treated as an issuance to an Affiliate of the Partnership to the extent the issuance of such Partnership Interests was to allow the General Partner to issue corresponding preferred stock to persons who are not Affiliates);

(iii) either (A) exchange shares, consolidate, merge into or with, or convey, transfer or lease its assets substantially as an entirety to, any corporation or other entity or (B) amend, alter or repeal the provisions of the Partnership Agreement, whether by merger, consolidation or otherwise, that would materially and adversely affect the powers, special rights, preferences, privileges or voting power of the Series E Preferred Units or the holders thereof; provided, however, that with respect to the occurrence of a share exchange, merger, consolidation or a sale or lease of all of the Partnership's assets as an entirety, so long as (1) the Partnership is the surviving entity and the Series E Preferred Units remain outstanding with the terms thereof unchanged, or (2) the resulting, surviving or transferee entity (I) is a partnership, limited liability company or other pass-through entity organized under the laws of any state, (II) is not taxable as a corporation for U.S. federal income tax purposes, and (III) substitutes the Series E Preferred Units for other interests in such entity having substantially the same terms and rights as the Series E Preferred Units, including with respect to distributions, voting rights and rights upon liquidation, dissolution or

winding-up, then the occurrence of any such event shall not be deemed to adversely affect such rights, privileges or voting powers of the holders of the Series E Preferred Units; and provided further that any increase in the amount of Partnership Interests or the creation or issuance of any other class or series of Partnership Interests, in each case ranking (y) junior to the Series E Preferred Units with respect to payment of distributions or the distribution of assets upon liquidation, dissolution or winding-up, or (z) on a parity to the Series E Preferred Units with respect to payment of distributions or the distribution of assets upon liquidation, dissolution or winding-up, to the extent such Partnership Interests are not issued to an Affiliate of the Partnership (an issuance to the General Partner shall not be treated as an issuance to an Affiliate of the Partnership to the extent the issuance of such Partnership Interests was to allow the General Partner to issue corresponding preferred stock to persons who are not Affiliates of the Partnership) such issuance shall not be deemed to materially and adversely affect such rights, preferences, privileges or voting powers; or

- (iv) increase the authorized or issued amount of Series E Preferred Units.

In addition to the foregoing, the Partnership will not (x) enter into any contract, mortgage, loan or other agreement that prohibits or restricts, or has the effect of prohibiting or restricting, the ability of a holder of the Preferred Units to exercise its rights set forth herein to effect in full an exchange or redemption pursuant to Section 8, below, except with the written consent of such holder; or (y) amend, alter, or repeal or waive Sections 7.6 or 11.3(f) of the Partnership Agreement without the affirmative vote of at least a majority of the Series E Preferred Units outstanding at the time.

Section 7. Transfer Restrictions. The holders of Series E Preferred Units shall be subject to all of the provisions of Section 11 of the Partnership Agreement except Section 11.3(b), as modified by this Section 7. Except as otherwise provided, if the General Partner's consent to a transfer of Series E Preferred Units is required by Section 11.3 of the Partnership Agreement, the General Partner agrees not to unreasonably withhold that consent. Subject to the consent of the General Partner, which shall not be unreasonably withheld or delayed, the Series E Preferred Units may be transferred to a maximum of five (5) persons. At no time shall the number of holders of the Series E Preferred Units exceed five.

Section 8. Exchange Rights. (a) Right to Exchange. (i) All, but not less than all, of the Series E Preferred Units will be exchangeable at any time on or after the tenth (10th) anniversary of the date of issuance, at the option of the Partnership or upon the affirmative vote of the holders of a majority of the outstanding Series E Preferred Units, for authorized but previously unissued shares of 9¼% Series E Cumulative Redeemable Preferred Stock of the General Partner (the "**Series E Preferred Stock**") at an exchange rate of one share of Series E Preferred Stock for one Series E Preferred Unit, subject to adjustment as described below (the "**Series E Exchange Price**"); provided that all, but not less than all, of the Series E Preferred Units will become exchangeable for Series E Preferred Stock at any time upon the affirmative vote of the holders of a majority of the outstanding Series E Preferred Units (x) if at any time full distributions shall not have been timely made on any Series E Preferred Unit with respect to six (6) prior quarterly distribution periods, whether or not consecutive; provided, however, that a distribution in respect of Series E Preferred Units shall be considered timely made if made within two (2) Business Days after the applicable Series E Preferred Units Distribution Payment Date if at the time of such late payment there shall not be any prior quarterly distribution periods in respect of which full distributions were not timely made, (y) upon receipt by a holder or holders of Series E Preferred Units of (1) notice from the General Partner that the General Partner or the Partnership has become aware of facts that will or likely will cause the Partnership to become a PTP or takes the position that the Partnership is, or upon consummation of an identified event in the immediate future will be, a PTP, and (2) an opinion rendered by an outside nationally recognized independent counsel familiar with such matters addressed to a holder or holders of Series E Preferred Units, that the Partnership is or likely is, or upon the occurrence of a defined event in the immediate future will be or likely will be a PTP, or (z) at any time (1) a holder of Series E Preferred Units concludes (in the reasonable judgment of the holder) that it is imminent that the Partnership will not or likely will not satisfy the income and asset tests of Section 856 of the Internal Revenue Code of 1986, as amended (the "**Code**") for a taxable year if the Partnership were a real estate investment trust within the meaning of the Code, (2) such holder delivers to the General Partner an opinion of nationally recognized

independent counsel to the effect that it is imminent that the Partnership will not or likely will not satisfy the income and asset tests of Section 856 of the Code for a taxable year if the Partnership were a real estate investment trust within the meaning of the Code, and (3) such failure would create a meaningful risk that a holder of the Series E Preferred Units would fail to maintain its qualification as a real estate investment trust.

In addition to and not in limitation of the foregoing, all, but not less than all, of the Series E Preferred Units may be exchanged (regardless of whether held by GSEP 2001 Realty Corp. (“**Contributor**”)) upon the affirmative vote of the holders of a majority of the outstanding Series E Preferred Units for Series E Preferred Stock (but only if the exchange in whole may be accomplished consistently with the ownership limitations set forth under the Article IV of the Charter of the General Partner, taking into account exceptions thereto) if at any time (i) such holders conclude based on results or projected results that there exists (in the reasonable judgment of such holders) an imminent and substantial risk that the Series E Preferred Units represent or will represent more than 19.5% of the total profits of or capital interests in the Partnership for a taxable year, (ii) such holders deliver to the General Partner an opinion of nationally recognized independent counsel, reasonably acceptable to the General Partner, to the effect that there is a substantial risk that its interest in the Partnership does not or will not satisfy the 19.5% limit, and (iii) the General Partner agrees with the conclusions referred to in clauses (i) and (ii) of this sentence, such agreement not to be unreasonably withheld.

(ii) Notwithstanding anything to the contrary set forth in Section 8(a)(i), if an Exchange Notice (as hereinafter defined) has been delivered to the General Partner, then the General Partner may, at its option, elect to redeem or cause the Partnership to redeem all (but not a portion) of the outstanding Series E Preferred Units for cash in an amount equal to the Liquidation Preference per Series E Preferred Unit. The General Partner may exercise its option to redeem the Series E Preferred Units for cash pursuant to this Section 8(a)(ii) by giving each holder of record of Series E Preferred Units notice of its election to redeem for cash, within five (5) Business Days after receipt of the Exchange Notice, by (m) fax, and (n) registered mail, postage paid at the address of each holder as it may appear on the records of the Partnership stating (A) the redemption date, which shall be no later than sixty (60) days following the receipt of the Exchange Notice, (B) the redemption price, (C) the place or places where the Series E Preferred Units are to be surrendered for payment of the redemption price, (D) that distributions on the Series E Preferred Units will cease to accrue on such redemption date; (E) that payment of the redemption price will be made upon presentation and surrender of the Series E Preferred Units and (F) the aggregate number of Series E Preferred Units to be redeemed.

(iii) If an exchange of Series E Preferred Units pursuant to Section 8(a)(i) would violate the provisions on ownership limitation of the General Partner set forth in Article IV of the Charter of the General Partner (taking into account exceptions thereto) with respect to the Series E Preferred Stock the General Partner shall give written notice thereof to each holder of record of Series E Preferred Units, within five (5) Business Days following receipt of the Exchange Notice, by (m) fax, and (n) registered mail, postage prepaid, at the address of each such holder set forth in the records of the Partnership. In such event, each holder of Series E Preferred Units shall be entitled to exchange, pursuant to the provisions of Section 8(b) a number of Series E Preferred Units which would comply with the provisions on the ownership limitation of the General Partner set forth in such Article IV of the Charter of the General Partner and any Series E Preferred Units not so exchanged (the “**Excess Units**”) shall be redeemed by the Partnership for cash in an amount equal to the Liquidation Preference. The written notice of the General Partner shall state (A) the number of Excess Units held by such holder, (B) the redemption price of the Excess Units, (C) the date on which such Excess Units shall be redeemed, which date shall be no later than sixty (60) days following the receipt of the Exchange Notice, (D) the place or places where such Excess Units are to be surrendered for payment of the Redemption Price, (E) that distributions on the Excess Units will cease to accrue on such redemption date, and (F) that payment of the redemption price will be made upon presentation and surrender of such Excess Units. If an exchange would result in Excess Units, as a condition to such exchange, each holder of such units agrees to provide representations and covenants reasonably requested by the General Partner relating to (1) the widely held nature of the interests in such holder, sufficient to assure the General Partner that the holder’s ownership of stock of the General Partner (without regard to the limits described above) will not cause any Person (as such term is defined in the Charter of the General Partner) to own stock of the General Partner in an amount that would cause such Person

not to comply with the provisions of the ownership limitation of the General Partner set forth in such Article IV of the Charter of the General Partner; and (2) to the extent such holder can so represent and covenant without obtaining information from its owners, the holder's ownership of tenants of the Partnership and its affiliates.

To the extent the General Partner would not be able to pay the cash set forth above in exchange for the Excess Units, and to the extent consistent with the Charter, the General Partner agrees that it will grant to the holders of the Series E Preferred Units exceptions to the Beneficial Ownership Limit and Constructive Ownership Limit set forth in the Charter sufficient to allow such holders to exchange all of their Series E Preferred Units for Series E Preferred Stock, provided such holders furnish to the General Partner representations acceptable to the General Partner in its sole and absolute discretion which assure the General Partner that such exceptions will not jeopardize the General Partner's tax status as a REIT for purposes of federal and applicable state law.

Notwithstanding any provision of the Agreement to the contrary, no holder of Series E Preferred Units shall be entitled to effect an exchange of Series E Preferred Units for Series E Preferred Stock to the extent that the ownership or right to acquire such shares would cause the holder or any other Person or, in the opinion of counsel selected by the General Partner, may cause the holder or any other Person, to violate the restrictions on ownership and transfer of Series E Preferred Stock set forth in the Charter (taking into account exceptions thereto). To the extent any such attempted exchange for Series E Preferred Stock would be in violation of the previous sentence, it shall be *void ab initio* and such holder of Series E Preferred Units shall not acquire any rights or economic interest in the Series E Preferred Stock otherwise issuable upon such exchange.

(iv) The redemption of Series E Preferred Units described in Sections 8(a)(ii) and 8(a)(iii) shall be subject to the provisions of Sections 5(b)(i) and 5(b)(ii); provided, however, that the term "redemption price" in such Section shall be read to mean the Liquidation Preference per Series E Preferred Unit being redeemed.

(b) Procedure for Exchange. (i) Any exchange shall be exercised pursuant to a notice of exchange (the "**Exchange Notice**") delivered to the General Partner by the holder who is exercising such exchange right, by (a) fax and (b) by certified mail postage prepaid. The exchange of Series E Preferred Units may be effected after the fifth (5th) Business Day following receipt by the General Partner of the Exchange Notice by delivering certificates if any, representing such Series E Preferred Units to be exchanged together with, if applicable, written notice of exchange and a proper assignment of such Series E Preferred Units to the office of the General Partner maintained for such purpose. Currently, such office is c/o PS Business Parks, Inc., 701 Western Avenue, Glendale, California 91201, Attention: Jack E. Corrigan. Each exchange will be deemed to have been effected immediately prior to the close of business on the date on which such Series E Preferred Units to be exchanged (together with all required documentation) shall have been surrendered and notice shall have been received by the General Partner as aforesaid and the Series E Exchange Price shall have been paid. Any Series E Preferred Stock issued pursuant to this Section 8 shall be delivered, as promptly as practicable, as shares which are duly authorized, validly issued, fully paid and nonassessable, free of pledge, lien, encumbrance or restriction other than those provided in the Charter, the Bylaws of the General Partner, the Securities Act of 1933, as amended, and relevant state securities or blue sky laws.

(ii) In the event of an exchange of Series E Preferred Units for shares of Series E Preferred Stock, an amount equal to the accrued and unpaid Priority Return, whether or not declared, to the date of exchange on any Series E Preferred Units tendered for exchange shall (a) accrue on the shares of the Series E Preferred Stock into which such Series E Preferred Units are exchanged, and (b) continue to accrue on such Series E Preferred Units, which shall remain outstanding following such exchange, with the General Partner as the holder of such Series E Preferred Units. Notwithstanding anything to the contrary set forth herein, in no event shall a holder of a Series E Preferred Unit that was validly exchanged into Series E Preferred Stock pursuant to this section (other than the General Partner now holding such Series E Preferred Unit), receive a distribution from the Partnership, if such holder, after exchange, is entitled to receive a distribution from the General Partner with respect to the share of Series E Preferred Stock for which such Series E Preferred Unit was exchanged or redeemed.

(iii) Fractional shares of Series E Preferred Stock are not to be issued upon exchange but, in lieu thereof, the General Partner will pay a cash adjustment based upon the fair market value of the Series E Preferred Stock on the day prior to the exchange date as determined in good faith by the Board of Directors of the General Partner.

(c) Adjustment of Exchange Price. (i) The Exchange Price is subject to adjustment upon certain events, including, (a) subdivisions, combinations and reclassification of the Series E Preferred Stock, and (b) distributions to all holders of Series E Preferred Stock of evidences of indebtedness of the General Partner or assets (including securities, but excluding dividends and distributions paid in cash out of equity applicable to Series E Preferred Stock).

(ii) In case the General Partner shall be a party to any transaction (including, without limitation, a merger, consolidation, statutory share exchange, tender offer for all or substantially all of the General Partner's capital stock or sale of all or substantially all of the General Partner's assets), in each case as a result of which the Series E Preferred Stock will be converted into the right to receive shares of capital stock, other securities or other property (including cash or any combination thereof), each Series E Preferred Unit will thereafter be exchangeable into the kind and amount of shares of capital stock and other securities and property receivable (including cash or any combination thereof) upon the consummation of such transaction by a holder of that number of shares of Series E Preferred Stock or fraction thereof into which one Series E Preferred Unit was exchangeable immediately prior to such transaction. The General Partner may not become a party to any such transaction unless the terms thereof are consistent with the foregoing. In addition, so long as a holder of Series E Preferred Units or any of its permitted successors or assigns, hold any Series E Preferred Units, as the case may be, the General Partner shall not, without the affirmative vote of the holders of at least a majority of the Series E Preferred Units outstanding at the time: (a) designate or create, or increase the authorized or issued amount of, any class or series of shares ranking senior to the Series E Preferred Stock with respect to the payment of distributions or rights upon liquidation, dissolution or winding-up or reclassify any authorized shares of the General Partner into any such shares, or create, authorize or issue any obligations or securities convertible into or evidencing the right to purchase any such shares; or (b) amend, alter or repeal the provisions of the Charter or bylaws of the General Partner, whether by merger, consolidation or otherwise, that would materially and adversely affect the powers, special rights, preferences, privileges or voting power of the Series E Preferred Stock or the holders thereof; provided, however, that any increase in the amount of authorized Preferred Shares or the creation or issuance of any other series or class of Preferred Shares, or any increase in the amount of authorized shares of each class or series, in each case ranking either (1) junior to the Series E Preferred Stock with respect to the payment of distributions and the distribution of assets upon liquidation, dissolution or winding-up, or (2) on a parity with the Series E Preferred Stock with respect to the payment of distributions and the distribution of assets upon liquidation, dissolution or winding-up shall not be deemed to materially and adversely affect such rights, preferences, privileges or voting powers. In the event of a conflict between the provisions of this Section 8(c)(ii) and any provision of the Partnership Agreement, the provisions of this Section 8(c)(ii) shall control.

Section 9. No Conversion Rights. Except as set forth in Section 8, the holders of the Series E Preferred Units shall not have any rights to convert such units into shares of any other class or series of stock or into any other securities of, or interest in, the Partnership.

Section 10. No Sinking Fund. No sinking fund shall be established for the retirement or redemption of Series E Preferred Units.

Section 11. Exhibit A to Partnership Agreement. In order to duly reflect the issuance of the Series E Preferred Units provided for herein, the Partnership Agreement is hereby further amended pursuant to Section 12.3 thereof by deleting Exhibit A thereto and replacing such Exhibit A with Exhibit C attached hereto.

Section 12. Inconsistent Provisions. Nothing to the contrary contained in the Partnership Agreement shall limit any of the rights or obligations set forth in this Amendment.

IN WITNESS WHEREOF this Amendment has been executed as of the date first above written.

PS BUSINESS PARKS, INC.

By: /s/ Jack Corrigan

Name: Jack E. Corrigan

Title: Chief Financial Officer

PS BUSINESS PARKS, INC.

EXHIBIT 12:

STATEMENT RE: COMPUTATION OF RATIO OF EARNINGS TO FIXED CHARGES

	Nine Months Ended September 30,	
	2001	2000
Net income	\$ 37,144,000	\$ 33,726,000
Minority interest	19,743,000	18,391,000
Interest expense	932,000	1,246,000
Earnings available to cover fixed charges	<u>\$ 57,819,000</u>	<u>\$ 53,363,000</u>
Fixed charges (1)	\$ 1,933,000	\$ 2,242,000
Preferred distributions	15,710,000	12,814,000
Combined fixed charges and preferred distributions	<u>\$ 17,643,000</u>	<u>\$ 15,056,000</u>
Ratio of earnings to fixed charges	<u>29.91</u>	<u>23.80</u>
Ratio of earnings to combined fixed charges and preferred distributions	<u>3.28</u>	<u>3.54</u>

	Years Ended December 31,				
	2000	1999	1998	1997	1996
Net income.....	\$51,181,000	\$41,255,000	\$29,400,000	\$ 3,836,000	\$ 519,000
Minority interest	26,741,000	16,049,000	11,208,000	8,566,000	-
Interest expense	1,481,000	3,153,000	2,361,000	1,000	-
Earnings available to cover fixed charges	<u>\$79,403,000</u>	<u>\$60,457,000</u>	<u>\$42,969,000</u>	<u>\$12,403,000</u>	<u>\$ 519,000</u>
Fixed charges (1)	\$ 2,896,000	\$ 4,142,000	\$ 2,629,000	\$ 1,000	\$ -
Preferred distributions	17,273,000	7,562,000	-	-	-
Combined fixed charges and preferred distributions	<u>\$20,169,000</u>	<u>\$11,704,000</u>	<u>\$ 2,629,000</u>	<u>\$ 1,000</u>	<u>\$ -</u>
Ratio of earnings to fixed charges	<u>27.42</u>	<u>14.60</u>	<u>16.34</u>	<u>12,403</u>	<u>N/A</u>
Ratio of earnings to combined fixed charges and preferred distributions.....	<u>3.94</u>	<u>5.17</u>	<u>16.34</u>	<u>12,403</u>	<u>N/A</u>

(1) Fixed charges include interest expense plus capitalized interest.

PS BUSINESS PARKS, INC.
EXHIBIT 12
STATEMENT RE: COMPUTATION OF RATIO OF EARNINGS TO FIXED CHARGES

Supplemental disclosure of Ratio of Funds from Operations (“FFO”) to fixed charges:

	Nine Months Ended September 30,	
	2001	2000
FFO.....	\$ 70,049,000	\$ 63,819,000
Interest expense	932,000	1,246,000
Minority interest in income – preferred units.....	9,696,000	8,998,000
Preferred dividends.....	6,014,000	3,816,000
Adjusted FFO available to cover fixed charges.....	<u>\$ 86,691,000</u>	<u>\$ 77,879,000</u>
Fixed charges (1).....	\$ 1,933,000	\$ 2,242,000
Preferred distributions	15,710,000	12,814,000
Combined fixed charges and preferred distributions	<u>\$ 17,643,000</u>	<u>\$ 15,056,000</u>
Ratio of FFO to fixed charges	<u>44.85</u>	<u>34.74</u>
Ratio of FFO to combined fixed charges and preferred distributions	<u>4.91</u>	<u>5.17</u>

	Years Ended December 31,				
	2000	1999	1998	1997	1996
FFO.....	\$ 85,977,000	\$ 76,353,000	\$ 57,430,000	\$ 17,597,000	\$ 303,000
Interest expense	1,481,000	3,153,000	2,361,000	1,000	-
Minority interest in income – preferred units.....	12,185,000	4,156,000	-	-	-
Preferred dividends.....	5,088,000	3,406,000	-	-	-
Adjusted FFO available to cover fixed charges	<u>\$104,731,000</u>	<u>\$ 87,068,000</u>	<u>\$ 59,791,000</u>	<u>\$ 17,598,000</u>	<u>\$ 303,000</u>
Fixed charges (1).....	\$ 2,896,000	\$ 4,142,000	\$ 2,629,000	\$ 1,000	\$ -
Preferred distributions	17,273,000	7,562,000	-	-	-
Combined fixed charges and preferred distributions	<u>\$ 20,169,000</u>	<u>\$ 11,704,000</u>	<u>\$ 2,629,000</u>	<u>\$ 1,000</u>	<u>\$ -</u>
Ratio of FFO to fixed charges	<u>36.16</u>	<u>21.02</u>	<u>22.74</u>	<u>17,598</u>	<u>N/A</u>
Ratio of FFO to combined fixed charges and preferred distributions.....	<u>5.19</u>	<u>7.44</u>	<u>22.74</u>	<u>17,598</u>	<u>N/A</u>

(1) Fixed charges include interest expense plus capitalized interest.