WELLS REAL ESTATE INVESTMENT TRUST II INC
Form 424B3
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WELLS REAL ESTATE INVESTMENT TRUST II, INC.

SUPPLEMENT NO. 6 DATED MARCH 31, 2006

TO THE PROSPECTUS DATED NOVEMBER 10, 2005

This document supplements, and should be read in conjunction with, our prospectus dated November 10, 2005 relating to our follow-on offering of 300,600,000 shares of common stock, as supplemented by supplement no. 1 dated November 16, 2005, supplement no. 2 dated December 9, 2005, supplement no. 3 dated December 21, 2005, supplement no. 4 dated December 28, 2005 and supplement no. 5 dated December 29, 2005. Capitalized terms used in this supplement have the same meanings as set forth in the prospectus. The purpose of this supplement is to disclose:

- the status of our public offerings;
- information regarding our indebtedness;
- revisions to our share redemption program, which revisions are primarily designed to enhance an investor s ability to redeem shares upon his or her death;
- changes to our Corporate Governance Guidelines designed to improve your ability to influence the composition of the board of directors in an uncontested election of directors;
- Management s Discussion and Analysis of Financial Condition and Results of Operations similar to that filed in our Annual Report on Form 10-K for the year ended December 31, 2005, filed on March 28, 2006;
- our audited financial statements as of December 31, 2005 and for the year ended December 31, 2005; and
- audited financial statements of property acquisitions since November 4, 2005, as reported in supplements no. 1 through 5.

Status of Our Public Offerings

We commenced our initial public offering of 785 million shares of common stock on December 1, 2003, which consisted of a 600 million-share primary offering and a 185 million-share offering under our dividend reinvestment plan. We stopped making offers under the primary offering on November 26, 2005. We received aggregate gross offering proceeds of approximately $2.0 billion from the sale of approximately 197.0 million shares in our initial public offering.

On November 10, 2005, we commenced our follow-on offering of 300.6 million shares of common stock. Of these shares, we are offering 300 million shares in a primary offering and 0.6 million shares under our dividend reinvestment plan. As of March 24, 2006, we had received gross offering proceeds of approximately $209.3 million from the sale of approximately 20.9 million shares in our follow-on offering.

As of March 24, 2006, we had received aggregate gross offering proceeds of approximately $2.2 billion from the sale of approximately 217.9 million shares in our public offerings. After incurring approximately $43.5 million in acquisition fees, approximately $205.2 million in selling commissions and dealer manager fees, approximately $34.7 million in other organization and offering expenses, and funding common stock redemptions of approximately $21.0 million pursuant to the share redemption program, as of March 24, 2006, we had raised aggregate net offering proceeds available for investment in properties of approximately $1.9 billion, all of which had been invested in real estate properties.

Indebtedness

As of March 24, 2006, our leverage ratio, that is, the ratio of total debt to total purchase price of real estate assets plus cash and cash equivalents, was approximately 26.3%. As of March 24, 2006, total indebtedness was

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approximately $675.3 million, which consisted of fixed-rate mortgages on certain properties of approximately $471.2 million and approximately $195.0 outstanding under our $400.0 million credit facility and $9.1 million outstanding under our construction line of credit. Based on the value of our borrowing-base properties, we had approximately $195.8 million in remaining capacity under our $400.0 million credit facility, of which $9.2 million was pledged in the form of letters of credit for future tenant improvements and leasing costs.

Revised Share Redemption Program

Our board of directors has approved revisions to the share redemption program, which enables stockholders to sell their shares to us, subject to the limitations described below. The revisions, which will go into effect April 27, 2006, relate to the total amount of redemptions we can make if the redemption is sought upon the death or qualifying disability of a stockholder and should increase the number of shares we can redeem upon the request of the heirs of our stockholders. Set forth below is a full description of our revised share redemption program.

For Ordinary Redemptions (those that do not occur within two years of death or qualifying disability), the initial price at which we will repurchase a share under the share redemption program is 91% of the price at which we sold the share. We will pay $9.10 to redeem a share issued at $10.00. This initial redemption price will remain fixed until three years after we complete our offering stage. We define the completion of our offering stage to be upon the termination of our first public equity offering that is followed by a one-year period in which we do not engage in another public equity offering. (For purposes of this definition, we do not consider a public equity offering to include offerings on behalf of selling stockholders or offerings related to a dividend reinvestment plan, employee benefit plan or the redemption of interests in the Wells operating partnership).

Three years after we complete our offering stage, the redemption price for Ordinary Redemptions will equal 95% of the estimated per share value of our shares, as estimated by our advisor or another firm chosen for that purpose. We will report this redemption price in the annual report and three quarterly reports that we publicly file with the SEC.

There are several limitations on our ability to redeem shares:

- We will not make an Ordinary Redemption until one year after the issuance of the share to be redeemed.

- We will not redeem shares on any redemption date to the extent that such redemptions would cause the amount paid for Ordinary Redemptions since the beginning of the then-current calendar year to exceed 50% of the net proceeds from the sale of shares under our dividend reinvestment plan during such period.

- We will limit Ordinary Redemptions and those in connection with a qualifying disability (as defined below) so that the aggregate of such redemptions during any calendar year do not exceed 100% of the net proceeds from our dividend reinvestment plan during the calendar year.

- We will limit all redemptions (including those upon the death or qualifying disability of a stockholder) during any calendar year to no more than 5% of the weighted-average number of shares outstanding in the prior calendar year.

Subject to the limitations described above, we will redeem shares on the last business day of each month. Requests for redemption must be received at least five business days before a month-end redemption date in order for us to repurchase the shares that month. If we cannot purchase all shares presented for redemption, we will honor redemption requests at the applicable month-end on a pro rata basis. We will deviate from pro rata purchases in two minor ways: (i) if a pro rata redemption would result in you owning less than half of the minimum amounts required by applicable state law, then we would redeem all of your shares; and (ii) if a pro rata redemption would result in a you owning more than half but less than all of the amounts required by applicable state law, then we would not redeem any shares that would reduce your holdings below the minimum amount. In the event that you seek the redemption of all of your shares, there is no holding-period requirement for shares purchased pursuant to our dividend reinvestment plan.

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If we do not completely satisfy your redemption request at month-end because the request was not received in time or because of the restrictions on the number of shares we can redeem under the program, we will treat the unsatisfied portion of the redemption request as a request for redemption in the following month unless you withdraw the request before the next date for redemptions. You may withdraw a redemption request upon written notice to us at the address below before the date for redemption.

In several respects we treat redemptions sought within two years of a stockholder s death or qualifying disability (as defined below) differently from Ordinary Redemptions. First, there is no requirement that the shares be outstanding for at least a year before being redeemed. Second, the redemption price equals 100% of the price at which we sold the share until three years after we complete our offering stage. At that time, the redemption price will be 100% of the price at which we sold the share or 100% of the estimate of our per share value, whichever is greater. Finally, there are the differences in the limitations imposed on different types of redemptions as described in the bullets above.

In order for a disability to entitle a stockholder to the special redemption terms described above (a qualifying disability), (1) the stockholder must receive a determination of disability based upon a physical or mental condition or impairment arising after the date the stockholder acquired the shares to be redeemed, and (2) such determination of disability must be made by the governmental agency responsible for reviewing the disability retirement benefits that the stockholder could be eligible to receive (the applicable governmental agency). The applicable governmental agencies are limited to the following: (i) if the stockholder paid Social Security taxes and therefore could be eligible to receive Social Security disability benefits, then the applicable governmental agency is the Social Security Administration; (ii) if the stockholder did not pay Social Security benefits and therefore could not be eligible to receive Social Security disability benefits, but the stockholder could be eligible to receive disability benefits under the Civil Service Retirement System (CSRS), then the applicable governmental agency is the U.S. Office of Personnel Management; or (iii) if the stockholder did not pay Social Security taxes and therefore could not be eligible to receive Social Security benefits but suffered a disability that resulted in the stockholder s discharge from military service under conditions that were other than dishonorable and therefore could be eligible to receive military disability benefits, then the applicable governmental agency is the Veteran s Administration.

Disability determinations by governmental agencies for purposes other than those listed above, including but not limited to worker s compensation insurance, administration or enforcement of the Rehabilitation Act or Americans with Disabilities Act or waiver of insurance premiums will not entitle a stockholder to the special redemption terms described above. Redemption requests following an award by the applicable governmental agency of disability benefits must be accompanied by: (1) the investor s initial application for disability benefits and (2) a Social Security Administration Notice of Award, a U.S. Office of Personnel Management determination of disability under CSRS, a Veteran s Administration record of disability-related discharge or such other documentation issued by the applicable governmental agency which we deem acceptable and demonstrates an award of the disability benefits.

We understand that the following disabilities do not entitle a worker to Social Security disability benefits:

- disabilities occurring after the legal retirement age,
- temporary disabilities and
- disabilities that do not render a worker incapable of performing substantial gainful activity.

Therefore, such disabilities will not qualify for the special redemption terms except in the limited circumstances when the investor is awarded disability benefits by the other applicable governmental agencies described above.

A stockholder that is a trust may only redeem on the terms available in connection with the death or disability of a stockholder if the deceased or disabled was the sole beneficiary of the trust or if the only other beneficiary of the trust was the spouse of the deceased or disabled.

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Qualifying stockholders who desire to redeem their shares must give written notice to Wells Investment Securities, our dealer manager for our ongoing public offering, at 6200 The Corners Parkway, Suite 250, Norcross, Georgia 30092, ATTN: Investor Services. Wells Investment Securities is responsible for all services to be performed in connection with the Share Redemption Plan, although it has outsourced clerical duties to our advisor.

Our board of directors may amend, suspend or terminate the share redemption program upon 30 days notice. We will notify you of such developments (i) in the annual or quarterly reports mentioned above or (ii) by means of a separate mailing, accompanied by disclosure in a current or periodic report under the Securities Exchange Act of 1934. During a public offering, we will also include this information in a prospectus supplement or post-effective amendment to the registration statement, as then required under federal securities laws.

Our share redemption program only provides stockholders a limited ability to redeem shares for cash until a secondary market develops for the shares, at which time the program will terminate. No such market presently exists, and we cannot assure you that any market for your shares will ever develop.

Amended Corporate Governance Guidelines

Set forth below is a description of changes we have made to our Corporate Governance Guidelines relating to the election of our directors. A copy of our Corporate Governance Guidelines is available on our website at www.wellsref.com/investors/governance_docs.html.

Our directors are elected by a plurality of the votes cast. Under this voting standard, the director nominees with the most votes are elected for the board seats to be filled. In uncontested elections, the number of nominees equals the number of board seats to be filled; therefore, in uncontested elections, a nominee need only receive a single for vote to be elected. In uncontested elections, abstentions and withhold votes should have no effect on the outcome of the election (although they do count toward the establishment of a quorum).

In order to enhance your ability to influence the composition of the board of directors in an uncontested election, we have recently amended our Corporate Governance Guidelines to require each candidate nominated by the board of directors to agree to offer to resign should he or she receive fewer for votes than withhold votes in an uncontested election. If a director must offer to resign because of withhold vote totals, the conflicts committee of our board of directors must accept or reject the offer of resignation within 90 days following certification of the stockholder vote. If the conflicts committee accepts the offer, then the resignation will be effective upon acceptance. If the conflicts committee rejects an offer, it must disclose the reasons for doing so.

Any director who tenders his or her resignation pursuant to this provision of our Corporate Governance Guidelines may not participate in any conflicts committee action regarding whether to accept his or her offer of resignation or whether to accept any other director s resignation. However, if the non-participation of resigning directors would leave fewer than three directors participating in the decision, then all conflicts committee members may participate other than the director whose resignation is at issue.

The offer of resignation may also be accepted at a stockholder meeting duly called for the express purpose of accepting such resignation and electing a successor to fill the vacancy created thereby. Unless previously accepted by the conflicts committee, such resignation will be effective immediately prior to the stockholders election of a successor at such meeting.

Management s Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis should be read in conjunction with our accompanying consolidated financial statements and notes thereto. This discussion contains forward-looking statements, which can be identified with the use of forward-looking terminology such as may, will, intend, or similar words. Actual results may differ from those described in forward-looking statements. For a discussion of the factors that could cause actual results to differ from those anticipated, see Risk Factors in the prospectus.

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Overview

We were formed on July 3, 2003 to acquire and operate a diversified portfolio of commercial real estate primarily consisting of high-quality, income-producing office and industrial properties leased to creditworthy entities that are located in major metropolitan areas throughout the United States. We have no paid employees and are externally advised and managed by Wells Capital and Wells Management. We have elected to be taxed as a real estate investment trust for federal income tax purposes.

Prior to commencing our initial public offering on December 1, 2003, we had approximately $200,000 in assets and no real estate operations. Following the receipt and acceptance of subscriptions for the minimum offering of $2,500,000 in our initial public offering on January 22, 2004, we began acquiring real estate assets. Thus, our results of operations for the years ended December 31, 2005 and 2004 reflect growing operational revenues and expenses resulting from the acquisition of properties, fluctuations in interest expense resulting from the use of varying levels of short-term and long-term debt financing for such acquisitions, and general and administrative expenses, which have declined as a percentage of total revenues for 2005, as compared to 2004, commensurate with the operational growth of the enterprise.

During 2004, we raised approximately $792.0 million through the issuance of common stock and acquired an interest in 18 properties for an aggregate purchase price of approximately $1.0 billion. During 2005, we raised approximately $1.2 billion through the issuance of common stock and acquired an interest in 21 properties for an aggregate purchase price of approximately $1.5 billion. To purchase these assets, we used net equity proceeds and indebtedness. As of December 31, 2005 and 2004, our borrowings totaled approximately $832.4 million and $350.5 million, respectively.

General Economic Conditions and Real Estate Market Commentary

Management reviews a number of economic forecasts and market commentaries in order to evaluate general economic conditions and formulate a view of the current environment s effect on the real estate markets in which we operate.

The U.S. economy experienced a moderate rate of growth at the end of 2005. Actual gross domestic product (GDP) grew at an annual rate of 1.1% for the fourth quarter of 2005, which declined from an annual growth rate of 4.1% for the third quarter of 2005. The decline in the rate of economic growth for the fourth quarter of 2005 is primarily attributable to corresponding declines in consumer and federal government spending, and net exports. Annual GDP growth is projected to remain in the range of three percent during 2006. The economy is anticipated to grow at a slower pace during 2006 due to rising energy prices and growing trade deficits. However, the rate of job growth relative to the labor force is expected to continue to improve in 2006, partially due to a shrinking labor force.

The U.S. office real estate market has shown some improvement over the past two years. The continued improvement of the overall economy is having a positive impact on office real estate fundamentals in certain markets. Office employment has grown moderately over the last year, and the pace is anticipated to accelerate in future years. The source of the future growth is projected to come predominately from the service sector. The U.S. office vacancy rate declined from approximately 14.1% for the third quarter of 2005 to approximately 13.6% for the fourth quarter of 2005. Positive absorption and low levels of new construction are projected to lead to a further reduction in vacancy in 2006. Increased tenant demand and steady absorption is expected to continue to contribute to positive rental rate growth in certain markets. Many markets are expected to move from the recovery cycle to the expansion cycle during 2006. The strength of office real estate market fundamentals will vary by location, as market conditions and real estate fundamentals differ based on geographic region, metropolitan area, and submarket.

The real estate capital transactions market remains healthy and exceedingly liquid. The national transaction volume has grown at an average annual rate of over 50% during the past two years. Cap rates, or first-year returns on real estate investments, remain low and are likely to remain flat through 2006. The spread between average cap rates and 10-year U.S. Treasuries remained relatively stable in 2005. We believe that, absent a significant movement in interest rates or a significant decrease in capital flows into the real estate market, cap rates will remain at or near their current levels.

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Impact of Economic Conditions on our Portfolio

The level of cap rates is reflective of current market conditions and, as a result, is a major factor affecting the purchase prices of properties in which we invest. While some of the factors noted above indicate that future cap rates could remain stable, the extent to which our portfolio may be affected by future cap rate levels is dependent upon the extent of our future fundraising and investing activities. We expect to continue to raise equity proceeds from the sale of our common stock at a similar rate to the fourth quarter of 2005 and anticipate cap rates to remain stable; as such, we do not anticipate that our portfolio will be significantly impacted by the market conditions described above in the near-term.

Liquidity and Capital Resources

Overview

From January 2004 through December 2005, we raised significant funds through the sale of our common stock under our public offerings. Proceeds from these sales of common stock, net of offering costs and other expenses, were used primarily to fund the acquisition of real properties and certain capital improvements identified at the time of acquisition. We anticipate receiving proceeds from the sale of our common stock under our follow-on offering in the future, and investing such proceeds in future acquisitions of real properties. We also anticipate receiving proceeds from the sale of our common stock under our dividend reinvestment plan in the future, and using a significant portion of such proceeds to fund redemptions of our common stock under our share redemption program. We expect that our primary source of future operating cash flows will be cash generated from the operations of the properties currently in our portfolio and those to be acquired in the future. The amount of future dividends to be paid to our stockholders will be largely dependent upon the amount of cash generated from our operating activities, our expectations of future cash flows, and our determination of near-term cash needs for capital improvements, tenant re-leasing, redemptions of our common stock, and debt repayments.

The competition to acquire high-quality commercial office properties remains high. In addition, we continue to raise capital at a rate comparable to the fourth quarter of 2005. As such, due to timing differences in acquiring properties, as compared to raising capital, and in making operating payments, as compared to collecting operating receipts, we may periodically be required to borrow funds on a short-term basis to meet our dividend payment schedule. Our primary focus is to continue to maintain the quality of our portfolio. Accordingly, in this intensely competitive environment, we may opt to lower the dividend rather than compromise that quality or accumulate significant borrowings to meet a dividend level higher than operating cash flow would support. We will continue to carefully monitor our cash flows and market conditions, and their impact on our earnings and future dividend projections.

Short-Term Liquidity and Capital Resources

During the year ended December 31, 2005, we generated net cash flows from operating activities of approximately $76.4 million, which is primarily comprised of receipts for rental revenues, tenant reimbursements, and interest income, less payments for property operating expenses, asset and property management fees, interest expense, and general and administrative expenses. From cash flows from operating activities and proceeds from master leases of approximately $15.4 million during the year ended December 31, 2005, we paid dividends to stockholders of approximately $80.6 million. During the year ended December 31, 2005, we generated net cash flow from financing activities of approximately $1,200.3 million, primarily as a result of raising net proceeds from the sale of our common stock under our public offerings of approximately $1,194.6 million and receiving proceeds from additional borrowings of approximately $592.4 million. Such cash inflows from financing activities were primarily used to invest approximately $1,225.1 million in real estate, to repay outstanding balances on our lines of credit and notes payable of approximately $360.7 million, and to pay commissions and dealer-manager fees of $109.4 million. We expect to utilize residual cash and cash equivalents of approximately $35.4 million as of December 31, 2005 to satisfy current liabilities, pay future dividends, fund future anticipated acquisitions of real properties, or reduce indebtedness.

On December 7, 2005, the board of directors of Wells REIT II declared a daily dividend for stockholders of record from December 16, 2005 through March 15, 2006 in an amount equal to an annualized dividend of $0.60 per share, which is consistent with the rate of dividends declared for each quarter in 2005 on a per share basis. Such

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dividend was paid on March 22, 2006. During the year ended December 31, 2005, our funds from operations of approximately $80.2 million (see Funds From Operations), when combined with master lease receipts of $15.4 million, were adequate to fund the payment of dividends to our stockholders of $80.6 million.

On May 9, 2005, we entered into a $400.0 million, three-year unsecured revolving financing facility (the Wachovia Line of Credit) with a syndicate of banks led by Wachovia Bank, N.A. (Wachovia). The Wachovia Line of Credit replaced the $430.0 million, 180-day secured revolving financing facility with Bank of America, N.A. In connection with the closing, we paid fees and expenses totaling approximately $2.1 million. We have pledged approximately $9.2 million of our total borrowing capacity under the Wachovia Line of Credit to letters of credit for future tenant improvements and leasing costs.

The Wachovia Line of Credit contains, among others, the following restrictive covenants:

- limits our ratio of debt to total asset value, as defined, to 50% or less at all times;
- limits our ratio of secured debt to total asset value, as defined, to 40% or less at all times;
- requires our ratio of unencumbered asset value, as defined, to total unsecured debt to be greater than 2:1 at all times;
- requires maintenance of certain interest coverage ratios;
- requires maintenance of certain minimum stockholders equity balances; and
- limits investments that fall outside our core investments of improved office and industrial properties.

Under the terms of the Wachovia Line of Credit, we may borrow up to 50% of the unencumbered asset value, or the aggregate value of a subset of lender-approved properties. The Wachovia Line of Credit also stipulates that our net distributions, which equal total dividends and other distributions less the amount reinvested through our dividend reinvestment plan, may not exceed the greater of 90% of our Funds from Operations for the corresponding period or the minimum amount required in order for us to maintain our status as a REIT. Funds from Operations, as defined by the agreement, means net income (loss), minus (or plus) gains (or losses) from debt restructuring and sales of property during such period, plus depreciation on real estate assets and amortization (other than amortization of deferred financing costs) for such period, all after adjustments for unconsolidated partnerships and joint ventures. The Wachovia Line of Credit includes a cross-default provision that provides that a payment default under any recourse obligation of $10 million or more or any non-recourse obligation of $20 million or more by us, Wells OP II, or any of our subsidiaries constitutes a default under the credit facility.

Our charter prohibits us from incurring debt that would cause our borrowings to exceed 50% of our assets (valued at cost before depreciation and other non-cash reserves) unless a majority of the members of the conflict committee of our board of directors approves the borrowing. Our charter also requires that we disclose the justification of any borrowings in excess of the 50% leverage guideline.

We intend to continue to generate capital from the sale of common stock under our follow-on offering and from third-party borrowings, and to use such capital primarily to fund future acquisitions of real estate. As of February 28, 2006, we held cash balances of approximately $52.3 million and had outstanding borrowings under the Wachovia Line of Credit of approximately $257.5 million. After consideration of letters of credit pledged against the Wachovia Line of Credit, we had a remaining borrowing capacity, as of February 28, 2006, of approximately $133.3 million under the Wachovia Line of Credit. Accordingly, we believe that we have adequate capacity to continue to expand our portfolio and meet our future operating cash flow needs. In 2006, we expect to use substantially all of our future operating cash flow to pay dividends to stockholders and to use cash on hand and third-party borrowings to fund capital expenditures.

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Long-term Liquidity and Capital Resources

We expect that our primary sources of capital over the long term will include proceeds from the sale of our common stock, proceeds from secured or unsecured borrowings from third-party lenders, and net cash flows from operations. We expect that our primary uses of capital will be for property acquisitions, either directly or through investments in joint ventures, for the payment of tenant improvements, for the payment of offering-related costs, for the payment of operating expenses, including interest expense on any outstanding indebtedness, and for the payment of dividends. Over the next five years, we anticipate funding capital expenditures necessary for the properties currently in our portfolio, including building improvements, tenant improvements, and leasing commissions of approximately $79.3 million, exclusive of costs of properties under development.

In determining how and when to allocate cash resources, we initially consider the source of the cash. We expect that substantially all future net operating cash flows, after payments for certain capital expenditures such as tenant improvements and leasing commissions, will be used to pay dividends. However, we may use other sources of cash, such as short-term borrowings, to fund dividends from time to time (see Liquidity and Capital Resources Overview above). We expect to use substantially all net cash flows generated from raising equity or debt financing to fund acquisitions, certain capital expenditures identified upon acquisition, the repayment of outstanding borrowings, and to redeem shares under our share redemption program. If sufficient equity or debt capital is not available, our future investments in real estate will be lower.

To the extent that future cash flows provided by operations are lower due to lower returns on properties, future dividends paid may be lower as well. Our cash flow from operations depends significantly on market rents and the ability of tenants to make rental payments. We believe that the diversity of our tenant base and the concentration of creditworthy tenants in our portfolio helps to mitigate the risk of tenants defaulting on leases. However, general economic downturns, or downturns in one or more of our core markets, could adversely impact the ability of our tenants to make lease payments and our ability to re-lease space on favorable terms when leases expire. In the event of either situation, our cash flow and consequently our ability to meet capital needs, could adversely affect our ability to pay dividends in the future.

Contractual Commitments and Contingencies

As further discussed in Note 5 to the accompanying consolidated financial statements, we entered into an agreement to purchase an office building, which is currently under construction, in Lancaster, South Carolina (the Decision One Building), for a gross purchase price of approximately $33.7 million, plus closing costs and an allowance for tenant improvements and leasing costs not to exceed $1.8 million upon completion. In connection with the execution of this agreement, we paid a nonrefundable deposit of $3.4 million to an escrow agent in June 2005, which will be applied to the purchase price. We anticipate construction of the Decision One Building to be completed in June 2006. We anticipate paying for this acquisition with equity proceeds, borrowings under the Wachovia Line of Credit, or a combination thereof, the allocation of which will depend upon the timing and amount of capital raised in our ongoing public offering and future property acquisitions.

We have executed a construction agreement with an unrelated third party for the purpose of constructing the LakePointe 3 office building in Charlotte, North Carolina. As of December 31, 2005, we had approximately $10.7 million in costs remaining to be incurred under the agreement. Construction is anticipated to be completed by September 2006. We anticipate funding up to $17.1 million of the costs to build this building with borrowings under the LakePointe 3 construction loan. In connection with this construction loan, we entered into an interest rate swap to hedge exposure to changing interest rates, resulting in us paying a fixed rate of 4.84% per annum of the balance outstanding at each payment date. The interest rate swap expires in 2007.

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Our contractual obligations as of December 31, 2005 are as follows (in thousands):

		Payments Due by Period			
Contractual Obligations	**Total**	**Less than 1 year**	**1-3 years**	**4-5 years**	**More than 5 years**
Outstanding debt obligations	$ 832,402	$ 21,426	$ 342,855	$ 32,604	$ 435,517
Capital lease obligations	109,380	4,680	9,360	9,360	85,980
Purchase obligations[1]	48,700	48,700			
Operating lease obligations	3,180	60	120	120	2,880
Total	$ 993,662	$ 74,866	$ 352,335	$ 42,084	$ 524,377

[1] Includes purchase commitments for the Decision One Building, the LakePointe 3 office building, and $7.7 million in connection with the University Circle earnout agreement. Refer to Note 5 to our accompanying consolidated financial statements for further explanation.

Results of Operations

Overview

Our results of operations are not indicative of those expected in future periods as we expect that rental income, tenant reimbursements, operating expenses, asset management fees, depreciation, amortization, and net income will each increase in future periods as a result of owning the assets acquired during 2005 for an entire period and as a result of anticipated future acquisitions of real estate assets.

During the period from inception (July 3, 2003) to December 31, 2003, we had not yet commenced real estate operations, as we had not received and accepted the minimum subscription of $2,500,000 under our initial public offering. Therefore, we had no material results of operations for the year ended December 31, 2003. Following the receipt and acceptance of subscriptions for the minimum offering of $2,500,000 on January 22, 2004, we acquired 18 real properties during 2004. During 2005, we invested in 21 additional properties, which increased the total number of properties held in our portfolio to 39 as of December 31, 2005. Accordingly, the results of operations presented for the years ended December 31, 2005 and 2004 are not directly comparable.

Comparison of the year ended December 31, 2005 vs. the year ended December 31, 2004

Rental income and tenant reimbursements increased from approximately $43.9 million and $6.8 million, respectively, for the year ended December 31, 2004 to approximately $135.0 million and $29.0 million, respectively, for the year ended December 31, 2005, primarily as a result of the growth in the portfolio during 2005 and owning the properties acquired in 2004 for a full year. Rental income and tenant reimbursements are expected to continue to increase in future periods, as compared to historical periods, as a result of owning the assets acquired during 2005 for an entire year and future acquisitions of real estate assets.

Property operating costs and asset and property management fees increased from approximately $12.8 million and $3.9 million, respectively, for the year ended December 31, 2004 to approximately $45.8 million and $13.2 million, respectively, for the year ended December 31, 2005, primarily as a result of the growth in the portfolio during 2005 and owning the properties acquired in 2004 for a full year. Property operating costs and property management fees represent approximately 33% and 36% of total revenue for the years ended December 31, 2004 and 2005, respectively. Property operating costs and asset and property management fees are expected to continue to increase in future periods, as compared to historical periods, due to owning the assets acquired during 2005 for an entire year and future acquisitions of additional real estate assets.

Depreciation of real estate and amortization of lease costs increased from approximately $7.5 million and $12.0 million, respectively, for the year ended December 31, 2004 to approximately $24.5 million and $43.2 million, respectively, for the year ended December 31, 2005, primarily due to the acquisition of properties during 2005 and owning the properties acquired in 2004 for a full year. Amortization increased at a higher rate than depreciation primarily because the period of amortization for lease assets is the respective lease term, which is generally shorter than the useful life over which buildings and improvements are depreciated. Depreciation and

amortization are expected to continue to increase in future periods, as compared to historical periods, due to owning the assets acquired during 2005 for an entire year and future acquisitions of real estate assets.

General and administrative expenses increased from approximately $4.3 million for the year ended December 31, 2004 to approximately $9.1 million for the year ended December 31, 2005, primarily due to increases in salary expense reimbursements payable to Wells Capital and Wells Management as a result of acquiring additional properties during 2005 and owning the properties acquired in 2004 for a full year. General and administrative expenses, as a percent of total revenues, decreased from approximately 9% for the year ended December 31, 2004 to approximately 6% for the year ended December 31, 2005. In connection with the acquisition of additional real properties, we anticipate future general and administrative expenses to continue to increase as measured in gross dollars and to continue to decrease as a percentage of total revenues as we achieve greater economies of scale with a larger portfolio of real estate assets in future periods, as compared to historical periods.

Interest expense increased from approximately $17.6 million for year ended December 31, 2004 to approximately $25.1 million for the year ended December 31, 2005. The additional interest expense incurred during 2005 relates primarily to amounts drawn on our lines of credit, new mortgage notes, and mortgage notes assumed in connection with acquisitions of properties during 2005, as well as 2004 borrowings being outstanding for a full year. Future levels of interest expense will vary primarily based on the amounts of future borrowings and the costs of borrowings. Future borrowings will be used primarily to fund future acquisitions of real estate assets or interests therein. Accordingly, the amounts of future borrowings and future interest expense will be largely dependent upon the level of additional investor proceeds raised in our ongoing public offering, the opportunities to acquire real estate assets consistent with our investment objectives, and the timing of such future acquisitions.

Interest and other income increased from approximately $2.9 million for the year ended December 31, 2004 to approximately $9.6 million for the year ended December 31, 2005, primarily as a result of interest earned on investor proceeds raised during 2005 prior to investing such proceeds in real estate assets. Future levels of interest income will be largely dependent upon the rate at which investor proceeds are raised and the timing and availability of future acquisitions of real estate assets.

Minority interest in (earnings) loss of consolidated subsidiaries increased from a loss of approximately $6,000 for year ended December 31, 2004 to earnings of approximately $220,000 for the year ended December 31, 2005, primarily as a result of owning an approximate 95% interest in a joint venture that holds the Highland Landmark III property for a full year, as we acquired our interest in the Highland Landmark III property on December 28, 2004. In addition, during August 2005, we acquired interests in the following three properties through separate joint ventures with minority interest partners: the One Robbins Road Building, the Four Robbins Road Building, and the Baldwin Point Building. Earnings allocated to minority interest partners fluctuate based on the level of earnings generated by the properties in which they own interests and the nature of the allocation provisions provided in respective joint venture agreements. Accordingly, minority interest in earnings of consolidated subsidiaries is expected to continue to increase in future periods, as compared to historical periods, due to owning the One Robbins Road Building, the Four Robbins Road Buildings, and the Baldwin Point Building for an entire year.

We recognized net income and net income per share of approximately $12.5 million and $0.09, respectively, for the year ended December 31, 2005, as compared to net loss and net loss per share of approximately $4.6 million and $0.15, respectively, for the year ended December 31, 2004, primarily due to the increase in net operating income generated from our growing portfolio of properties outpacing the increase in portfolio expenses during 2005, as compared to 2004. Future net income is expected to continue to increase as a result of owning the assets acquired during 2005 for an entire year and future acquisitions of real estate. The level of future net income per share will vary primarily based on the level of equity proceeds raised and the rate at which we are able to invest such proceeds in income-generating real estate assets.

Portfolio Information

As of December 31, 2005, we owned interests in 37 office properties, one industrial building, and one hotel located in 15 states and the District of Columbia. All of these properties are included in our accompanying consolidated financial statements, as 33 are wholly owned and six are owned through consolidated joint ventures. As of December 31, 2005, our office and industrial properties were approximately 96% leased with an average lease term remaining of approximately 7.9 years.

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As of December 31, 2005, our five highest geographic concentrations were as follows:

Location	2005 Annualized Gross Base Rents (in thousands)	Rentable Square Feet (in thousands)	Percentage of 2005 Annualized Gross Base Rents
Cleveland	$ 35,643	1,321	14%
Atlanta	30,281	1,778	12%
San Jose	26,351	451	10%
Houston	22,935	841	9%
Baltimore	19,903	656	8%
	$ 135,113	5,047	53%

As of December 31, 2005, our five highest tenant industry concentrations were as follows:

Industry	2005 Annualized Gross Base Rents (in thousands)	Rentable Square Feet (in thousands)	Percentage of 2005 Annualized Gross Base Rents
Legal Services	$ 46,218	1,243	18%
Depository Institutions	31,587	1,141	12%
Security & Commodity Brokers	21,137	666	8%
Communication	20,175	799	8%
Business Services	19,794	835	8%
	$ 138,911	4,684	54%

As of December 31, 2005, our five highest tenant concentrations were as follows:

Tenant	2005 Annualized Gross Base Rents (in thousands)	Percentage of 2005 Annualized Gross Base Rents
Key Bank	$ 20,241	8%
T. Rowe Price	11,892	5%
Northrop Grumman	8,695	3%
AT&T	8,255	3%
Bingham McCutchen LLP	7,573	3%
	$ 56,656	22%

Funds From Operations

We believe that funds from operations (FFO) is a beneficial indicator of the performance of any equity REIT. Because FFO calculations exclude such factors as depreciation and amortization of real estate assets and gains or losses from sales of operating real estate assets (which can vary among owners of identical assets in similar conditions based on historical cost accounting and useful-life estimates), they facilitate comparisons of operating performance between periods and with other REITs. Our management believes that accounting for real estate assets in accordance with U.S generally accepted accounting principles (GAAP) implicitly assumes that the value of real estate assets diminishes predictably over time. Since real estate values have historically risen or fallen with market conditions, many industry investors and analysts have considered the presentation of operating results for real estate companies that use historical cost accounting to be insufficient by themselves. As a result, we believe that the use of FFO, together with the required GAAP presentation, provides a more complete understanding of our performance relative to our competitors and a more informed and appropriate basis on which to make decisions involving operating, financing, and investing activities. Other REITs may not define FFO in accordance with the current National Association of Real

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Estate Investment Trust s (NAREIT) definition (as we do) or may interpret the current NAREIT definition differently than we do.

FFO is a non-GAAP financial measure and does not represent net income determined in accordance with GAAP. We believe that net income, as determined in accordance with GAAP, is the most relevant measure of our operating performance and, accordingly, believe that FFO should not be viewed as an alternative measurement of our operating performance to net income.

Certain noncash items such as depreciation, amortization, and gains on the sale of real estate assets are excluded from our calculation of FFO. Conversely, FFO is not adjusted to reflect the cost of capital improvements or any related capitalized interest. Our calculation of FFO is presented in the following table (in thousands):

	For the Year Ended December 31,	
	2005	**2004**
Net income (loss)	**$ 12,521**	$ (4,562)
Add:		
Depreciation of real assets	**24,505**	7,456
Amortization of lease-related costs	**43,210**	12,028
FFO	**$ 80,236**	$ 14,922
Weighted-average shares outstanding	**139,680**	31,372

Set forth below is additional information related to selected material cash and noncash items included in or excluded from net income (loss) above, which may be helpful in assessing our operating results:

Included in Net Income (Loss):

Straight-line rental revenue of approximately $15.7 million and $5.1 million was recognized for the years ended December 31, 2005 and 2004, respectively;

Amortization of intangible lease assets and liabilities was recognized as net decreases to rental revenues of approximately $3.9 million and $1.4 million for the years ended December 31, 2005 and 2004, respectively; and

Amortization of deferred financing costs of approximately $1.4 million and $5.4 million was recognized as interest expense for the years ended December 31, 2005 and 2004, respectively.

Excluded from Net Income (Loss):

Master lease proceeds of $15.4 million were recorded as an adjustment to the basis of real estate assets acquired during the year ended December 31, 2005 and, accordingly, are not included in net income or FFO above. We consider master lease proceeds when determining cash available for dividends to our stockholders.

REIT Qualification

We have elected to be taxed as a REIT under the Internal Revenue Code of 1986, as amended, and have operated as such beginning with our taxable year ended December 31, 2003. To qualify as a REIT, we must meet certain organizational and operational requirements, including a requirement to distribute at least 90% of our REIT taxable income to our stockholders, computed without regard to the dividends-paid deduction and by excluding our net capital gain. As a REIT, we generally will not be subject to federal income tax on income that we distribute to our stockholders. If we fail to qualify as a REIT in any taxable year, we will then be subject to federal income taxes on our taxable income for that year and for the four years following the year during which qualification is lost, unless the Internal Revenue Service grants us relief under certain statutory provisions. Such an event could materially adversely affect our net income and net cash available for distribution to our stockholders. However, we

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believe that we are organized and operate in such a manner as to qualify for treatment as a REIT for federal income tax purposes.

On October 4, 2005, we created Wells TRS II, LLC (Wells TRS), a wholly owned subsidiary organized as a Delaware limited liability company. We have elected to treat Wells TRS as a taxable REIT subsidiary. We may perform additional, non-customary services for tenants of buildings that we own through Wells TRS, including any real estate or non-real estate related services; however, any earnings related to such services are subject to federal and state income taxes. In addition, in order for us to continue to qualify as a REIT, our investment in taxable REIT subsidiaries cannot exceed 20% of the value of our total assets. For the year ended December 31, 2005, Wells TRS incurred a net operating loss on an income tax basis; therefore, we recorded the related deferred tax asset and benefit in the accompanying consolidated balance sheet and statements of operations, respectively.

No provision for federal income taxes has been made in our accompanying consolidated financial statements, other than for income earned by Wells TRS, as we made distributions in excess of taxable income for the periods presented. We are subject to certain state and local taxes related to the operations of properties in certain locations, which have been provided for in our accompanying consolidated financial statements.

Inflation

We are exposed to inflation risk, as income from long-term leases is the primary source of our cash flows from operations. There are provisions in the majority of our tenant leases that are intended to protect us from, and mitigate the risk of, the impact of inflation. These provisions include rent steps, reimbursement billings for operating expense pass-through charges, real estate tax and insurance reimbursements on a per square-foot basis, or in some cases, annual reimbursement of operating expenses above a certain per square-foot allowance. However, due to the long-term nature of the leases, the leases may not re-set frequently enough to fully cover inflation.

Application of Critical Accounting Policies

Our accounting policies have been established to conform with GAAP. The preparation of financial statements in conformity with GAAP requires management to use judgment in the application of accounting policies, including making estimates and assumptions. These judgments affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenue and expenses during the reporting periods. If our judgment or interpretation of the facts and circumstances relating to various transactions had been different, it is possible that different accounting policies would have been applied, thus, resulting in a different presentation of the financial statements. Additionally, other companies may utilize different estimates that may impact comparability of our results of operations to those of companies in similar businesses.

The critical accounting policies outlined below have been discussed with members of the audit committee of the board of directors.

Investment in Real Estate Assets

We are required to make subjective assessments as to the useful lives of our depreciable assets. We consider the period of future benefit of the asset to determine the appropriate useful lives. These assessments have a direct impact on net income. The estimated useful lives of our assets by class are as follows:

Buildings	40 years
Building improvements	5-25 years
Tenant improvements	Shorter of economic life or lease term
Intangible lease assets	Lease term

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Allocation of Purchase Price of Acquired Assets

Upon the acquisition of real properties, we allocate the purchase price of properties to acquired tangible assets, consisting of land and building, and identified intangible assets and liabilities, consisting of the value of above-market and below-market leases and the value of in-place leases, based in each case on their estimated fair values.

The fair values of the tangible assets of an acquired property (which includes land and building) are determined by valuing the property as if it were vacant, and the as-if-vacant value is then allocated to land and building based on management s determination of the relative fair value of these assets. We determine the as-if-vacant fair value of a property using methods similar to those used by independent appraisers. Factors considered by us in performing these analyses include an estimate of carrying costs during the expected lease-up periods considering current market conditions and costs to execute similar leases, including leasing commissions and other related costs. In estimating carrying costs, we include real estate taxes, insurance, and other operating expenses during the expected lease-up periods based on current market conditions.

The fair values of above-market and below-market in-place leases are recorded based on the present value (using an interest rate that reflects the risks associated with the leases acquired) of the difference between (i) the contractual amounts to be paid pursuant to the in-place leases and (ii) our estimate of fair market lease rates for the corresponding in-place leases, measured over a period equal to the remaining terms of the leases. The capitalized above-market and below-market lease values are recorded as intangible lease assets or liabilities and amortized as an adjustment to rental income over the remaining terms of the respective leases.

The fair values of in-place leases include direct costs associated with obtaining a new tenant, opportunity costs associated with lost rentals that are avoided by acquiring an in-place lease, and tenant relationships. Direct costs associated with obtaining a new tenant include commissions, tenant improvements and other direct costs and are estimated based on our consideration of current market costs to execute a similar lease. These direct costs are included in deferred lease costs in the accompanying consolidated balance sheets and are amortized to expense over the remaining terms of the respective leases. The value of opportunity costs is calculated using the contractual amounts to be paid pursuant to the in-place leases over a market absorption period for a similar lease. Customer relationships are valued based on expected renewal of a lease or the likelihood of obtaining a particular tenant for other locations. These lease intangibles are included in intangible lease assets in the accompanying consolidated balance sheets and are amortized to expense over the remaining terms of the respective leases.

Estimates of the fair values of the tangible and intangible assets require us to estimate market lease rates, property operating expenses, carrying costs during lease-up periods, discount rates, market absorption periods, and the number of years the property is held for investment. The use of inappropriate estimates would result in an incorrect assessment of our purchase price allocations, which would impact the amount of our reported net income.

Valuation of Real Estate Assets

We continually monitor events and changes in circumstances that could indicate that the carrying amounts of the real estate and related intangible assets of both operating properties and properties under construction, in which we have an ownership interest, either directly or through investments in joint ventures, may not be recoverable. When indicators of potential impairment are present that suggest that the carrying amounts of real estate and related intangible assets may not be recoverable, we assess the recoverability of these assets by determining whether the carrying value will be recovered through the undiscounted future operating cash flows expected from the use of the asset and its eventual disposition. In the event that such expected undiscounted future cash flows do not exceed the carrying value, we decrease the carrying value of the real estate and related intangible assets to the estimated fair values, as defined by Statement of Financial Accounting Standard No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, and recognize an impairment loss. Estimated fair values are calculated based on the following information, in order of preference, dependent upon availability: (i) recently quoted market prices, (ii) market prices for comparable properties, or (iii) the present value of undiscounted cash flows, including estimated salvage value. We have determined that there has been no impairment in the carrying value of our real estate assets during the years ended December 31, 2005 and 2004. We held no real estate assets as of December 31, 2003.

Projections of expected future operating cash flows require that we estimate future market rental income amounts subsequent to the expiration of current lease agreements, property operating expenses, the number of

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months it takes to re-lease the property and the number of years the property is held for investment, among other factors. The subjectivity of assumptions used in the future cash flow analysis, including discount rates, could result in an incorrect assessment of the property s fair value and could result in the misstatement of the carrying value of our real estate and related intangible assets and net income.

Related-Party Transactions and Agreements

We have entered into agreements with Wells Capital and its affiliates, whereby we pay certain fees or reimbursements to Wells Capital or its affiliates for acquisition and advisory fees and expenses, organization and offering costs, sales commissions, dealer-manager fees, asset and property management fees and reimbursement of operating costs. See Note 8 to our accompanying consolidated financial st