MISSION WEST PROPERTIES INC
Form 10-K
March 16, 2009

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

# FORM 10-K

(Mark One)
[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For Fiscal Year Ended: December 31, 2008

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 No. 1-8383

MISSION WEST PROPERTIES, INC.
(Exact name of registrant as specified in its charter)

| Maryland | 95-2635431 |
|---|---|
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

| 10050 Bandley Drive, Cupertino, CA | 95014 |
|---|---|
| (Address of principal executive offices) | (Zip Code) |

Registrant's telephone number, including area code: (408) 725-0700

Securities Registered Pursuant to Section 12(b) of the Act:

Title of each class Name of each exchange on which registered Common Stock, $.001 par value per share The Nasdaq Stock Market LLC

Securities Registered Pursuant to Section 12(g) of the Act: NONE

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes [ ] No [X]

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes [ ] No [X]

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

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

Form 10-K. [X]

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. Large accelerated filer [ ] Accelerated filer [X] Non-accelerated filer [ ]

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes [ ] No [X]

As of June 30, 2008, the aggregate market value of the Registrant's common stock held by non-affiliates of the registrant was $213,611,025 based on the closing price as reported on the NASDAQ Stock Market LLC.

Indicate the number of shares outstanding of each of the Registrant's classes of common stock, as of the latest practicable date.

| Class | Outstanding at February 28, 2009 |
|---|---|
| Common Stock, $.001 par value per share | 21,748,211 shares |

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's proxy statement to be delivered to stockholders in connection with the Registrant's 2009 Annual Meeting of Stockholders to be held May 20, 2009 are incorporated by reference into Part III of this Form 10-K. The Registrant intends to file its proxy statement within 120 days after its fiscal year end.

FORWARD LOOKING INFORMATION

This annual report contains forward-looking statements within the meaning of the federal securities laws. We intend such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995, and are including this statement for purposes of complying with these safe harbor provisions. Forward-looking statements include our discussion of "Quantitative and Qualitative Disclosures about Market Risks" in Item 7A below. Forward-looking statements, which are based on certain assumptions and describe future plans, strategies and expectations of us, are generally identifiable by use of the words "believe," "expect," "intend," "anticipate," "estimate," "project" or similar expressions. Our ability to predict results or the actual effect of future plans or strategies is inherently uncertain. Factors which could have a material adverse effect on the operations and future prospects or would cause actual results in the future to differ materially from any of our forward-looking statements of the Company include, but are not limited to, changes in: the credit markets and the overall availability and cost of credit, economic conditions generally and the real estate market specifically, legislative or regulatory provisions affecting the Company (including changes to laws governing the taxation of Real Estate Investment Trusts ("REITs")), availability of capital, interest rates, competition, supply of and demand for office and industrial properties in our current and proposed market areas, tenant defaults and bankruptcies, and general accounting principles, policies and guidelines applicable to REITs. In addition, the actual timing of development, construction, and leasing on the projects that the Company believes it may acquire in the future is unknown presently. These risks and uncertainties, together with the other risks described from time to time in our reports and documents filed with the Securities and Exchange Commission, should be considered in evaluating forward-looking statements and undue reliance should

not be placed on such statements (see Item 1A, "Risk Factors").



MISSION WEST PROPERTIES, INC.
2008 FORM 10-K ANNUAL REPORT

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PART I

ITEM 1. BUSINESS

ORGANIZATION AND GENERAL BUSINESS DESCRIPTION

Mission West Properties, Inc. (the "Company") acquires, markets, leases, and manages research and development ("R&D") properties, primarily located in the Silicon Valley portion of the San Francisco Bay Area. As of December 31, 2008, we owned and managed 111 properties totaling approximately 8.0 million rentable square feet of R&D properties through four limited partnerships, or operating partnerships, for which we are the sole general partner. R&D property is designed for research and development and office uses and, in some cases, includes space for light manufacturing operations with loading docks. We believe that we have one of the largest portfolios of R&D properties in the Silicon Valley. There are two tenants who individually lease in excess of 300,000 rentable square feet from us: Microsoft Corporation and Apple Computer, Inc. For federal income tax purposes we have operated as a self-managed, self-administered and fully integrated Real Estate Investment Trust ("REIT") since fiscal 1999.

Prior to July 1, 1998, most of our properties were under the ownership or control of Carl E. Berg, his brother Clyde J. Berg, certain members of their respective immediate families, and certain entities in which Carl E. Berg and/or Clyde J. Berg held controlling or other ownership interests, including Berg & Berg Developers, Berg & Berg Enterprises, Inc. and Berg & Berg Enterprises, LLC (the "Berg Group"). We acquired these properties as of July 1, 1998 by becoming the general partner of each of the four operating partnerships in an UPREIT transaction. At that time, we also acquired ten properties comprising approximately 560,000 rentable square feet from entities controlled by third parties in which the Berg Group members were significant owners.

Through various property acquisition agreements with the Berg Group and subject to the approval of the Independent Directors Committee of the Board of Directors, we have the right to purchase, on pre-negotiated terms, R&D and other types of office and light industrial properties that the Berg Group develops in the future. With in-house development, architectural and construction personnel, the Berg Group continues to focus on a full range of land acquisition, development and construction activities for R&D properties, often build-to-suit, to meet the demands of Silicon Valley information technology companies. As the developer, the Berg Group takes on the risks of purchasing the land, obtaining regulatory approvals and permits and financing construction. Since September 1998, we have acquired approximately 3,386,000 additional rentable square feet of R&D properties from the Berg Group under these agreements.

Our executive offices are located at 10050 Bandley Drive, Cupertino, California 95014, and our telephone number is (408) 725-0700. Our website is located at http://www.missionwest.com. On our website, you can access, free of charge, our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act of 1934, as amended, as soon as reasonably practicable after such material is electronically filed with, or furnished to, the Securities and Exchange Commission (the "SEC"). A copy of these filings is available to all interested parties upon written request to "Investor Relations" at our corporate offices.

We file annual, quarterly and special reports, proxy statements and other information with the SEC. You may read and copy any document we file with the SEC at the SEC's Public Reference Room at 100 F Street, N.W., Washington, D.C. 20549. You may obtain information about the operation of the SEC's Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC also maintains a website that contains reports, proxy and information statements, and other information regarding registrants that file electronically with the SEC (http://www.sec.gov).

OUR RELATIONSHIP WITH THE BERG GROUP

Through a series of transactions occurring between May 1997 and December 1998, we became the vehicle for substantially all of the Silicon Valley R&D property operating activities of the Berg Group. We are the general partner pursuant to the partnership agreements of the operating partnerships and, along with members of the Berg Group and other individuals, are party to an acquisition agreement dated as of May 14, 1998 and amended, as of July 1, 1998, exchange rights agreement and the Berg Land Holdings Option Agreement. Each agreement defines the material rights and obligations among us, the Berg Group members, and other parties to those agreements. Among other things, these agreements give us rights to:

- control the operating partnerships;
- until December 31, 2010, acquire, subject to approval of the Independent Directors Committee of the Board of Directors, on pre-negotiated terms, all future R&D properties developed by the Berg Group on land currently owned or acquired in the future; and
- acquire R&D, office and industrial properties identified by the Berg Group in California, Oregon and Washington, subject to approval of the Independent Directors Committee of the Board of Directors.

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Under these agreements, our charter or our bylaws, the Berg Group has the right to:

- designate two of five nominees for director to be elected by our stockholders, subject to the Berg Group's maintenance of certain ownership interests;
- participate in our securities offerings;
- exchange their operating partnership interests ("O.P. Units") for shares of our common stock;
- vote on major transactions, subject to maintenance of certain ownership thresholds; and
- prevent us from selling properties when the sale will have adverse tax consequences to the Berg Group members.

To comply with REIT requirements that restrict the percentage of the total value of our stock that may be owned by five or fewer individuals to 50% or less, our charter generally prohibits the direct or indirect ownership of more than 9% of our common stock by any stockholder. This limit excludes the Berg Group, which has an aggregate ownership limit of 20%. Currently, the Berg Group members collectively own approximately 9.2% of the outstanding shares of our common stock.

Carl E. Berg, the Company's Chairman of the Board of Directors and Chief Executive Officer and the controlling member of the Berg Group, has been engaged in the development and long-term ownership of Silicon Valley real estate for almost 40 years. In 1969, Mr. Berg foresaw the rising demand for efficient, multi-purpose facilities for the rapidly growing information technology industry in the Silicon Valley. Since 1972, in addition to his real estate activities, Mr. Berg also has been actively involved in venture capital investments in many information technology companies in the Silicon Valley, including such companies as Amdahl Corporation, Sun Microsystems, Inc., and Integrated Device Technologies, Inc. He serves on the board of directors of numerous electronics and energy technology companies. These activities have helped Mr. Berg develop a detailed understanding of the real estate requirements of technology companies, acquire valuable market information and increase his name recognition within the venture capital and entrepreneurial communities. These activities also manifest his commitment to the growth and success of Silicon Valley companies. We believe

that Mr. Berg's substantial knowledge of and contacts in various technology industries provide a significant benefit to the Company.

BUSINESS STRATEGY

Our acquisition, growth and operating strategy incorporates the following elements:

- working with the Berg Group to take advantage of their abilities and resources to pursue development opportunities which we have an option to acquire until December 31, 2010, on pre-negotiated terms, upon completion and leasing;
- capitalizing on opportunistic acquisitions from third parties of high-quality R&D properties that provide attractive initial yields and significant potential for growth in cash-flow;
- focusing on general purpose, single-tenant Silicon Valley R&D properties for technology companies in order to maintain low operating costs, reduce tenant turnover and capitalize on our relationships with these companies and our extensive knowledge of their real estate needs; and
- maintaining prudent financial management principles that emphasize current cash flow while building long-term value, the acquisition of pre-leased properties to reduce development and leasing risks and the maintenance of sufficient liquidity to acquire and finance properties on desirable terms.

ACQUIRING PROPERTIES DEVELOPED BY THE BERG GROUP

We entered into the Berg Land Holdings Option Agreement in December 1998 under which we have an option to purchase all land acquired, directly or indirectly, by Carl E. Berg or Clyde J. Berg that has not been improved with completed buildings and which is zoned, intended or appropriate for R&D, office and/or industrial development or use in the states of California, Oregon and Washington. Currently, the Berg Land Holdings Option Agreement gives us the right to acquire future R&D property developments by the Berg Group on up to 84 additional acres of land currently controlled by the Berg Group, which could support approximately 1.4 million square feet of new development. In light of the continued overcapacity in the Silicon Valley R&D properties market, however, at this time we do not anticipate acquiring any additional newly constructed R&D properties from the Berg Group for several years because of the current market conditions in the Silicon Valley.

For example, the Berg Group currently is seeking local government approval of a proposed rezoning of the 160-acre Evergreen site to permit residential development on a substantial portion of the site. The Independent Directors Committee, which is responsible for reviewing, evaluating and authorizing action with respect to any transaction between us and any member of the Berg Group, has authorized removal of the Evergreen site from the scope of the Berg Land Holdings Option Agreement, subject to the completion of the rezoning of the 160-acre Evergreen site, or portion thereof, for residential development. In making this determination, the Independent Directors Committee considered a number of factors, including the lack of benefit to be derived from future R&D property development on this site and the risks and other potentially adverse consequences that could be associated with large scale



residential development activities. Any portion of the Evergreen site that is not rezoned as residential property is not deemed to be removed from the scope of the agreement and would remain eligible for potential future acquisition by the Company under the Berg Land Holdings Option Agreement.

As of December 31, 2008, we have acquired 23 leased R&D properties totaling

approximately 2,243,000 rentable square feet under the Berg Land Holdings Option Agreement at a cost of approximately $237.8 million, for which we have issued 8,482,085 O.P. Units and assumed debt of approximately $141.4 million. The principal terms of the agreement include the following:

- So long as the Berg Group members and their affiliates own or have the right to acquire shares representing at least 65% of our common stock on a Fully Diluted basis, or until December 31, 2010, whichever occurs first, we will have the option to acquire any building developed by any member of the Berg Group on the land subject to the Berg Land Holdings Option Agreement at such time as the building has been leased. Upon our exercise of the option, the option price will equal the sum of the following or a lesser amount as approved by the Independent Directors Committee:

  1. the full construction cost of the building; plus
  2. 10% of the full construction cost of the building; plus
  3. interest at LIBOR plus 1.65%, on the amount of the full construction cost of the building for the period from the date funds were disbursed by the developer to the close of escrow; plus
  4. the original acquisition cost of the parcel on which the improvements will be constructed, which range from $8.50 to $20.00 per square foot for land currently owned or under option; plus
  5. 10% per annum of the amount of the original acquisition cost of the parcel from the later of January 1, 1998 and the seller's acquisition date, to the close of escrow; minus
  6. the aggregate principal amount of all debt encumbering the acquired property.

- The acquisition cost, net of any debt, will be payable in cash, or O.P. Units valued at the average closing price of our common stock over the 30-trading-day period preceding the acquisition or, in cash, at the option of the Berg Group .

- We also must assume all property tax assessments.

- If we elect not to exercise the option with respect to any property, the Berg Group may hold and lease the property for its own account, or may sell it to a third party.

- All action taken by us under the Berg Land Holdings Option Agreement, including any variations from stated terms outlined above must be approved by a majority of the members of the Independent Directors Committee.

In addition, under the Acquisition Agreement, Carl E. Berg has agreed not to directly or indirectly acquire or develop any real property zoned for office, industrial or R&D use in the states of California, Oregon and Washington without first disclosing and making the acquisition opportunity available to us. The Independent Directors Committee decides whether we will pursue each opportunity presented to us by Mr. Berg. This restriction will expire when there is no Berg Group nominee on our board of directors and the Berg Group's fully diluted ownership percentage, which is calculated based on all outstanding shares of common stock and all shares of common stock that could be acquired upon the exercise of all outstanding options to acquire our voting stock, as well as all shares of common stock issuable upon exchange of all O.P. Units ("Fully Diluted"), falls below 25%.

As a general policy which has been established by the Independent Directors Committee, we do not acquire properties under the Berg Land Holdings Option Agreement until they have been leased. We are responsible for a significant portion of the leasing process in connection with such acquisitions, however.

The following table presents certain information concerning currently identified

land that we have the right to acquire under the Berg Land Holdings Option Agreement.

| Available Land: | Net Acres | Approximate Rentable Area (Square Feet) |
|---|---|---|
| Piercy & Hellyer | 30 | 490,000 |
| Morgan Hill (1) | 18 | 288,000 |
| King Ranch | 12 | 207,000 |
| Fremont & Cushing | 24 | 387,000 |
| Total | 84 | 1,372,000 |

(1) This land is owned by the TBI joint ventures partnership. We expect to own an approximate 50% interest in the partnership through one of our operating partnerships. The property will be operated and managed by the other joint venture partner in the entity.



Although we may acquire new properties or joint ventures available to us under the terms of the Berg Land Holdings Option Agreement, subject to approval by the Independent Directors Committee, there can be no assurance that we actually will consummate any additional transactions. Furthermore, we have not yet determined the means by which we would acquire and pay for any such properties or the impact of any of the acquisitions on our business, results of operations, financial condition, Funds from Operation ("FFO") or available cash for distribution (see Item 1A, "Risk Factors - Our contractual business relationships with the Berg Group present additional conflicts of interest which may result in the realization of economic benefits or the deferral of tax liabilities by the Berg Group without equivalent benefits to our stockholders").

OPPORTUNISTIC ACQUISITIONS

In addition to our potential acquisition opportunities under the Berg Land Holdings Option Agreement, we believe our acquisitions experience, established network of real estate and information technology professionals, and overall financial condition will continue to provide opportunities for external growth. In general, we will seek opportunistic acquisitions of high quality, well located Silicon Valley R&D properties in situations where illiquidity or inadequate management permit their acquisition at favorable prices, and where our management skills and knowledge of Silicon Valley submarkets may facilitate increases in cash flow and asset value.

Furthermore, our use of the operating partnership structure allows us to offer prospective sellers the opportunity to contribute properties on a tax-deferred basis in exchange for O.P. Units. Although we have not consummated any transactions on this basis since our July 1, 1998 acquisition of the Berg Group properties, this capacity to complete tax-deferred transactions with sellers of real property further enhances our ability to acquire additional properties.

FOCUS ON SINGLE TENANT SILICON VALLEY R&D PROPERTIES

We intend to continue to emphasize the acquisition of single-tenant rather than

multi-tenant properties, a practice that has historically contributed to the relatively low turnover and higher occupancy rates on our properties. We believe that the relatively small number of tenants (75 total) leasing our properties, mostly under the triple net lease structure, allows us to efficiently manage the properties and to serve our tenants' needs without extensive in-house staff or the assistance of a third-party property management organization. In addition, this emphasis allows us to incur less expense for tenant improvements and leasing commissions than multi-tenant, high turnover property owners. This strategy also reduces the time and expense associated with obtaining building permits and other governmental approvals. We believe that the relatively stable, extended relationships that we have developed with our key tenants are valuable in the expansion of our business.

RECENT RENTAL MARKET DEVELOPMENTS AND THEIR IMPACT ON OUR BUSINESS

All of the Company's properties are located in the Northern California area known as Silicon Valley, which generally consists of portions of Santa Clara County, Southwestern Alameda County, Southeastern San Mateo County and Eastern Santa Cruz County. In the past several years, the Silicon Valley R&D property market has fluctuated with the local economy. According to a recent report by NAI BT Commercial Real Estate (the "BT Report"), vacancy rates for Silicon Valley R&D property decreased from approximately 16.6% in late 2007 to 16.3% at the end of 2008. Total vacant R&D square footage in Silicon Valley at the end of the fourth quarter of 2008 amounted to approximately 25.1 million rentable square feet, of which 17.7%, or 4.5 million rentable square feet, was sublease space. According to the BT Report, in 2007, total positive net absorption (which is the computation of gross square footage leased less gross new square footage vacated for the period presented) amounted to approximately 2.9 million rentable square feet, and in 2008, there was total negative net absorption of approximately 33 thousand rentable square feet as local economic conditions deteriorated due to a weakened economy, dysfunctional financial markets, depressed housing, a falling stock market and rising unemployment rates. According to the BT Report, the average asking market rent per square foot was $1.26 at year-end for 2008 and 2007, although individual properties within any particular submarket presently may be leased above or below the current average asking market rental rates within that submarket and the region as a whole. Moreover, the impact of vacancies has not been uniform throughout the area. The Silicon Valley R&D property market is characterized by a substantial number of submarkets, with rent and vacancy rates varying by submarket and location within each submarket.

In addition, leasing activity for new build-to-suit and vacated R&D properties has slowed considerably during the past several years. The time to complete the marketing and lease up of vacant space has increased from an average of several months to as much as an average of 18 to 40 months as a result of the over-supply of R&D properties in the market.

For the years ended December 31, 2008 and 2007, the occupancy rates for leased properties in our portfolio were 66.4% and 61.7%, respectively.



Despite our strategic focus on single tenant properties and leases, in order to meet market conditions we have been, and expect to continue, leasing less than the entire premises of some of our R&D properties to a single tenant from time to time. Leasing our R&D properties, which generally have been built for single tenant occupancy, to multiple tenants tends to increase our leasing costs and operating expenses and reduce the profitability of our leasing activities. Although we scrutinize each prospective tenant's creditworthiness and

continually evaluate the financial capacity of both our prospective and existing tenants, a downturn in tenants' businesses may weaken their financial condition and could result in defaults under their lease obligations.

We believe that the average 2009 renewal rental rates for our properties will be approximately equal to, or perhaps, below current market rents. Leases representing approximately 370,000 rentable square feet, or 2.2% of our 2009 cash rent, are scheduled to expire during 2009. If we are unable to lease a significant portion of any vacant space or space scheduled to expire; if we experience significant tenant defaults as a result of the current economic downturn; if we restructure existing leases and lower existing rents in order to retain tenants for an extended term; if we increase our lease costs and operating expenses substantially to accommodate multiple tenants in our R&D properties; or if we are not able to lease space at or above current market rates, our results of operations and cash flows will be affected adversely.

OPERATIONS

We operate as a self-administered, self-advised and self-managed REIT with our own employees. As the sole general partner of the operating partnerships, we control the business and assets of the operating partnerships and have full and complete authority, discretion and responsibility with respect to the operating partnerships' operations and transactions, including, without limitation, acquiring additional properties, borrowing funds, raising new capital, leasing buildings and selecting and supervising all agents of the operating partnerships.

Although most of our leases are triple net and building maintenance and tenant improvements are the responsibility of the tenants, from time to time we may be required to undertake construction and repair work at our properties. We bid all major work competitively to subcontractors. Members of the Berg Group may participate in the competitive bidding for the work, but all contracts with the Berg Group are subject to review and approval by the Independent Directors Committee.

We generally market our properties and negotiate leases ourselves. We make the availability of our properties known to the brokerage community to garner their assistance in locating prospective tenants, however. As a result, we expect to retain our policy of paying fixed commissions to tenants' brokers.

We believe that our business practices provide us with competitive advantages, including -

- EXTERNAL DEVELOPMENT AFFILIATE. Until December 31, 2010, we have the option to purchase all future R&D, office, industrial property developments of the Berg Group under the Berg Land Holdings Option Agreement on land currently held or acquired directly or indirectly by Carl E. Berg or Clyde J. Berg that is zoned for those purposes and located in California, Oregon and Washington following completion and lease-up of the property. The acquisition terms and conditions for the existing and identified projects have been pre-negotiated and are documented under the Berg Land Holdings Option Agreement. This relationship provides us with the economic benefits of development while eliminating development and initial lease-up risks. It also provides us with access to one of the most experienced development teams in the Silicon Valley without the expense of maintaining development personnel.

- LEAN ORGANIZATION, EXPERIENCED TEAM. In part because of our primary focus on Silicon Valley, our experience with the special real estate requirements of information technology tenants and the long-term triple-net structure of our leases, we are able to conduct and expand our business with a small management team comprised of highly qualified and experienced professionals

working within a relatively flat organizational structure. We believe that the leanness of our organization and our experience will enable us to rapidly assess and respond to market opportunities and tenant needs, control operating expenses and develop and maintain excellent relationships with tenants. We further believe that these advantages translate into significantly lower costs for operations and give us the ability, along with the Berg Group, to compete favorably with other R&D property developers in Silicon Valley, especially for build-to-suit projects subject to competitive bidding. Furthermore, we believe this lower cost structure allows us to generate better returns from properties whose value can be increased through appropriate remodeling and efficient property management.

- SOUND PROPERTY MANAGEMENT PRACTICES. For each property, the management team, along with the Berg Group staff, develops a specific marketing and property management program. We select vendors and subcontractors on a competitive bid basis from a select group of highly qualified firms with whom we maintain ongoing relationships and carefully supervise their work.



OPERATING PARTNERSHIP AGREEMENTS

MANAGEMENT

The operating partnerships consist of four separate limited partnerships engaged in the combined operation and ownership of all our properties. The operating partnership agreements are identical in all material respects for all four of the limited partnerships. Pursuant to the operating partnership agreements, we act as the sole general partner of the operating partnerships, in which capacity we have exclusive control of the business and assets of the operating partnerships and generally have full and complete authority, discretion and responsibility with respect to the operating partnerships' operations and transactions, including, without limitation, acquisitions of additional properties, borrowing funds, raising new capital, leasing buildings, as well as selecting and supervising all employees and agents of the operating partnerships. Through our authority to manage our business and affairs, our Board of Directors directs the business of the operating partnerships.

Notwithstanding our effective control of the operating partnerships, the Berg Group holds a substantial majority of the outstanding O.P. Units and the consent of the limited partners holding a majority of the outstanding O.P. Units is required with respect to certain extraordinary actions involving the operating partnerships, including:

- the amendment, modification or termination of the operating partnership agreements;
- a general assignment for the benefit of creditors or the appointment of a custodian, receiver or trustee for any of the assets of the operating partnerships;
- the institution of any proceeding for bankruptcy of the operating partnerships;
- the transfer of any general partner interests in the operating partnerships, including, with certain exceptions, transfers attendant to any merger, consolidation or liquidation of our corporation;
- the admission of any additional or substitute general partner in the operating partnerships; and
- a change of control of the operating partnerships.

In addition, until the ownership interest of the Berg Group and its affiliates

is less than 15% of the common stock on a Fully Diluted basis, the consent of the limited partners holding a majority of the outstanding O.P. Units is also required with respect to:

- the liquidation of the operating partnerships;
- the sale or other transfer of all or substantially all of the assets of the operating partnerships and certain mergers and business combinations resulting in the complete disposition of all O.P. Units; and
- the issuance of limited partnership interests having seniority as to distributions, assets and voting over the O.P. Units.

TRANSFERABILITY OF O.P. UNITS

The operating partnership agreements provide that the limited partners may transfer their O.P. Units, subject to certain limitations. Except for certain transfers by the limited partners to or from certain of their affiliates, however, all transfers may be made only with our prior written consent as the sole general partner of the operating partnerships.

In addition, no transfer of O.P. Units by the limited partners may be made in violation of certain regulatory and other restrictions set forth in the operating partnership agreements. Except in the case of certain permitted transfers to or from certain affiliates of the limited partners, the exchange rights, the put rights, rights to participate in future equity financings and provisions requiring the approval of certain limited partners for certain matters will no longer be applicable to O.P. Units so transferred, and the transferee will not have any rights to nominate persons to our Board of Directors.

ADDITIONAL CAPITAL CONTRIBUTIONS AND LOANS

Each operating partnership agreement provides that, if the operating partnership requires additional funds to pursue its investment objectives, we may fund such investments by raising additional equity capital and making a capital contribution to the operating partnerships or by borrowing such funds and lending the net proceeds of such loans to the operating partnerships. If we intend to provide additional funds through a contribution to capital and purchase of units of general partner interest, the limited partners will have the right to participate in such funding on a pro rata, pari passu basis and to acquire additional O.P. Units. If the limited partners do not participate in such financing, we will acquire additional units of general partner interest. In either case, the number of additional units of partnership interest will be increased based upon the amount of the additional capital contributions and the value of the operating partnerships as of the date such contributions are made.



In addition, as general partner of the operating partnerships, we have the ability to cause the operating partnerships to issue additional O.P. Units. In the event that the operating partnerships issue new O.P. Units for cash but not property, the limited partners will have the right to purchase new O.P. Units at the price we offer in the transaction giving rise to such participation right in order, and to the extent necessary, to maintain their respective percentage interests in the operating partnerships.

EXCHANGE RIGHTS, PUT RIGHTS AND REGISTRATION RIGHTS

Under the Exchange Rights Agreement between us and the limited partners, the limited partners have exchange rights that generally became exercisable on

December 29, 1999. The Exchange Rights Agreement permits every limited partner to tender O.P. Units to us, and, at our election, to receive common stock on a one-for-one basis at then-current market value, an equivalent amount of cash, or a combination of cash and common stock in exchange for the O.P. Units tendered, subject to the 9% overall ownership limit imposed on non-Berg Group stockholders under our charter document, or the overall 20% Berg Group ownership limit, as the case may be. For more information, please refer to Item 1A, "Risk Factors - Failure to satisfy federal income tax requirements for REITs could reduce our distributions, reduce our income and cause our stock price to fall." This exchange ratio is subject to adjustment for stock splits, stock dividends, recapitalizations of our common stock and similar types of corporate actions. In addition, once in each 12-month period beginning each December 29, the limited partners, other than Carl E. Berg and Clyde J. Berg, may exercise a put right to sell their O.P. Units to the operating partnerships at a price equal to the average market price of the common stock for the 10-trading day period immediately preceding the date of tender. Upon any exercise of the put rights, we will have the opportunity for a period of 15 days to elect to fund the purchase of the O.P. Units and purchase additional general partner interests in the operating partnerships for cash, unless the purchase price exceeds $1 million in the aggregate for all tendering limited partners, in which case, the operating partnerships or we will be entitled, but not required, to reduce proportionally the number of O.P. Units to be acquired from each tendering limited partner so that the total purchase price is not more than $1 million. Through December 31, 2008 no limited partner ever has exercised this put right.

The number of shares of our common stock issuable in exchange for the total number of O.P. Units outstanding at July 1, 1998 and the O.P. Units issued pursuant to the Pending Projects Acquisition Agreement were registered under the Securities Act and generally may be sold without restriction if they are acquired by limited partners that are not affiliates, as defined under SEC Rule 144. For more information please refer to Item 1A, "Risk Factors - Shares eligible for future sale could affect the market price of our stock." The Exchange Rights Agreement gives the holders of O.P. Units the right to participate in any registered public offering of the common stock initiated by us to the extent of 25% of the total shares sold in the offering upon converting O.P. Units to shares of common stock, but subject to the underwriters' unlimited right to reduce the participation of all selling stockholders. The holders of O.P. Units will be able to request resale registrations of shares of common stock acquired on exchange of O.P. Units on a Form S-3, or any equivalent form of registration statement, subject to limitations and restrictions contained in the Exchange Rights Agreement. In April 2006, we registered up to 86,088,095 shares of common stock issuable on exchange of O.P. Units for resale pursuant to the prospectus included in a registration statement on Form S-3 that the SEC declared effective on April 28, 2006. We intend to maintain the effectiveness of this registration statement in order to facilitate re-sales of shares of common stock acquired by O.P. Unit holders from time to time without volume limitations or other resale restrictions under SEC Rule 144.

OTHER MATTERS

The operating partnership agreements require that the operating partnerships be operated in a manner that will enable us to satisfy the requirements for being classified as a REIT and to avoid any federal income or excise tax liability.

The operating partnership agreements provide that the combined net operating cash flow from all the operating partnerships, as well as net sales and refinancing proceeds, will be distributed from time to time as determined by our Board of Directors, but not less frequently than quarterly, pro rata in accordance with the partners' percentage interests in the operating partnerships, taken as a whole. This provision is intended to cause the periodic distributions per O.P. Unit and per share of our common stock to be equal. As a consequence of this provision, the capital interest of a partner in each of the

operating partnerships, including our capital interests, might at times differ significantly from the partner's percentage interest in the net income and cash flow of that operating partnership. We do not believe that such differences would have a material impact on our business, financial condition or funds available for distributions, however.

Pursuant to the operating partnership agreements, the operating partnerships will also assume and pay when due, or reimburse us for payment of, certain costs and expenses relating to our continuity of existence and operations.

The operating partnership agreements provide that, upon the exercise of an outstanding option under the 2004 Equity Incentive Plan (including options granted originally under the 1997 Stock Option Plan), we may purchase additional general partner interests in the operating partnerships by contributing the exercise proceeds to the operating partnerships. Our increased interest will be equal to the percentage of outstanding shares of common stock and O.P. Units on an as-converted basis represented by the shares acquired upon exercise of the option.



TERM

The operating partnerships will continue in full force and effect until December 31, 2048 or until sooner dissolved pursuant to the terms of the operating partnership agreements.

EMPLOYEES

As of February 28, 2009, we employed six people, all of whom work at our executive offices at 10050 Bandley Drive, Cupertino, California, 95014.

FACILITIES

We lease office space at 10050 Bandley Drive, Cupertino, California from Berg & Berg Enterprises, Inc. and share clerical staff and other overhead on what we consider to be favorable terms. The total monthly rent payable by us to Berg & Berg Enterprises, Inc. is $10,000.



ITEM 1A. RISK FACTORS

YOU SHOULD CAREFULLY CONSIDER THE FOLLOWING RISKS, TOGETHER WITH THE OTHER INFORMATION CONTAINED ELSEWHERE IN THIS FORM 10-K. THE FOLLOWING RISKS RELATE PRINCIPALLY TO OUR BUSINESS AND THE INDUSTRY IN WHICH WE OPERATE. THE RISKS AND UNCERTAINTIES CLASSIFIED BELOW ARE NOT THE ONLY ONES WE FACE.

SILICON VALLEY MARKET AND ECONOMIC CONDITIONS.

In the Silicon Valley, recent market and economic conditions have been unprecedented and challenging with tighter credit conditions and slower growth through the fourth quarter of 2008. For the year ended December 31, 2008, continued concerns about the systemic impact of inflation, energy costs, the availability and cost of credit and a declining real estate market have contributed to increased market volatility and diminished expectations for the

Silicon Valley economy. These conditions, combined with declining business and consumer confidence and increased unemployment have contributed to volatility of unprecedented levels.

As a result of these market conditions, the cost and availability of credit has been and may continue to be adversely affected by illiquid credit markets and wider credit spreads. Concern about the stability of the markets generally and the strength of counterparties specifically has led many lenders and institutional investors to reduce, and in some cases, cease to provide funding to borrowers. Continued turbulence in the Silicon Valley economy may adversely affect the financial condition and the liquidity and financial condition of our tenants and result in a significantly higher level of defaults. If these market conditions continue, they may limit our ability and the ability of our tenants, to timely refinance maturing liabilities and access the capital markets to meet liquidity needs, resulting in adverse effects on our financial condition and results of operations.

WE MAY NOT BE ABLE TO OBTAIN ADDITIONAL CAPITAL TO FURTHER OUR BUSINESS OBJECTIVES.

Our ability to acquire properties depends upon our ability to obtain capital. The real estate industry is currently experiencing a volatile capital market. The lack of capital is expected to cause a decrease in the level of new investment activity. An inability to obtain debt capital on acceptable terms could delay or prevent us from acquiring desirable investments.

WE ARE DEPENDENT ON CARL E. BERG, AND IF WE LOSE HIS SERVICES OUR BUSINESS MAY BE HARMED AND OUR STOCK PRICE COULD FALL.

We are substantially dependent upon the leadership of Carl E. Berg, our Chairman and Chief Executive Officer. Losing Mr. Berg's knowledge and abilities could have a material adverse effect on our business and the value of our common stock. Mr. Berg manages our day-to-day operations and devotes a significant portion of his time to our affairs, but he has a number of other business interests as well. These other activities reduce Mr. Berg's attention to our business.

MR. BERG AND HIS AFFILIATES EFFECTIVELY CONTROL OUR CORPORATION AND THE OPERATING PARTNERSHIPS AND MAY ACT IN WAYS THAT ARE DISADVANTAGEOUS TO OTHER STOCKHOLDERS.

SPECIAL BOARD VOTING PROVISIONS
Our governing corporate documents, which are our articles of amendment and restatement, or charter, and our bylaws, provide substantial control rights for the Berg Group. The Berg Group's control of our corporation means that the value and returns from an investment in the Company's common stock are subject to the Berg Group's exercise of its rights. These rights include a requirement that Mr. Berg or his designee as director approve certain fundamental corporate actions, including amendments to our charter and bylaws and any merger, consolidation or sale of all or substantially all of our assets. In addition, our bylaws provide that a quorum necessary to hold a valid meeting of the Board of Directors must include Mr. Berg or his designee. The rights described in the two preceding sentences apply only as long as the Berg Group members and their affiliates, other than us and the operating partnerships, beneficially own, in the aggregate, at least 15% of our outstanding shares of common stock on a Fully Diluted basis. Also, directors representing more than 75% of the entire Board of Directors must approve other significant transactions, such as incurring debt above certain amounts and conducting business other than through the operating partnerships. Without the approval of Mr. Berg or his designee, the Board of Directors' approval that we may need for actions that might result in a sale of your stock at a premium or raising additional capital when needed could be difficult or impossible to obtain.

BOARD OF DIRECTORS REPRESENTATION

The Berg Group members have the right to designate two of the director nominees submitted by our Board of Directors to stockholders for election, as long as the Berg Group members and their affiliates, other than us and the operating partnerships, beneficially own, in the aggregate, at least 15% of our outstanding shares of common stock calculated on a Fully Diluted basis. If the Fully Diluted ownership of the Berg Group members and their affiliates, other than us and the operating partnerships, is less than 15% but is at least 10% of the common stock, the Berg Group members have the right to designate one of the director nominees submitted by our Board of Directors to stockholders for election. Its right to designate director nominees affords the Berg Group substantial control and influence over the management and direction of our corporation. The Berg Group's interests could conflict with the interests of our stockholders and could adversely affect the price of our common stock.



SUBSTANTIAL OWNERSHIP INTEREST

The Berg Group currently owns O.P. Units representing approximately 74.1% of the equity interests in the operating partnerships and approximately 73.7% of our equity interests on a Fully Diluted basis as of December 31, 2008. The O.P. Units may be converted into shares of common stock, subject to limitations set forth in our charter and other agreements with the Berg Group, and upon conversion would represent voting control of our corporation. The Berg Group's ability to exchange its O.P. Units for common stock permits it to exert substantial influence over the management and direction of our corporation. This influence increases our dependence on the Berg Group.

LIMITED PARTNER APPROVAL RIGHTS

Mr. Berg and other limited partners, including other members of the Berg Group, may restrict our operations and activities through rights provided under the terms of the amended and restated agreement of limited partnership which governs each of the operating partnerships and our legal relationship to each operating partnership as its general partner. Matters requiring approval of the holders of a majority of the O.P. Units, which necessarily would include the Berg Group, include the following:

- the amendment, modification or termination of any of the operating partnership agreements;
- the transfer of any general partner interest in the operating partnerships, including, with certain exceptions, transfers attendant to any merger, consolidation or liquidation of our corporation;
- the admission of any additional or substitute general partners in the operating partnerships;
- any other change of control of the operating partnerships;
- a general assignment for the benefit of creditors or the appointment of a custodian, receiver or trustee for any of the assets of the operating partnerships; and
- the institution of any bankruptcy proceeding for any operating partnership.

In addition, as long as the Berg Group members and their affiliates, other than us and the operating partnerships, beneficially own, in the aggregate, at least 15% of the outstanding shares of common stock on a Fully Diluted basis, the consent of the limited partners holding the right to vote a majority of the total number of O.P. Units outstanding is also required with respect to:

- the sale or other transfer of all or substantially all of the assets of the operating partnerships and certain mergers and business combinations resulting in the complete disposition of all O.P. Units;
- the issuance of limited partnership interests senior to the O.P. Units as

to distributions, assets and voting; and
- the liquidation of the operating partnerships.

The liquidity of an investment in the Company's common stock, including our ability to respond to acquisition offers, will be subject to the exercise of these rights.

OUR CONTRACTUAL BUSINESS RELATIONSHIPS WITH THE BERG GROUP PRESENT ADDITIONAL CONFLICTS OF INTEREST, WHICH MAY RESULT IN THE REALIZATION OF ECONOMIC BENEFITS OR THE DEFERRAL OF TAX LIABILITIES BY THE BERG GROUP WITHOUT EQUIVALENT BENEFITS TO OUR STOCKHOLDERS.

Our contracts with the Berg Group provide it with interests that could conflict with those of our other stockholders, including the following:

- our headquarters are leased from an entity owned by the Berg Group, to whom we pay rent of $10,000 per month;
- the Berg Group is permitted to conduct real estate and business activities other than our business;
- if we decline an opportunity that has been offered to us, the Berg Group may pursue it, which would reduce the amount of time that Mr. Berg could devote to our affairs and could result in the Berg Group's development of properties that compete with our properties for tenants;
- in general, we have agreed to limit the liability of the Berg Group to our corporation and our stockholders arising from the Berg Group's pursuit of these other opportunities;
- we acquired most of our properties from the Berg Group on terms that were not negotiated at arm's length and without many customary representations and warranties that we would have sought in an acquisition from an unrelated party; and
- we have assumed liability for debt to the Berg Group and debt for which the Berg Group was liable.

The Berg Group has agreed that the Independent Directors Committee of our Board of Directors must approve all new transactions between us and any of its members, or between us and any entity in which it directly or indirectly owns 5% or more of the equity interests, including the operating partnerships for this purpose. This committee currently consists of three directors who are independent of the Berg Group.



BERG LAND HOLDINGS

The Berg Group owns several parcels of unimproved land in the Silicon Valley that the operating partnerships and we have the right to acquire under the terms of the Berg Land Holdings Option Agreement. We have agreed to pay an amount based on pre-negotiated terms for any of the properties that we do acquire. We must pay the acquisition price in cash unless the Berg Group elects, in its discretion, to receive O.P. Units valued at the average market price of a share of common stock during the 30-trading-day period preceding the acquisition date. At the time of acquisition, which is subject to the approval of the Independent Directors Committee, these properties may be encumbered by debt that we or the operating partnerships will be required to assume or repay. The use of our cash or an increase in our indebtedness to acquire these properties could have a material adverse effect on our financial condition, results of operations and ability to make cash distributions to our stockholders. This agreement will expire on December 31, 2010, after which we will no longer have the right to acquire properties from the Berg Group or the pre-determined terms provided in that agreement.

TERMS OF TRANSFERS: ENFORCEMENT OF AGREEMENT OF LIMITED PARTNERSHIP
The terms of the Pending Projects Acquisition Agreement, the Berg Land Holdings Option Agreement, the partnership agreement of each operating partnership and other material agreements through which we have acquired our interests in the operating partnerships and the properties formerly controlled by the Berg Group were not determined through arm's-length negotiations and could be less favorable to us than those obtained from an unrelated party. In addition, Mr. Berg and representatives of the Berg Group sitting on our Board of Directors may be subject to conflicts of interests with respect to their obligations as our directors to enforce the terms of the partnership agreement of each operating partnership when such terms conflict with their personal interests. The terms of our charter and bylaws also were not determined through arm's-length negotiations. Some of these terms, including representations and warranties applicable to acquired properties, are not as favorable as those that we would have sought through arm's-length negotiations with unrelated parties. As a result, an investment in our common stock may involve risks not found in businesses in which the terms of material agreements have been negotiated at arm's length.

RELATED PARTY DEBT
We are liable under a mortgage loan of approximately $8.8 million due June 2013, which was extended from the original maturity date of June 2010, in connection with our acquisition of the 5300-5350 Hellyer Avenue R&D properties that we acquired in May 2000 under the Berg Land Holdings Option Agreement. If we are unable to repay our debt to the Berg Group when due, the Berg Group could take action to enforce our payment obligations. Potential actions by the Berg Group to enforce these obligations could result in the foreclosure in one or more of our properties and a reduction in the amount of cash distributions to our stockholders. In turn, if we fail to meet the minimum distributions test because of a loan default or another reason, we could lose our REIT classification for federal income tax purposes. For more information please refer to Item 1A, "Risk Factors - Failure to satisfy federal income tax requirements for REITs could reduce our distributions, reduce our income and cause our stock price to fall."

OUR OPTION TO ACQUIRE R&D PROPERTIES DEVELOPED ON EXISTING LAND AND LAND ACQUIRED IN THE FUTURE BY THE BERG GROUP WILL TERMINATE WHEN THE BERG GROUP'S OWNERSHIP INTEREST HAS BEEN REDUCED, OR IF EARLIER, ON DECEMBER 31, 2010.

The Berg Land Holdings Option Agreement, as amended, which provides us with significant benefits and opportunities to acquire additional R&D properties from the Berg Group, will expire on the earlier of December 31, 2010 and the date on which the Berg Group and their affiliates (excluding us and the operating partnerships) own less than 65% of our common stock on a Fully Diluted basis. Although we do not currently perceive growth opportunities from the land that is subject to the Berg Land Holdings Option Agreement, it is possible that the termination of that agreement will result in limitation of our growth, which could cause our stock price to fall.

WE MAY CHANGE OUR INVESTMENT AND FINANCING POLICIES AND INCREASE YOUR RISK WITHOUT STOCKHOLDER APPROVAL.

Our Board of Directors determines the investment and financing policies of the operating partnerships and our policies with respect to certain other activities, including our business growth, debt capitalization, distribution, and operating policies. Our Board of Directors may amend these policies at any time without a vote of the stockholders. Changes in these policies could materially adversely affect our financial condition, results of operations and ability to make cash distributions to our stockholders, which could harm our business and cause our stock price to fall. For more information please refer to Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Policies with Respect to Certain Activities."

ANTI-TAKEOVER PROVISIONS IN OUR CHARTER COULD PREVENT ACQUISITIONS OF OUR STOCK AT A SUBSTANTIAL PREMIUM.

Provisions of our charter and our bylaws could delay, defer or prevent a transaction or a change in control of our corporation, or a similar transaction, that might involve a premium price for our shares of common stock or otherwise be in the best interests of our stockholders. Provisions of the Maryland general corporation law, which would apply to potential business combinations with acquirers other than the Berg Group or stockholders who invested in us in December 1998, also could prevent the acquisition of our stock for a premium, as discussed in "Certain Provisions of Maryland Law and of our Charter and Bylaws."



AN INVESTMENT IN OUR STOCK INVOLVES RISKS RELATED TO REAL ESTATE INVESTMENTS THAT COULD HARM OUR BUSINESS AND CAUSE OUR STOCK PRICE TO FALL.

RENTAL INCOME VARIES
Real property investments are subject to varying degrees of risk. Investment returns available from equity investments in real estate depend in large part on the amount of income earned and capital appreciation, which our properties generate, as well as our related expenses incurred. If our properties do not generate revenues sufficient to meet operating expenses, debt service and capital expenditures, our income and ability to make distributions to our stockholders will be adversely affected. Income from our properties may also be adversely affected by general economic conditions, local economic conditions such as oversupply of commercial real estate, the attractiveness of our properties to tenants and prospective tenants, competition from other available rental property, our ability to provide adequate maintenance and insurance, the cost of tenant improvements, leasing commissions and tenant inducements and the potential of increased operating costs, including real estate taxes.

EXPENDITURES FOR PROPERTY OWNERSHIP ARE FIXED
Income from properties and real estate values also are affected by a variety of other factors, such as governmental regulations and applicable laws, including real estate, zoning and tax laws, interest rate levels and the availability of financing. Various significant expenditures associated with an investment in real estate, such as mortgage payments, real estate taxes and maintenance expenses, generally are not reduced when circumstances cause a reduction in revenue from the investment. Thus, our operating results and our cash flow may decline materially if our rental income is reduced.

ILLIQUIDITY
Real estate investments are relatively illiquid, which limits our ability to restructure our portfolio in response to changes in economic or other conditions.

GEOGRAPHIC CONCENTRATION
All of our properties are located in the southern portion of the San Francisco Bay Area commonly referred to as the "Silicon Valley." The Silicon Valley economy has weakened after relatively recent years and there remains significant excess capacity for R&D properties in the Silicon Valley. At present, future increases in values and rents for our properties depend to a significant extent on a strong recovery of this region's economy, which we do not currently foresee.

LOSS OF KEY TENANTS
Single tenants, many of whom are large, publicly traded information technology companies, occupy most of our properties. We may lose tenants when existing leases expire because it may be difficult to re-lease the same property due to

substantial overcapacity of R&D properties in the Silicon Valley at present. Losing a key tenant could adversely affect our operating results and our ability to make distributions to stockholders if we are unable to obtain replacement tenants promptly. Moreover, to retain key tenants upon the expiration of existing leases we may need to reduce rents, which also could adversely affect our operating results and ability to make distributions.

TENANT BANKRUPTCIES

Key tenants could seek the protection of the bankruptcy laws, which could result in the rejection and termination of their leases, thereby causing a reduction in our rental income. Under the bankruptcy laws, these tenants may have the right to reject their leases with us and our claim for rent will be limited to the greater of one year or 15% of the total amount owing under the leases upon default, but not to exceed three years of the remaining term of the lease following the earlier of the petition filing date or the date on which we gained repossession of the property, as well as any rent that was unpaid on the earlier of those dates.

OUR SUBSTANTIAL INDEBTEDNESS

Our properties are subject to substantial indebtedness. If we are unable to make required mortgage payments, we could sustain a loss as a result of foreclosure on our properties by the mortgagor. Furthermore, our mortgage loans may be subject to covenants that we are obligated to satisfy. For example, under our mortgage loan agreements with Northwestern Mutual Life Insurance Company, the payment of all $100 million outstanding could be accelerated upon the sale or certain other transfers of more than 51% of the total number of O.P. Units and shares of common stock of the Company held by the members of the Berg Group. We have no reason to expect such a sale or transfer in the foreseeable future, but the members of the Berg Group have no obligation to us to refrain from any such sale or other transfer. We have adopted a policy of maintaining a consolidated ratio of debt to total market capitalization, which includes for this purpose the market value of all shares of common stock for which outstanding O.P. Units are exchangeable, of less than 50%. This ratio may not be exceeded without the approval of more than 75% of our entire Board of Directors. Our Board of Directors may vote to change this policy, however, and we could become more highly leveraged, resulting in an increased risk of default on our obligations and an increase in debt service requirements that could adversely affect our financial condition, our operating results and our ability to make distributions to our stockholders.



ENVIRONMENTAL CLEAN-UP LIABILITIES

Our properties may expose us to liabilities under applicable environmental and health and safety laws. If these liabilities are material, our financial condition and ability to pay cash distributions may be affected adversely, which would cause our stock price to fall.

UNINSURED LOSSES

We may sustain uninsured losses with respect to some of our properties. If these losses are material, our financial condition, our operating results and our ability to make distributions to our stockholders may be affected adversely.

EARTHQUAKE DAMAGES ARE UNINSURED

All of our properties are located in areas that are subject to earthquake activity. Our insurance policies do not cover damage caused by seismic activity although they do cover losses from fires after an earthquake. We generally do not consider such insurance coverage to be economical. If an earthquake occurs and results in substantial damage to our properties, we could lose our

investment in those properties, which loss could have a material adverse effect on our financial condition, our operating results and our ability to make distributions to our stockholders.

OUR REAL ESTATE ASSETS MAY BE SUBJECT TO IMPAIRMENT CHARGES.

We continually evaluate the recoverability of the carrying value of our real estate assets for impairment indicators. Factors considered in evaluating impairment of our existing real estate assets include significant declines in property operating profits, recurring property operating losses and other significant adverse changes in general market conditions that are considered permanent in nature. Generally, a real estate asset is not considered impaired if the undiscounted, estimated future cash flows of the asset over its estimated holding period are in excess of the asset's net book value at the balance sheet date. Assumptions used to estimate annual and residual cash flow, the estimated holding period of such assets, the lease up period when properties are vacant and future rental income require the judgment of management. Actual results could be different than our estimates.

There can be no assurance that we will not take impairment charges in the future related to the impairment of our assets. As of the years ended December 31, 2008 and 2007, management believed it had applied reasonable estimates and judgments in determining the proper classification of its real estate assets. However, should external or internal circumstances change requiring the need to shorten the holding periods or adjust the estimated future cash flows of certain of our assets, we could be required to record additional impairment charges. If any real estate asset held for sale is considered impaired, a loss is provided to reduce the carrying value of the asset to its fair value, less selling costs. Any future impairment could have a material adverse affect on the Company's results of operations and funds from operations in the period in which the charge is taken.

FAILURE TO SATISFY FEDERAL INCOME TAX REQUIREMENTS FOR REITS COULD REDUCE OUR DISTRIBUTIONS, REDUCE OUR INCOME AND CAUSE OUR STOCK PRICE TO FALL.

FAILURE TO QUALIFY AS A REIT
Although we currently operate in a manner designed to enable us to qualify and maintain our REIT status, it is possible that economic, market, legal, tax or other considerations may cause us to fail to qualify as a REIT or may cause our Board of Directors either to refrain from making the REIT election or to revoke that election once made. To maintain REIT status, we must meet certain tests for income, assets, distributions to stockholders, ownership interests, and other significant conditions. If we fail to qualify as a REIT in any taxable year, we will not be allowed a deduction for distributions to our stockholders in computing our taxable income and would be subject to federal income tax, including any applicable alternative minimum tax, on our taxable income at regular corporate rates. Moreover, unless we were entitled to relief under certain provisions of the tax laws, we would be disqualified from treatment as a REIT for the four taxable years following the year in which our qualification was lost. As a result, funds available for distributions to our stockholders would be reduced for each of the years involved and, in addition, we would no longer be required to make distributions to our stockholders.

REIT DISTRIBUTION REQUIREMENTS
To maintain REIT status, we must distribute as a dividend to our stockholders at least 90% of our otherwise net taxable income, after certain adjustments, with respect to each tax year. We also may be subject to a 4% non-deductible excise tax in the event our distributions to stockholders fail to meet certain other requirements. Failure to comply with these requirements could result in our income being subject to tax at regular corporate rates and could cause us to be liable for the excise tax.

OWNERSHIP LIMIT NECESSARY TO MAINTAIN REIT QUALIFICATION

As a REIT, the federal tax laws restrict the percentage of the total value of our stock that may be owned by five or fewer individuals to 50% or less. Our charter generally prohibits the direct or indirect ownership of more than 9% of our common stock by any stockholder. This limit excludes the Berg Group, which has an aggregate ownership limit of 20%. In addition, as permitted by our charter, our Board of Directors has authorized an exception applicable to two other stockholders that permits them to collectively own, directly or indirectly, up to 18.5% of our common stock on an aggregate basis, subject to the terms of an ownership limit exemption agreement. In general, our charter prohibits the transfer of shares that result in a loss of our REIT qualification and provides that any



such transfer or any other transfer that causes a stockholder to exceed the ownership limit will result in the shares being automatically transferred to a trust for the benefit of a charitable beneficiary. Accordingly, in the event that either the Berg Group or the two stockholders increase their stock ownership in our corporation, a stockholder who acquires shares of our common stock, even though his, her or its aggregate ownership may be less than 9%, may be required to transfer a portion of that stockholder's shares to such a trust in order to preserve our status as a REIT.

STOCKHOLDERS ARE NOT ASSURED OF RECEIVING CASH DISTRIBUTIONS FROM US.

Our income consists primarily of our share of the income of the operating partnerships, and our cash flow consists primarily of our share of distributions from the operating partnerships. Differences in timing between the receipt of income and the payment of expenses in arriving at our taxable income or the taxable income of the operating partnerships and the effect of required debt amortization payments could require us to borrow funds, directly or through the operating partnerships, on a short-term basis to meet our intended distribution policy.

Our Board of Directors will determine the amount and timing of distributions by the operating partnerships and of distributions to our stockholders. Our Board of Directors will consider many factors prior to making any distributions, including the following:

- the amount of cash available for distribution;
- availability of financing;
- our financial condition;
- whether to reinvest funds rather than to distribute such funds;
- our committed and projected capital expenditures;
- the amount of cash required for new property acquisitions, including acquisitions under our existing agreements with the Berg Group;
- the amount of our annual debt service requirements;
- the annual distribution requirements under the REIT provisions of the federal income tax laws;
- our projected rental rates and revenues;
- our ability to collect rent payments;
- prospects of tenant renewals and re-leases of properties subject to expiring leases;
- cash required for re-leasing activities; and o such other factors as our Board of Directors deem relevant.

We cannot assure you that we will be able to meet or maintain our cash distribution objectives.

OUR PROPERTIES COULD BE SUBJECT TO PROPERTY TAX REASSESSMENTS.

We do not believe that the acquisition of any of our interests in the operating partnerships has resulted in a statutory change in ownership that could give rise to a reassessment of any of our properties for California property tax purposes. We cannot assure you, however, that county assessors or other tax administrative agencies in California will not attempt to assert that such a change occurred as a result of these transactions. Although we believe that such a challenge would not be successful ultimately, we cannot assure you regarding the outcome of any related dispute or proceeding. A reassessment could result in increased real estate taxes on our properties that, as a practical matter, we may be unable to pass through to our tenants in full. This could reduce our net income and our funds available for distributions and cause our stock price to fall.

OUR OBLIGATION TO PURCHASE TENDERED O.P. UNITS COULD REDUCE OUR CASH DISTRIBUTIONS.

Each of the limited partners of the operating partnerships, other than Carl E. Berg and Clyde J. Berg, has the annual right to cause the operating partnerships to purchase the limited partner's O.P. Units at a purchase price based on the average market value of the common stock for the ten-trading-day period immediately preceding the date of tender. Upon a limited partner's exercise of any such right, we will have the option to purchase the tendered O.P. Units with available cash, borrowed funds or the proceeds of an offering of newly issued shares of common stock. These put rights became exercisable on December 29, 1999, and are available once during a 12-month period. If the total purchase price of the O.P. Units tendered by all of the eligible limited partners in one year exceeds $1 million, the operating partnerships or we will be entitled, but not required, to reduce proportionately the number of O.P. Units to be acquired from each tendering limited partner so that the total purchase price does not exceed $1 million. Thus, we might repurchase O.P. Units for a total purchase price of more than $1 million in one year. The exercise of these put rights may reduce the amount of cash that we have available to distribute to our stockholders and could cause our stock price to fall.

In addition, all O.P. Unit holders may tender their O.P. Units to us in exchange for shares of common stock on a one-for-one basis at then-current market value or an equivalent amount in cash, at our election. If we elect to pay cash for the O.P. Units, our liquidity may

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be reduced and we may lack sufficient funds to continue paying the amount of our anticipated or historical cash distributions. This could cause our stock price to fall.

SHARES ELIGIBLE FOR FUTURE SALE COULD AFFECT THE MARKET PRICE OF OUR STOCK.

We cannot predict the effect, if any, that future sales of shares of common stock, or the availability of shares for future sale, could have on the market price of our common stock. As of December 31, 2008, all outstanding shares of our common stock, other than shares controlled by affiliates, were eligible for sale in the public market without resale restrictions under the federal securities laws. Sales of substantial amounts of common stock, including shares issued in connection with the exercise of the exchange rights held by the limited partners of the operating partnerships, or the perception that such sales could occur, could adversely affect prevailing market prices for the common stock. Additional shares of common stock may be issued to limited partners, subject to the applicable REIT qualification ownership limit, if they exchange their O.P. Units for shares of common stock pursuant to their exchange rights, or may be sold by us to raise funds required to purchase such O.P. Units

if eligible limited partners elect to tender O.P. Units to us using their put rights. Shares of stock controlled by our affiliates may be sold subject to Rule 144, including the limitation under Rule 144(e) on the number of shares that may be sold within a three-month period. In addition, pursuant to a registration statement on Form S-3 declared effective by the SEC in April 2006, all shares of common stock acquired upon exchange of currently outstanding O.P. Units may be resold without any such restrictions. Additional common stock reserved under our 2004 Equity Incentive Plan, including stock options, also may be sold in the market at some time in the future. Future sales of our common stock in the market could adversely affect the price of our common stock.

MARKET INTEREST RATES MAY REDUCE THE VALUE OF THE COMMON STOCK.

One of the factors that investors consider important in deciding whether to buy or sell shares of a REIT is the distribution rate on such shares, as a percentage of the price of such shares, relative to market interest rates. If market interest rates go up, prospective purchasers of REIT shares may expect a higher distribution rate. Higher interest rates would not, however, increase the funds available for us to distribute, and, in fact, would likely increase our borrowing costs and decrease funds available for distributions. Thus, higher market interest rates could cause the price of our common stock to fall.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

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ITEM 2. PROPERTIES

GEOGRAPHIC AND TENANT FOCUS

We focus principally on the facility requirements of information technology companies in the Silicon Valley, which include space for office, R&D, light manufacturing and assembly. With the Silicon Valley's highly educated and skilled work force, history of numerous successful start-up companies and large contingent of venture capital firms, we believe that this region will, following the current significant slowdown in the market, continue to spawn successful new high-growth industries and entrepreneurial businesses to an extent matched nowhere else in the United States. We believe that our focus and thorough understanding of the Silicon Valley real estate market enables us to:

- anticipate trends in the market;
- identify and concentrate our efforts on the most favorably located sub-markets;
- take advantage of our experience and extensive contacts and relationships with local government agencies, real estate brokers and subcontractors, as well as with tenants and prospective tenants; and
- identify strong tenants.

All of our properties are general-purpose R&D/office type properties located in desirable sub-markets of the Silicon Valley. Many of our properties have been developed for or leased to single tenants, many of whom are large, publicly traded information technology companies. Most of our major tenants have occupied our properties for many years under triple-net leases that require the tenant to pay substantially all operating costs, including property insurance, real estate taxes and general operating costs.

LEASING

The current leases for our properties have terms ranging from month-to-month to 12 years. Most of the leases provide for fixed periodic rental increases. Substantially all of the leases are triple-net leases pursuant to which the tenant is required to pay substantially all of the property operating expenses, including all maintenance and repairs, property taxes and insurance, and excluding only certain structural repairs to the building shell. Most of the leases contain renewal options that allow the tenant to extend the lease based on adjustments to then prevailing market rates, or based on fixed rental adjustments, which may be at or below market rates.

PROPERTY PORTFOLIO

All of our properties are R&D/office type properties. Generally, these properties are one- to two-story buildings of tilt-up concrete construction, have on average 3.5 or more parking spaces per thousand rentable square feet, clear ceiling heights of less than 18 feet, and range in size from approximately 4,500 to 211,000 rentable square feet. Most of the office space is open and suitable for configuration to meet the tenants' requirements with the use of movable dividers.

The following table sets forth certain information relating to our properties as of December 31, 2008:

| Location | No. of Properties | Total Rentable Sq. Ft. | Percentage Occupied as of Dec. 31, 2008 | Average 2008 Occupancy | Major Tenants |
|---|---|---|---|---|---|
| 5300-5350 Hellyer Avenue (2) | 2 | 160,000 | 100% | 100% | Tyco Electronics Cor |
| 10401-10411 Bubb Road (2) | 1 | 20,330 | 78% | 78% | Aeroflex, Inc. |
| 45365 Northport Loop West | 1 | 64,218 | 0% | 0% | Vacant |
| 45738 Northport Loop West | 1 | 44,256 | 100% | 100% | Quicksil, Inc. |
| 4050 Starboard Drive | 1 | 52,232 | 100% | 100% | Flash Electronics, I |
| 3501 West Warren Avenue & 46600 Fremont Boulevard | 1 | 67,864 | 24% | 63% | Oakland Fluid System |
| 48800 Milmont Drive | 1 | 53,000 | 0% | 0% | Vacant |
| 4750 Patrick Henry Drive | 1 | 63,105 | 100% | 100% | Infoblox, Inc. |
| Triangle Technology Park (2) | 7 | 416,927 | 73% | 77% | Intevac Corporation<br>Xicom Technology, In<br>LSA Cleanpart, LLC<br>SASCO |



Total Percentage Average

| Location | No. of Properties | Rentable Sq. Ft. | Occupied as of Dec. 31, 2008 | 2008 Occupancy | Major Tenants |
|---|---|---|---|---|---|
| 5830-5870 Hellyer Avenue | 1 | 109,715 | 24% | 24% | MeiVac, Inc. |
| 5750 Hellyer Avenue | 1 | 73,312 | 100% | 100% | NDS Surgical Imaging |
| 5500-5550 Hellyer Avenue | 2 | 196,534 | 66% | 20% | CTS Corporation<br>Snap-on, Inc. |
| 5400 Hellyer Avenue | 1 | 77,184 | 73% | 69% | Nortel Networks, Inc<br>Capella, Inc. |
| 5325-5345 Hellyer Avenue | 2 | 256,500 | 100% | 100% | Celestica Asia, Inc. |
| 5905-5965 Silver Crk Valley Rd. | 4 | 346,000 | 0% | 0% | Vacant |
| 5845 Hellyer Avenue | 1 | 98,500 | 0% | 0% | Vacant |
| 855 Embedded Way | 1 | 67,912 | 100% | 47% | Celestica Asia, Inc.<br>Lynuxworks, Inc. |
| 1065-1105 La Avenida Street | 5 | 515,700 | 100% | 100% | Microsoft Corporatio |
| 1875 Charleston Road | 1 | 42,126 | 100% | 100% | Netlogic Microsystem |
| 1750 Automation Parkway | 1 | 80,641 | 100% | 100% | JDS Uniphase Corpora |
| 1756 Automation Parkway | 1 | 80,640 | 36% | 36% | A&D Engineering, Inc |
| 1762 Automation Parkway | 1 | 61,100 | 100% | 100% | Hermes Microvision, |
| 1768 Automation Parkway | 1 | 110,592 | 67% | 86% | 2Wire, Inc. |
| 255 Caspian Drive | 1 | 119,756 | 100% | 100% | Equinix Operating Co |
| 245 Caspian Drive (3) | 1 | - | - | - | - |
| 5981 Optical Court | 1 | 110,542 | 100% | 100% | SoloPower, Inc. |
| 5970 Optical Court | 1 | 128,520 | 100% | 100% | Photon Dynamics, Inc |
| 5900 Optical Court | 1 | 165,000 | 100% | 100% | Stryker Corporation |
| 2630 Orchard Parkway | 1 | 60,633 | 0% | 0% | Vacant |
| 2610 Orchard Parkway | 1 | 54,093 | 0% | 0% | Vacant |
| 55 West Trimble Road | 1 | 91,722 | 0% | 0% | Vacant |
| 2001 Walsh Avenue | 1 | 80,000 | 100% | 100% | Nvidia Corporation |
| 2880 Scott Boulevard | 1 | 200,000 | 100% | 100% | NEC Electronics Amer |
| 2890 Scott Boulevard | 1 | 75,000 | 100% | 50% | Nvidia Corporation |
| 2770-2800 Scott Boulevard | 1 | 99,800 | 100% | 100% | Nvidia Corporation |
| 2300 Central Expressway | 1 | 46,338 | 100% | 100% | Juniper Networks, In |
| 2220 Central Expressway | 1 | 62,522 | 100% | 100% | Tellabs, Inc. |

| | | | | | |
|---|---|---|---|---|---|
| 2330 Central Expressway | 1 | 62,522 | 100% | 100% | Tellabs, Inc. |
| 233 South Hillview Drive | 2 | 95,690 | 100% | 100% | Exar Corporation |
| 2251 Lawson Lane | 1 | 125,000 | 51% | 7% | Synaptics, Inc. |
| 1230 East Arques | 1 | 60,000 | 100% | 100% | Fujitsu |
| 1250 East Arques | 4 | 200,000 | 100% | 100% | Fujitsu |

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| Location | No. of Properties | Total Rentable Sq. Ft. | Percentage Occupied as of Dec. 31, 2008 | Average 2008 Occupancy | Major Tenants |
|---|---|---|---|---|---|
| 20400 Mariani Avenue | 1 | 105,000 | 100% | 75% | Apple, Inc. |
| 10500 De Anza Boulevard | 1 | 211,000 | 100% | 100% | Apple, Inc. |
| 20605-705 Valley Green Drive | 2 | 142,000 | 100% | 100% | Apple, Inc. |
| 10300 Bubb Road | 1 | 23,400 | 100% | 100% | Apple, Inc. |
| 10440 Bubb Road | 1 | 19,500 | 100% | 100% | Novare Surgical Syst |
| 10450-10460 Bubb Road | 1 | 45,460 | 100% | 100% | Ricoh Corporation<br>VMWare, Inc. |
| 1135 Kern Avenue | 1 | 18,300 | 0% | 0% | Vacant |
| 450 National Avenue | 1 | 36,100 | 0% | 20% | Vacant |
| 3301 Olcott Street | 1 | 64,500 | 0% | 0% | Vacant |
| 2800 Bayview Avenue | 1 | 59,736 | 0% | 0% | Vacant |
| 5521 Hellyer Avenue | 1 | 203,800 | 44% | 44% | Nanosolar, Inc. |
| 6850 Santa Teresa Boulevard | 1 | 30,000 | 41% | 41% | Bio-Medical Applicat |
| 6810 Santa Teresa Boulevard & 180 Great Oaks Boulevard | 1 | 54,996 | 87% | 87% | ZiLOG, Inc. |
| 140-160 Great Oaks Boulevard & 6781 Via Del Oro | 2 | 105,300 | 75% | 75% | Semiconductor Toolin<br>Santa Clara Valley W |
| 6540-6541 Via Del Oro & 6385-6387 San Ignacio Avenue | 2 | 66,600 | 71% | 73% | Modutek Corporation |
| 6311-6351 San Ignacio Avenue | 5 | 362,767 | 55% | 48% | Saint Gobain<br>Stion Corporation<br>Teledex, LLC |
| 6320-6360 San Ignacio Avenue | 1 | 157,292 | 12% | 12% | Quantum 3D, Inc. |
| 75 East Trimble Road & 2610 North First Street | 2 | 170,810 | 59% | 59% | Comerica, Inc. |

| | | | | | |
|---|---|---|---|---|---|
| 2904 Orchard Parkway | 1 | 75,335 | 100% | 100% | BAE Systems Land & A |
| 3236 Scott Boulevard | 1 | 54,672 | 100% | 100% | Mimix Broadband, Inc |
| 1212 Bordeaux Lane | 1 | 71,800 | 100% | 100% | Loral Space & Communications, Inc. |
| McCandless Technology Park | 14 | 705,958 | 22% | 24% | ST Assembly Test Ser Consentry Networks, |
| 1600 Memorex Drive | 1 | 107,500 | 21% | 21% | International Networ Services, Inc. |
| 1688 Richard Avenue | 1 | 52,800 | 100% | 100% | NWE Technology, Inc. |
| 1700 Richard Avenue | 1 | 58,783 | 100% | 100% | Cincinnati Bell, Inc |
| Morgan Hill Land (4) | - | - | - | - | - |
| 300 Montague Expressway | 1 | 49,457 | 0% | 1% | Vacant |
| 337 Trade Zone Boulevard | 1 | 42,912 | 0% | 0% | Vacant |
| 324-368 Montague Expressway | 1 | 56,265 | 0% | 0% | Vacant |
| TOTAL | 111 | 8,047,569 | 66% | | |



(1) Annual cash rents do not include the recognition of rental income on the straight-line method of accounting required by accounting principles generally accepted in the United States of America ("GAAP") under which contractual rent payment increases are recognized evenly over the lease term.
(2) Joint venture properties.
(3) Property represents a commitment by the Berg Group to construct an approximate 75,000 to 90,000 square foot building on land acquired during 2001.
(4) This property comprises of 55 acres of vacant land, which could support approximately 800,000 rentable square feet of space. The vacant land is currently zoned for industrial use and a portion has the potential to be rezoned for residential use.

We own 100% of all of the properties listed in the table, except: one of the buildings in the Triangle Technology Park, which is owned by a joint venture in which we, through an operating partnership, own a 75% interest; the property at 10401-10411 Bubb Road, which is owned by a joint venture in which we, through an operating partnership, own an 83.33% interest; and the properties at 5300-5350 Hellyer Avenue, which are owned by a joint venture in which we, through an operating partnership, own a 50% interest, and a Berg affiliate owns the other 50% venture interest.

SCHEDULE OF LEASE EXPIRATIONS

The following table sets forth a schedule of the lease expirations for the properties beginning with 2009, assuming that none of the tenants exercise existing renewal options or termination rights. The table excludes 2,701,554

rentable square feet that were vacant as of December 31, 2008.

| Year of Lease Expiration | Number of Expiring Leases | Rentable Square Footage Subject to Expiring Leases | 2009 Annual Base Rent Under Expiring Leases (1) | Perce Base E |
|---|---|---|---|---|
| 2009 | 22 | 369,613 | $1,777,373 | |
| 2010 | 12 | 572,000 | 9,298,560 | |
| 2011 | 15 | 827,605 | 12,225,746 | |
| 2012 | 13 | 1,001,452 | 14,883,768 | |
| 2013 | 6 | 459,737 | 5,801,817 | |
| 2014 | 11 | 1,281,952 | 23,158,141 | |
| 2015 | 4 | 328,211 | 6,313,276 | |
| 2016 | 2 | 144,600 | 2,959,748 | |
| 2017 | 3 | 241,089 | 3,050,940 | |
| Thereafter | 1 | 119,756 | 2,608,286 | |
| | 89 | 5,346,015 | $82,077,655 | |

(1) The base rent for expiring leases is based on 2009 scheduled cash rent, which is different than annual rent determined in accordance with GAAP.
(2) Based upon 2009 cash rent as discussed in Note (1).

If we are unable to lease a significant portion of the available space or space scheduled to expire in 2009 and thereafter at any of our properties; if existing tenants do not renew their leases; or if rental rates decrease, our results of operations, financial condition and cash flows would be affected adversely.

ENVIRONMENTAL MATTERS

To date, compliance with laws and regulations relating to the protection of the environment, including those regarding the discharge of materials into the environment has not had any material effects upon our capital expenditures, earnings or competitive position.

Under various federal, state and local laws, ordinances and regulations, an owner or operator of real property may be held liable for the costs of removal or remediation of certain hazardous or toxic substances located on or in the property. Such laws often impose liability on the owner and expose the owner to governmental proceedings without regard to whether the owner knew of, or was responsible for, the presence of the hazardous or toxic substances. The cost of any required remediation or removal of such substances may be substantial. In addition, the owner's liability as to any specific property is generally not limited and could exceed the value of the property and/or the aggregate assets of the owner. The presence of such substances, or the failure to properly remove

or remediate such substances, may also adversely affect the owner's ability to sell or rent the property or to borrow using the property as collateral. Persons who arrange for treatment or the disposal of hazardous or toxic substances may also be liable for the costs of any required



remediation or removal of the hazardous or toxic substances at a disposal facility, regardless of whether the facility is owned or operated by such owner or entity. In connection with the ownership of the properties or the treatment or disposal of hazardous or toxic substances, we may be liable for such costs.

Some of our properties are leased, in part, to businesses, including manufacturers that use, store or otherwise handle hazardous or toxic substances in their business operations. These operations create a potential for the release of hazardous or toxic substances. In addition, groundwater contaminated by chemicals used in various manufacturing processes, including semiconductor fabrication, underlies a significant portion of northeastern Santa Clara County, where many of our properties are located.

Environmental laws also govern the presence, maintenance and removal of asbestos. These laws require that owners or operators of buildings containing asbestos properly manage and maintain the asbestos, that they adequately inform or train those who may come into contact with asbestos and that they undertake special precautions, including removal or other abatement in the event that asbestos is disturbed during renovation or demolition of a building. These laws may impose fines and penalties on building owners or operators for failure to comply with these requirements and may allow third parties to seek recovery from owners or operators for personal injury associated with exposure to asbestos fibers. We are aware that there are asbestos-containing materials, or ACMs, present at several of the properties, primarily in floor coverings. We believe that the ACMs present at these properties are generally in good condition and that no ACMs are present at the remaining properties. We believe we are in compliance in all material respects with all present federal, state and local laws relating to ACMs and that if we were given limited time to remove all ACMs present at the properties, the cost of such removal would not have a material adverse effect on our financial condition, results of operations and ability to make cash distributions to our stockholders.

Phase I assessments are intended to discover and evaluate information regarding the environmental condition of the surveyed property and surrounding properties. Phase I assessments generally include a historical review, a public records review, an investigation of the surveyed site and surrounding properties and the preparation and issuance of a written report, but do not include soil sampling or subsurface investigations and typically do not include an asbestos survey. Environmental assessments have been conducted for about half of the properties.

The environmental investigations that have been conducted on our properties have not revealed any environmental liability that we believe would have a material adverse effect on our financial condition, results of operations and assets, and we are not aware of any such liability. Nonetheless, it is possible that there are material environmental liabilities of which we are unaware. We cannot assure you that future laws, ordinances, or regulations will not impose any material environmental liability, or that the current environmental condition of the properties has not been, or will not be, affected by tenants and occupants of the properties, by the condition of properties in the vicinity of the properties, or by third parties unrelated to us.

ITEM 3. LEGAL PROCEEDINGS

Neither the operating partnerships, our properties nor we are subject to any material litigation nor, to our knowledge, is any material litigation threatened against the operating partnerships, our properties or us. From time to time, we are engaged in legal proceedings arising in the ordinary course of our business. We do not expect any of such proceedings to have a material adverse effect on our cash flows, financial condition or results of operations. We are currently involved in the following legal proceedings and we believe that the ultimate outcome of these proceedings will not have a material adverse effect on our operating results, cash flows or financial condition.

Mission West Properties, L.P. v. Republic Properties Corporation, et al. Santa Clara County Superior Court, Case No. CV 796249. In February 2001, while the Maryland case was pending, we filed a suit against RPC in the Superior Court of the State of California for the County of Santa Clara, Case No. CV 796249. The case was stayed pending resolution of the Maryland case, and we dismissed our suit on March 4, 2005. In April 2005, RPC submitted a motion asking the Superior Court to reinstate the case, which the Court granted on May 25, 2005. On July 5, 2006, RPC filed a cross-complaint in the case seeking partnership distributions to which we demurred. The Court sustained our demurrer with leave to amend. Subsequently, RPC filed an amended complaint, and we submitted another demurrer seeking dismissal of the claims on statute of limitations grounds. On February 20, 2007, the Court overruled our demurrer. We sought a writ from the California State Court of Appeal for the Sixth District to direct the lower court to reverse its decision, but the petition for the writ was denied. In April 2008, we filed a motion for summary judgment in the California Superior Court which was denied. In October 2008, a motion filed by RPC for summary judgment in the California Superior Court was denied. A trial in the California Superior Court commenced in February 2009.

The Independent Directors Committee of the Board of Directors has exercised the right to acquire on behalf of the Company the former RPC interest and related distributions from Berg & Berg Enterprises, Inc. under the terms of the Berg Land Holdings Option Agreement between the Company and the Berg Group if the litigation is ultimately decided in favor of the Company, as more fully explained under Item 8, "Financial Statements and Supplementary Data - Note 13."

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of stockholders during the fourth quarter of the year ended December 31, 2008.



PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

HISTORICAL PERFORMANCE COMPARISON

The following graph compares the change in the Company's cumulative stockholder return on its shares of common stock to the cumulative total return of the

NAREIT Equity REIT Total Return Index ("NAREIT Equity Index") and the Standard & Poor's 500 Stock Index ("S&P 500 Index") from December 31, 2003 to December 31, 2008. The line graph starts December 31, 2003. The graph assumes that the value of the investment in the Company's common stock was $100 at December 31, 2003 and that all dividends were reinvested. The common stock's price on December 31, 2003 was $12.95. The Company obtained the information about the NAREIT Equity Index and S&P 500 Index from each entity respectively, and has assumed that the information is reliable, but cannot assume its accuracy.

[OBJECT OMITTED]

The stock price performance shown in the graph is not necessarily indicative of future performance of the Company's common stock.

Our common stock is listed on the Nasdaq Stock Market, LLC ("NASDAQ") and trades under the symbol "MSW." The closing price of our common stock on December 31, 2008, the last trading day of the year, was $7.65 per share. The high and low closing price per share of common stock as reported on NASDAQ during each quarter of 2008 and 2007 were as follows:

| | 2008 | | 2007 | |
|---|---|---|---|---|
| | High | Low | High | Lo |
| 1st Quarter | $10.13 | $8.36 | $14.60 | $11 |
| 2nd Quarter | $12.39 | $9.45 | $14.85 | $13 |
| 3rd Quarter | $11.36 | $8.58 | $14.01 | $11 |
| 4th Quarter | $9.27 | $6.11 | $12.50 | $9 |



On February 28, 2009, there were 171 registered holders of the Company's common stock.

DIVIDEND POLICY

We declared and paid dividends in each quarter of 2008 and 2007. We expect to pay quarterly dividends during 2009. The following tables show information for quarterly dividends for 2008 and 2007.

| | 2008 | | |
|---|---|---|---|
| | Record Date | Payment Date | Dividend Per Share |
| 1st Quarter | 03/31/08 | 04/03/08 | $0.20 |
| 2nd Quarter | 06/30/08 | 07/03/08 | 0.20 |
| 3rd Quarter | 09/30/08 | 10/09/08 | 0.20 |
| 4th Quarter | 12/31/08 | 01/08/09 | 0.20 |

| | | | |
|---|---|---|---|
| Total | | | $0.80 |

| | 2007 | | |
|---|---|---|---|
| | Record Date | Payment Date | Dividend Per Share |
| 1st Quarter | 03/30/07 | 04/05/07 | $0.16 |
| 2nd Quarter | 06/30/07 | 07/05/07 | 0.16 |
| 3rd Quarter | 09/28/07 | 10/04/07 | 0.16 |
| 4th Quarter | 12/31/07 | 01/03/08 | 0.16 |
| Total | | | $0.64 |

The declaration and payment of dividends and distributions will continue to be determined by the Board of Directors in light of conditions then existing, including the Company's earnings, financial condition, capital requirements, debt service requirements and other factors.

For federal income tax purposes, we have characterized the dividends declared in 2008 as follows: 73.3% taxable ordinary income, 22.2% capital gain and 4.5% unrecaptured section 1250 gain (unaudited). For 2007, we have characterized 97% taxable ordinary income, 2% capital gain and 1% unrecaptured section 1250 gain (unaudited).

SECURITIES AUTHORIZED FOR ISSUANCE UNDER EQUITY COMPENSATION PLANS

See Item 12 of Part III of this Report regarding information about securities authorized for issuance under our equity compensation plans.



Item 6. Selected Financial Data

The following table sets forth selected historical financial information for Mission West Properties, Inc. (see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Overview and Background" for discussion of business combinations and property dispositions that materially affect the comparability of the selected financial data).

Selected consolidated financial data is derived from the audited financial statements and notes thereto (see Item 8, "Financial Statements and Supplementary Data") and is as follows:

| | Year Ended Decemb | | |
|---|---|---|---|
| | 2008 | 2007 | 2006 |
| | (dollars in thousands, excep | | |
| OPERATING INFORMATION: (1) | | | |
| Operating revenues: | | | |
| Rental revenue from real estate | $79,075 | $80,337 | $91,457 |

| | | | |
|---|---|---|---|
| Above market lease intangible asset amortization | - | (4,091) | (1,888) |
| Tenant reimbursements | 16,406 | 13,355 | 13,061 |
| Other income, including lease terminations and settlements | 4,223 | 61,982 | 18,222 |
| Total operating revenues | 99,704 | 151,583 | 120,852 |
| Operating expenses: | | | |
| Property operating, maintenance and real estate taxes | 23,460 | 20,371 | 18,505 |
| General and administrative | 2,635 | 3,035 | 2,248 |
| Depreciation and amortization of real estate | 23,224 | 22,588 | 21,579 |
| Total operating expenses | 49,319 | 45,994 | 42,332 |
| Operating income | 50,385 | 105,589 | 78,520 |
| Other income (expenses): | | | |
| Equity in earnings of unconsolidated joint venture | 19,617 | 1,408 | 1,985 |
| Interest and dividend income | 1,735 | 3,086 | 2,344 |
| Unrealized loss from investment in marketable securities | (278) | - | - |
| Interest expense | (19,787) | (20,131) | (20,708) |
| Interest expense - related parties | (1,332) | (724) | (755) |
| Income from continuing operations before minority interests | 50,340 | 89,228 | 61,386 |
| Minority interests from continuing operations | (40,206) | (71,471) | (49,928) |
| Income from continuing operations | 10,134 | 17,757 | 11,458 |
| Discontinued operations, net of minority interests: | | | |
| Gain from disposal of discontinued operations(2) | - | 1,126 | 2,935 |
| Income attributable to discontinued operations (2) | - | 5 | 237 |
| Income from discontinued operations | - | 1,131 | 3,172 |
| Net income to common stockholders | $10,134 | $18,888 | $14,630 |
| Net income to minority interests | $40,206 | $76,960 | $66,358 |
| Basic net income per share from continuing operations | $0.51 | $0.90 | $0.60 |
| Diluted net income per share from continuing operations | $0.51 | $0.89 | $0.59 |
| Basic net income per share from discontinued operations | - | $0.06 | $0.17 |
| Diluted net income per share from discontinued operations | - | $0.06 | $0.17 |
| Basic net income per share to common stockholders | $0.51 | $0.96 | $0.77 |

| | | | |
|---|---|---|---|
| Diluted net income per share to common stockholders | $0.51 | $0.95 | $0.76 |
| PROPERTY AND OTHER INFORMATION: | | | |
| Total properties, end of period (3) | 111 | 109 | 107 |
| Total rentable square feet, end of period(000's) | 8,048 | 7,862 | 7,701 |
| Average monthly rental revenue per square foot(4) | $1.25 | $1.42 | $1.57 |
| Occupancy for leased properties, end of period | 66% | 62% | 69% |
| Dividends per share to common stockholders | $0.80 | $0.64 | $0.64 |
| Funds from operations (5) | $55,334 | $114,867 | $86,585 |
| Funds from operations per share (5)(6) | $0.52 | $1.09 | $0.83 |
| CASH FLOW INFORMATION: | | | |
| Cash flows provided by operating activities | $39,775 | $23,501 | $27,012 |
| Cash flows used in investing activities | ($29,605) | ($8,548) | ($5,369) |
| Cash flows (used in) provided by financing activities | ($33,861) | ($25,047) | ($19,299) |



| | December 31, | | |
|---|---|---|---|
| | 2008 | 2007 | 2006 |
| | | (dollars in thous | |
| BALANCE SHEET INFORMATION: | | | |
| Real estate assets, net of accumulated depr. & amort. | $943,579 | $922,117 | $898,889 |
| Total assets | $1,034,285 | $1,053,885 | $1,027,487 |
| Mortgage notes payable | $330,908 | $337,520 | $348,101 |
| Mortgage notes payable - related parties | $8,761 | $9,224 | $9,654 |
| Revolving line of credit | $13,079 | - | - |
| Line of credit - related parties | - | - | - |
| Total liabilities | $402,382 | $388,581 | $397,327 |
| Minority interests | $497,485 | $526,626 | $501,282 |
| Stockholders' equity | $134,418 | $138,678 | $128,878 |
| Common stock outstanding | 19,748,211 | 19,664,087 | 19,443,587 |
| O.P. Units issued and outstanding | 85,526,965 | 85,533,935 | 85,206,199 |

(1) Certain reclassifications have been made to prior period amounts in order to conform to current period presentation.

(2) Upon the implementation of SFAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," on January 1, 2002, the operating results of real estate held for sale and sold are reported as discontinued operations for all years presented. Additionally, all gains and losses on the sale of assets classified as held for sale subsequent to January 1, 2002 are included in discontinued operations.

(3) As of December 31, 2008, 2007, 2006, 2005 and 2004, total properties include a property at 245 Caspian in Sunnyvale with no building. In 2001, we paid the Berg Group approximately $7.5 million for their commitment to complete an approximate 75,000 to 90,000 square foot building on the

property.

(4) Average monthly rental revenue per square foot has been determined by taking the total cash base rent for the period divided by the number of months in the period, and then divided by the average occupied square feet in the period.

(5) Funds from Operations ("FFO") is a non-GAAP financial term used by REITs to measure and compare operating performance. As defined by the National Association of Real Estate Investment Trusts ("NAREIT"), FFO represents net income (loss) before minority interest of unit holders (computed in accordance with GAAP), including non-recurring events other than "extraordinary items" under GAAP and excluding gains and losses from sales of discontinued operations or depreciable operating properties, plus real estate related depreciation and amortization (excluding amortization of deferred financing costs and depreciation of non-real estate assets) and after adjustments for unconsolidated partnerships and joint ventures. FFO does include impairment losses for properties held for sale and held for use. Additionally, our 2008, 2007, 2006, 2005 and 2004 FFO calculation includes our portion of the depreciation and amortization of real estate from our unconsolidated joint venture, but excludes the above-market lease intangible asset, which was recorded as a reduction of revenues. Management considers FFO to be an appropriate supplemental measure of our operating and financial performance because when compared year over year, it reflects the impact to operations from trends in occupancy rates, rental rates, operating costs, general and administrative expenses and interest costs, providing a perspective not immediately apparent from net income. In addition, management believes that FFO provides useful information about our financial performance when compared to other REITs because FFO is generally recognized as the industry standard for reporting the operations of REITs. FFO should neither be considered as an alternative for neither net income as a measure of profitability nor is it comparable to cash flows provided by operating activities determined in accordance with GAAP. FFO is not comparable to similarly entitled items reported by other REITs that do not define them exactly as we define FFO.

(6) Considering the potential effect of all O.P. Units being exchanged for shares of the Company's common stock.

Our definition of FFO also assumes conversion at the beginning of the period of all convertible securities, including O.P. Units represented by O.P. Units that may be exchanged for shares of common stock. Our FFO does not represent the amount available for management's discretionary use; as such funds may be needed for capital replacement or expansion, debt service obligations or other commitments and uncertainties. Furthermore, FFO is not comparable to similarly entitled items reported by other REITs that do not define FFO exactly as we do.

A reconciliation of net income to common stockholders to FFO for the years ended December 31, 2008, 2007, 2006, 2005 and 2004 follows:

| | Year Ended Decemb | | |
|---|---|---|---|
| | 2008 | 2007 | 2006 |
| | | (dollars in thousands, exce | |
| Net income to common stockholders | $10,134 | $18,888 | $14,630 |
| Add: | | | |
| Minority interests (1) | 39,838 | 76,458 | 65,859 |
| Depreciation and amortization of real estate (2) | 25,833 | 26,050 | 24,636 |
| Less: | | | |
| Gain on sales of assets or joint venture assets | (20,471) | (6,529) | (18,540) |

| | | | |
|---|---|---|---|
| FFO | $55,334 | $114,867 | $86,585 |
| Weighted average common shares and O.P. Units-diluted | 105,524,677 | 105,016,651 | 104,809,155 |
| FFO per common share and O.P. Unit-diluted | $0.52 | $1.09 | $0.83 |

(1) Minority interests in net income is calculated by taking the net income of the operating partnerships (on a stand-alone basis) multiplied by the respective weighted average minority interests' ownership percentage. Minority interests for third parties totaling approximately $368, $502, $499, $479 and $486 in 2008, 2007, 2006, 2005 and 2004, respectively, was deducted from total minority interest in calculating FFO. (dollars in thousands)

(2) Also includes our portion of depreciation and amortization of real estate from our unconsolidated joint venture totaling approximately $900, $757, $849, $984 and $874 in 2008, 2007, 2006, 2005 and 2004, respectively, and amortization of leasing commissions totaling approximately $1,709, $2,558, $1,513, $1,703 and $1,644 in 2008, 2007, 2006, 2005 and 2004, respectively. Amortization of leasing commissions is included in the property operating, maintenance and real estate taxes line item in our consolidated statements of operations. (dollars in thousands)

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## ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

THE FOLLOWING DISCUSSION INCLUDES FORWARD-LOOKING STATEMENTS, INCLUDING, BUT NOT LIMITED TO, STATEMENTS WITH RESPECT TO THE FUTURE FINANCIAL PERFORMANCE, OPERATING RESULTS, PLANS AND OBJECTIVES OF MISSION WEST PROPERTIES, INC. ACTUAL RESULTS MAY DIFFER MATERIALLY FROM THOSE CURRENTLY ANTICIPATED DEPENDING UPON A VARIETY OF FACTORS, INCLUDING THOSE DESCRIBED IN PART I - ITEM 1A, RISK FACTORS.

### OVERVIEW AND BACKGROUND

Our original predecessor was formed in 1969 as Palomar Mortgage Investors, a California business trust, which operated as a mortgage REIT until 1979 when, under the name of Mission Investment Trust, it terminated its status as a REIT and began to develop and market its own properties. In 1982, Mission West Properties was incorporated as a successor to Mission Investment Trust. In 1997, our predecessor, Mission West Properties, sold all of its real estate assets and paid a special dividend of $9.00 per share to stockholders, after which it retained only nominal assets. Subsequently, the Berg Group acquired control of the corporation as a vehicle to acquire R&D properties, or interests in entities owning such properties, in a transaction completed on September 2, 1997. At that time the Berg Group and other investors acquired an aggregate 79.6% controlling ownership position. In May 1998, we, the Berg Group members, an independent limited partner, and certain other persons entered into an acquisition agreement providing, among other things, for our acquisition of interests as the sole general partner in the operating partnerships. At the time, the operating partnerships held approximately 4.34 million rentable square feet of R&D property located in Silicon Valley. The agreement also provided for the parties to enter into the Pending Projects Acquisition Agreement, the Berg Land Holdings Option Agreement and the Exchange Rights Agreement, following stockholder approval. Effective July 1, 1998, we consummated our acquisition of the general partner interests in the operating partnerships through the purchase of the general partner interests, and all limited partnership interests in the operating partnerships were converted into 59,479,633 O.P. Units, which

represented ownership of approximately 87.89% of the operating partnerships. Our general partner interests represented the balance of the ownership of the operating partnerships. At December 31, 2008, we owned an 18.73% general partner interest in the operating partnerships, taken as a whole, on a weighted average basis.

Since the beginning of calendar year 1999, we have been taxed as a qualified REIT.

Our reincorporation under the laws of the State of Maryland through the merger of Mission West Properties into Mission West Properties, Inc. occurred on December 30, 1998, at which time all outstanding shares issued by our predecessor California corporation were converted into shares of our common stock on a one-for-one basis.

In July 1999, we completed a public offering of 8,680,000 shares of our common stock at $8.25 per share. The net proceeds of approximately $66.9 million, after deducting underwriting discounts and other offering costs, were used primarily to repay indebtedness.

We have grown through property acquisitions. Since September 1998, we have acquired a total of approximately 7.14 million rentable square feet of R&D buildings and vacant land under the Pending Project Acquisition Agreement, the Berg Land Holdings Option Agreement, and from unrelated third parties. The total cost of these properties was approximately $739.3 million. To acquire these properties, we paid cash or exchanged existing properties, issued a total of 28,510,261 O.P. Units and assumed debt totaling approximately $331.3 million.

Since 1998, we have sold a total of approximately 1.0 million rentable square feet of R&D buildings. The total sales price of these properties was approximately $144.2 million.

Almost all of our earnings and cash flow is derived from rental revenue received pursuant to leased R&D space at our properties. Key factors that affect our business and financial results include the following:

- the current turmoil in the credit markets;
- economic conditions generally and the real estate market specifically;
- the occupancy rates of the properties;
- rental rates on new and renewed leases;
- tenant improvement and leasing costs incurred to obtain and retain tenants;
- operating expenses;
- cost and availability of capital;
- interest rates;
- the extent of acquisitions and sales of real estate;
- legislative or regulatory provisions (including changes to laws governing the taxation of REITs);
- competition;



- supply of and demand for R&D, office and industrial properties in our current and proposed market areas;
- tenant defaults and bankruptcies;
- lease term expirations and renewals;
- changes in general accounting principles, policies and guidelines applicable to REITs; and
- ability to timely refinance maturing debt obligations and the terms of any such refinancing.

Negative effects from any of these factors could cause a deterioration in our operating results, cash flows and financial condition.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

We prepare our consolidated financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP"), which requires us to make certain estimates, judgments and assumptions that affect the reported amounts in the accompanying consolidated financial statements, disclosure of contingent assets and liabilities and related footnotes. Accounting and disclosure decisions with respect to material transactions that are subject to significant management judgments or estimates include impairment of long lived assets, deferred rent receivables, and allocation of purchase price relating to property acquisitions and the related depreciable lives assigned. Actual results may differ from these estimates under different assumptions or conditions.

Critical accounting policies are defined as those that require management to make estimates, judgments and assumptions, giving due consideration to materiality, in certain circumstances that affect amounts reported in the consolidated financial statements, and potentially result in materially different results under different conditions and assumptions. We believe that the following best describe our critical accounting policies:

REAL ESTATE ASSETS
Real estate assets are stated at cost. Cost includes expenditures for improvements or replacements. Maintenance and repairs are charged to expense as incurred. Gains and losses from sales are included in income in accordance with Statement of Financial Accounting Standard ("SFAS") 66, "Accounting for Sales of Real Estate." The gain on the sale is only recognized proportionately as the seller receives payments from the purchaser. Interest income is recognized on an accrual basis, when appropriate.

BUSINESS COMBINATIONS
Statement of Financial Accounting Standards 141, "Business Combinations" ("SFAS 141"), was effective July 1, 2001. The acquisition costs of each property acquired prior to July 1, 2001 were allocated only to building, land and leasing commission with building depreciation being computed based on an estimated weighted average composite useful life of 40 years and leasing commission amortization being computed over the term of the lease. Acquisitions of properties made subsequent to the effective date of SFAS 141 are based on an allocation of the acquisition cost to land, building, tenant improvements, and intangibles for at market and above market in place leases, and the determination of their useful lives are guided by a combination SFAS 141 and management's estimates. Amortization expense of above and below market lease intangible asset is offset against rental revenue in the revenue section while amortization of in-place lease value intangible asset is included in depreciation and amortization of real estate in the expense section of our consolidated statements of operations. If we do not appropriately allocate these components or we incorrectly estimate the useful lives of these components, our computation of depreciation and amortization expense may not appropriately reflect the actual impact of these costs over future periods, which will affect net income.

IMPAIRMENT OF LONG-LIVED ASSETS
We review real estate assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable in accordance with Statement of Financial Accounting Standards 144, "Accounting for the Impairment and Disposal of Long-Lived Assets" ("SFAS 144"). If the carrying amount of the asset exceeds its estimated undiscounted net cash flow, before interest, we will recognize an impairment loss equal to the difference between its carrying amount and its estimated fair value. If

impairment is recognized, the reduced carrying amount of the asset will be accounted for as its new cost. For a depreciable asset, the new cost will be depreciated over the asset's remaining useful life. Generally, fair values are estimated using discounted cash flow, replacement cost or market comparison analyses. The process of evaluating for impairment requires estimates as to future events and conditions, which are subject to varying market factors, such as the vacancy rates, future rental rates and operating costs for R&D facilities in the Silicon Valley area and related submarkets. The analysis that we prepare in connection with determining if there may be any asset impairment loss under SFAS 144 considers several assumptions: holding period of ten years, 36 months lease up period and cap rate ranging from 8% to 9%. Therefore, it is reasonably possible that a change in estimate resulting from judgments as to future events could occur which would affect the recorded amounts of the property.

ALLOWANCE FOR DEFERRED RENT AND DOUBTFUL ACCOUNTS

The preparation of the consolidated financial statements requires us to make estimates and assumptions. As such, we must make estimates of the uncollectability of our accounts receivable based on the evaluation of our tenants' financial position, analyses of accounts receivable and current economic trends. We also make estimates for a straight-line adjustment reserve for existing tenants with the potential of early termination, bankruptcy or ceasing operations. Our estimates are based on our review of tenants' payment



histories, the remaining lease term, whether or not the tenant is currently occupying our building, publicly available financial information and such additional information about their financial condition as tenants provide to us. The information available to us might lead us to overstate or understate these reserve amounts. The use of different estimates or assumptions could produce different results. Moreover, actual future collections of accounts receivable or reductions in future reported rental income due to tenant bankruptcies or other business failures could differ materially from our estimates.

CONSOLIDATION OF JOINT VENTURES

We, through an operating partnership, own three properties that are in joint ventures of which we have controlling interests. We manage and operate all three properties. The recognition of these properties and their operating results are 100% reflected on our consolidated financial statements, with appropriate allocation to minority interest, because we have operational and financial control of the investments. We make judgments and assumptions about the estimated monthly payments made to our minority interest joint venture partners, which are reported with our periodic results of operations. Actual results may differ from these estimates under different assumptions or conditions.

INVESTMENT IN UNCONSOLIDATED JOINT VENTURE

We, through an operating partnership, have a 50% non-controlling limited partnership interest in one unconsolidated joint venture. This investment is not consolidated because we do not exercise significant control over major operating and financial decisions. We account for the joint venture using the equity method of accounting.

CONSOLIDATION OF VARIABLE INTEREST ENTITIES

We consolidate all variable interest entities ("VIE") in which we are deemed to be the primary beneficiary in accordance with FASB Interpretation No. 46 (Revised December 2003), "Consolidation of Variable Interest Entities" ("FIN 46R"). As of December 31, 2008, we consolidated one VIE in the accompanying consolidated financial statements in connection with an assignment of a lease agreement with an unrelated party, M&M Real Estate Control & Restructuring, LLC (see Item 8, "Financial Statements and Supplementary Data - Note 7" for further

discussion of this transaction).

REVENUE RECOGNITION

Rental revenue is recognized on the straight-line method of accounting required by GAAP under which contractual rent payment increases are recognized evenly over the lease term, regardless of when the rent payments are received by us. The difference between recognized rental income and rental cash receipts is recorded as "Deferred rent receivable" on the consolidated balance sheets.

Rental revenue is affected if existing tenants terminate or amend their leases. We try to identify tenants who may be likely to declare bankruptcy, cease operations or are likely to seek a negotiated settlement of their obligation. By anticipating these events in advance, we expect to take steps to minimize their impact on our reported results of operations through lease renegotiations, reserves against deferred rent receivable, and other appropriate measures. Our judgments and estimations about tenants' capacity to continue to meet their lease obligations will affect the rental revenue recognized. Material differences may result in the amount and timing of our rental revenue for any period if we made different judgments or estimations.

Lease termination fees are recognized as other income when there is a signed termination letter agreement, all of the conditions of the agreement have been met, and when the tenant no longer has the right to occupy the property. These fees are paid by tenants who want to terminate their lease obligations before the end of the contractual term of the lease by agreement with us. We cannot predict or forecast the timing or amounts of future lease termination fees.

We recognize income from rent, tenant reimbursements and lease termination fees and other income once all of the following criteria are met in accordance with SEC Staff Accounting Bulletin 104:

- the agreement has been fully executed and delivered;
- services have been rendered;
- the amount is fixed and determinable; and
- collectability is reasonably assured.

With regard to critical accounting policies, where applicable, we have explained and discussed the criteria for identification and selection, methodology in application and impact on the financial statements with the Audit Committee of our Board of Directors, which has reviewed these policies.

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RESULTS OF OPERATIONS

COMPARISON OF THE YEAR ENDED DECEMBER 31, 2008 TO THE YEAR ENDED DECEMBER 31, 2007

RENTAL REVENUE FROM CONTINUING PROPERTY OPERATIONS

As of December 31, 2008 and 2007, through our controlling interests in the operating partnerships, we owned 111 and 109 R&D properties totaling approximately 8.0 and 7.9 million rentable square feet, respectively. We acquired two R&D properties during 2008.

The following table depicts the amounts of rental revenue from continuing operations for the years ended December 31, 2008 and 2007 represented by our historical properties and the percentage of the total decrease in rental revenue over the period that is represented by each group of properties.

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2008 | 2007 | $ Change |
| | (dollars in thousands) | | |
| Same Property (1) | $76,375 | $80,282 | ($3,907) |
| 2007 Acquisitions (2) | 33 | 55 | (22) |
| 2008 Acquisitions (3) | 3,389 | - | 3,389 |
| Total | $79,797 | $80,337 | ($540) |

(1) "Same Property" is defined as properties owned by us prior to 2007 that we still owned as of December 31, 2008.
(2) Operating rental revenue for 2007 Acquisitions do not reflect a full 12 months of operations in 2007 because these properties were acquired at various times during the year.
(3) Operating rental revenue for 2008 Acquisitions do not reflect a full 12 months of operations in 2008 because these properties were acquired at various times during the year.

For the year ended December 31, 2008, our rental revenue from real estate decreased by approximately ($0.5) million, or (0.7%). Pursuant to SFAS 141, approximately $4.1 million of amortization expense with respect to above-market leases that we obtained through property acquisitions was offset against revenue for the year ended December 31, 2007. The ($0.5) million decrease in rental revenue resulted from current adverse market conditions as "Same Property" rents decreased due to lease terminations, cessation of tenant operations and tenant relocations since December 31, 2007.

Our overall occupancy rate for leased properties at December 31, 2008 and 2007 was approximately 66.4% and 61.7%, respectively. According to the BT Report, the leased occupancy rate for R&D property in the Silicon Valley at December 31, 2008 was approximately 83.7%. Due to an over supply of R&D properties and competitive bidding for tenants by other landlords in the Silicon Valley bidding for tenants, our occupancy rate may drop further in 2009 if the approximately 370,000 rentable square feet scheduled to expire is not renewed or re-leased. Factors that contributed to our low occupancy rate were primarily the general downturn in the Silicon Valley's economy in recent years, the softening of the R&D property market specifically, as well as the weaker relative performance of certain properties due to their location and the weak demand in those submarkets.

OTHER INCOME FROM CONTINUING PROPERTY OPERATIONS

The following table depicts the amounts of other income, including lease terminations and settlements, from continuing operations for the years ended December 31, 2008 and 2007.

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2008 | 2007 | $ Change |
| | (dollars in thousands) | | |
| Other income | $4,223 | $61,982 | ($57,759) |

Other income, including lease terminations and settlements, of approximately $4.2 million for the year ended December 31, 2008 included approximately $3.0 million from lease termination fees, $1.0 million from management fees, and $0.2 million from miscellaneous income. Other income, including lease terminations and settlements, of approximately $62.0 million for the year ended December 31, 2007 included approximately $57.5 million from lease termination fees, $1.8 million from security deposit forfeitures, $1.0 million from management fees, $0.3 million from tenant bankruptcy settlements and $1.4 million from miscellaneous income. In 2007, of the $57.5 million in lease termination fees, approximately $46 million was from the Ciena Corporation lease termination. Management fees are paid by the tenants to the landlord for the administration and supervision of the property. We do not consider termination fees and tenant bankruptcy settlements to be recurring items.

EXPENSES FROM CONTINUING PROPERTY OPERATIONS

The following table reflects the amounts of property operating and maintenance expenses and real estate taxes ("operating expenses") from continuing operations for the years ended December 31, 2008 and 2007 and the percentage of total increase in expenses over the period that is represented by each group of properties.



| | Year Ended December 31, | | |
|---|---|---|---|
| | 2008 | 2007 | $ Change |
| | (dollars in thousands) | | |
| Same Property (1) | $22,657 | $20,107 | $2,550 |
| 2007 Acquisitions (2) | 403 | 264 | 139 |
| 2008 Acquisitions (3) | 400 | - | 400 |
| Total | $23,460 | $20,371 | $3,089 |

(1) "Same Property" is defined as properties owned by us prior to 2007 that we still owned as of December 31, 2008.

(2) Operating expenses for 2007 Acquisitions do not reflect a full 12 months of operations in 2007 because these properties were acquired at various times during the year.

(3) Operating expenses for 2008 Acquisitions do not reflect a full 12 months of operations in 2008 because these properties were acquired at various times during the year.

Operating expenses from continuing operations increased by approximately $3.1 million, or 15.2%, from $20.4 million for the year ended December 31, 2007 to $23.5 million for the year ended December 31, 2008 primarily due to higher real estate taxes, maintenance and repair costs and utility rates. Tenant reimbursements from continuing operations increased by approximately $3.0 million, or 22.8%, from $13.4 million for the year ended December 31, 2007 to $16.4 million for the year ended December 31, 2008. The increase in tenant reimbursements resulted primarily from the increase in operating expenses. Total operating expenses exceeded tenant reimbursements because of vacancies which reached approximately 2.7 million rentable square feet by year-end 2008. Certain

operating expenses such as property insurance, real estate taxes, and other fixed expenses are not recoverable from vacant properties. At December 31, 2008 our vacancy rate was approximately 34%.

The following table depicts the amounts of general and administrative expenses from operations for the years ended December 31, 2008 and 2007.

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2008 | 2007 | $ Change |
| | | (dollars in thousands) | |
| General and administrative | $2,635 | $3,035 | $400 |

General and administrative expenses decreased by approximately ($0.4) million, or (13.2%), from $3.0 million for the year ended December 31, 2007 to $2.6 million for the year ended December 31, 2008. The decrease in general and administrative expenses was primarily a result of higher legal fees associated with a potential acquisition of the Company in 2007 that did not recur in 2008.

The following table depicts the amounts of depreciation and amortization expense of real estate from continuing operations for the years ended December 31, 2008 and 2007.

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2008 | 2007 | $ Change |
| | | (dollars in thousands) | |
| Depreciation and amortization | $23,224 | $22,588 | $636 |

Depreciation and amortization expense of real estate from continuing operations increased by approximately $0.6 million, or 2.8%, primarily due to two property acquisitions, new construction of tenant improvements and the write-off of tenant improvements in connection with a lease termination.

EQUITY IN EARNINGS FROM UNCONSOLIDATED JOINT VENTURE

The following table depicts the amounts of equity in earnings of unconsolidated joint venture from operations for the years ended December 31, 2008 and 2007.

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2008 | 2007 | $ Change |
| | | (dollars in thousands) | |
| Equity in earnings of unconsolidated joint venture | $19,617 | $1,408 | $18,209 |

As of December 31, 2008, we had investments in one R&D building, totaling approximately 155,500 rentable square feet in Morgan Hill, California, through an unconsolidated joint venture with TBI, in which we acquired a 50% interest from the Berg Group in January 2003. We have a non-controlling limited partnership interest in this joint venture, which we account for using the equity method of accounting. For the years ended December 31, 2008 and 2007, equity in earnings from the unconsolidated joint venture was approximately $19.6 million and $1.4 million, respectively. Our equity in earnings from this unconsolidated joint venture increased primarily due to a gain on sale of two R&D properties in 2008. The occupancy rate for the properties owned by this joint venture at December 31, 2008 and 2007 was 100%.

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The following table depicts the amounts of interest and dividend income from operations for the years ended December 31, 2008 and 2007.

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2008 | 2007 | $ Change |
| | (dollars in thousands) | | |
| Interest and dividend income | $1,735 | $3,086 | ($1,351) |

Interest and dividend income decreased by approximately ($1.4) million, or (43.8%), from $3.1 million for the year ended December 31, 2007 to $1.7 million for the year ended December 31, 2008. The decrease in interest and dividend income was primarily a result of lower cash balance and interest rates. For the year ended December 31, 2008, interest and dividend income totaled approximately $1.1 million and $0.6 million, respectively. For the year ended December 31, 2007, interest income totaled approximately $3.1 million.

In 2008, we recorded an unrealized loss from investment in marketable securities of approximately ($0.3) million. As of December 31, 2008, the fair value of the investment totaled approximately $3.3 million and the cost thereof was approximately $3.6 million.

The following table depicts the amounts of interest expense from operations for the years ended December 31, 2008 and 2007.

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2008 | 2007 | $ Change |
| | (dollars in thousands) | | |
| Interest | $19,787 | $20,131 | ($344) |
| Interest (related parties) | 1,332 | 724 | 608 |
| Total | $21,119 | $20,855 | $264 |

Interest expense decreased by approximately ($0.3) million, or (1.7%). Interest

expense (related parties) increased by approximately $0.6 million, or 84.0%, due to short-term notes payable issued to the Berg Group in connection with quarterly dividend distributions. As of December 31, 2008, the short-term notes payable were paid off in full.

NET INCOME TO COMMON STOCKHOLDERS AND NET INCOME TO MINORITY INTERESTS

The following table depicts the amounts of earnings attributable to common stockholders and minority interests for the years ended December 31, 2008 and 2007.

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2008 | 2007 | $ Change |
| | (dollars in thousands) | | |
| Net income to common stockholders | $10,134 | $18,888 | ($8,754) |
| Net income to minority interests | 40,206 | 76,960 | (36,754) |
| Total | $50,340 | $95,848 | ($45,508) |

As of December 31, 2008 and 2007, we owned a controlling general partner interest of 20.02%, 21.85%, 16.31% and 12.52% and 19.94%, 21.78%, 16.26% and 12.48% in the four operating partnerships, Mission West Properties, L.P., Mission West Properties, L.P. I, Mission West Properties, L.P. II and Mission West Properties, L.P. III, respectively. We owned an 18.73% general partner interest in the operating partnerships, taken as a whole, on a consolidated weighted average basis as of December 31, 2008 and 2007. Net income to common stockholders in 2008 decreased by approximately ($8.8) million, or (46.3%), from 2007. Our net income attributable to minority interests in 2008 decreased by approximately ($36.8) million, or (47.8%), from December 31, 2007. The decrease in net income attributable to common stockholders and minority interests resulted primarily due to lower lease termination income and higher operating expenses described above.

Minority interests represent the limited partners' ownership interest of 81.27% in the operating partnerships, on a weighted average basis, as of December 31, 2008 and 2007.

INCOME FROM DISCONTINUED OPERATIONS

The following table depicts the amounts of income from discontinued operations for the years ended December 31, 2008 and 2007.

| | Year Ended D |
|---|---|
| | 2008 |
| | (dollars in |
| Income attributable to discontinued operations | - |
| Minority interests in earnings attributable to discontinued operations | - |
| Income from discontinued operations | - |

In 2007, we sold two R&D properties and in accordance with our adoption of SFAS 144, classified the net gains on sale and operating results of the disposed properties as discontinued operations. SFAS 144 requires prior period results of operations for these properties to be retrospectively adjusted and presented in discontinued operations in prior consolidated statements of operations.

We recognized total income of approximately $6.6 million from discontinued operations, of which $1.1 million and $5.5 million were attributable to common stockholders and minority interests, respectively, for the year ended December 31, 2007.

COMPARISON OF THE YEAR ENDED DECEMBER 31, 2007 TO THE YEAR ENDED DECEMBER 31, 2006

RENTAL REVENUE FROM CONTINUING PROPERTY OPERATIONS

As of December 31, 2007 and 2006, through our controlling interests in the operating partnerships, we owned 109 and 107 R&D properties totaling approximately 7.9 and 7.7 million rentable square feet, respectively. We sold two R&D properties and acquired four R&D properties and 55 acres of vacant land during 2007.

The following table depicts the amounts of rental revenue from continuing operations for the years ended December 31, 2007 and 2006 represented by our historical properties and the percentage of the total decrease in rental revenue over the period that is represented by each group of properties.

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | $ Change |
| | (dollars in thousands) | | |
| Same Property (1) | $78,067 | $89,685 | ($11,618) |
| 2006 Acquisitions (2) | 2,215 | 1,772 | 443 |
| 2007 Acquisitions (3) | 55 | - | 55 |
| Total | $80,337 | $91,457 | ($11,120) |

(1) "Same Property" is defined as properties owned by us prior to 2006 that we still owned as of December 31, 2007. (
2) Operating rental revenue for 2006 Acquisitions do not reflect a full 12 months of operations in 2006 because these properties were acquired at various times during the year.
(3) Operating rental revenue for 2007 Acquisitions do not reflect a full 12 months of operations in 2007 because these properties were acquired at various times during the year.

For the year ended December 31, 2007, our rental revenue from real estate decreased by approximately ($11.1) million, or (12.2%). Pursuant to SFAS 141, approximately $4.1 million and $1.9 million of amortization expense with respect to above-market leases that we obtained through property acquisitions was offset against revenue for the years ended December 31, 2007 and 2006, respectively. The ($11.1) million decrease in rental revenue resulted from current adverse market conditions as "Same Property" rents decreased due to lease terminations, cessation of tenant operations and tenant relocations since December 31, 2006.

Our overall occupancy rate for leased properties at December 31, 2007 and 2006 was approximately 61.7% and 69.5%, respectively. According to the BT Report, the leased occupancy rate for R&D property in the Silicon Valley at December 31, 2007 was approximately 83.4%. Factors that contributed to our low occupancy rate were primarily the general downturn in the Silicon Valley's economy in recent years, the softening of the R&D property market specifically, as well as the weaker relative performance of certain properties due to their location and the weak demand in those submarkets.

OTHER INCOME FROM CONTINUING PROPERTY OPERATIONS

The following table depicts the amounts of other income, including lease terminations and settlements, from continuing operations for the years ended December 31, 2007 and 2006.

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | $ Change |
| | (dollars in thousands) | | |
| Other income | $61,982 | $18,222 | $43,760 |

Other income, including lease terminations and settlements, of approximately $62.0 million for the year ended December 31, 2007 included approximately $57.5 million from lease termination fees, $1.8 million from security deposit forfeitures, $1.0 million from management fees, $0.3 million from tenant bankruptcy settlements and $1.4 million from miscellaneous income. In 2007, of the $57.5 million in lease termination fees, approximately $46 million was from the Ciena Corporation lease termination. Other income, including lease terminations and settlements, of approximately $18.2 million for the year ended December 31, 2006 included approximately $16.0 million from lease termination fees, $1.1 million from management fees, $0.5 million from a property tax accrual, $0.2 million from tenant bankruptcy settlements, $0.1 million from security deposit forfeitures and $0.3 million from miscellaneous income. In 2006, of the $16.0 million in lease termination fees, approximately $11.1 million was from the JDS Uniphase lease termination. Management fees are paid by the tenants to the landlord for the administration and supervision of the property. We do not consider termination fees and tenant bankruptcy settlements to be recurring items.

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EXPENSES FROM CONTINUING PROPERTY OPERATIONS

The following table reflects the amounts of property operating and maintenance expenses and real estate taxes ("operating expenses") from continuing operations for the years ended December 31, 2007 and 2006 and the percentage of total increase in expenses over the period that is represented by each group of properties.

| Year Ended December 31, | | |
|---|---|---|
| 2007 | 2006 | $ Change |
| (dollars in thousands) | | |

| | | | |
|---|---|---|---|
| Same Property (1) | $19,393 | $18,001 | $1,392 |
| 2006 Acquisitions (2) | 714 | 504 | 210 |
| 2007 Acquisitions (3) | 264 | - | 264 |
| Total | $20,371 | $18,505 | $1,866 |

(1) "Same Property" is defined as properties owned by us prior to 2006 that we still owned as of December 31, 2007.
(2) Operating expenses for 2006 Acquisitions do not reflect a full 12 months of operations in 2006 because these properties were acquired at various times during the year.
(3) Operating expenses for 2007 Acquisitions do not reflect a full 12 months of operations in 2007 because these properties were acquired at various times during the year.

Operating expenses from continuing operations increased by approximately $1.9 million, or 10.1%, from $18.5 million for the year ended December 31, 2006 to $20.4 million for the year ended December 31, 2007 primarily due to increase in real estate taxes, higher maintenance and repair costs and lease commission write-offs associated with lease terminations. Tenant reimbursements from continuing operations increased by approximately $0.3 million, or 2.3%, from $13.1 million for the year ended December 31, 2006 to $13.4 million for the year ended December 31, 2007. The increase in tenant reimbursements resulted primarily from the increase in operating expenses. Total operating expenses exceeded tenant reimbursements because of vacancies, which reached approximately 3.0 million rentable square feet by year-end 2007. Certain operating expenses such as property insurance, real estate taxes, and other fixed expenses are not recoverable from vacant properties. At December 31, 2007 our vacancy rate was approximately 38%.

The following table depicts the amounts of general and administrative expenses from operations for the years ended December 31, 2007 and 2006.

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | $ Change |
| | (dollars in thousands) | | |
| General and administrative | $3,035 | $2,248 | $787 |

General and administrative expenses increased by approximately $0.8 million, or 35.0%, from $2.2 million for the year ended December 31, 2006 to $3.0 million for the year ended December 31, 2007. The increase in general and administrative expenses was primarily a result of higher legal fees associated with a potential acquisition of the Company, salaries and wages and share-based compensation expense.

The following table depicts the amounts of depreciation and amortization expense of real estate from continuing operations for the years ended December 31, 2007 and 2006.

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | $ Change |

| | | | |
|---|---|---|---|
| | (dollars in thousands) | | |
| Depreciation and amortization | $22,588 | $21,579 | $1,009 |

Depreciation and amortization expense of real estate from continuing operations increased by approximately $1.0 million, or 4.7%, primarily due to new construction of tenant improvements and the write-offs of additional amortization expense relating to in-place lease value intangible assets pursuant to SFAS 141 in connection with two lease terminations.

EQUITY IN EARNINGS FROM UNCONSOLIDATED JOINT VENTURE
The following table depicts the amounts of equity in earnings of unconsolidated joint venture from operations for the years ended December 31, 2007 and 2006.

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | $ Change |
| | (dollars in thousands) | | |
| Equity in earnings of unconsolidated joint venture | $1,408 | $1,985 | ($577) |

As of December 31, 2007, we had investments in three R&D buildings, totaling approximately 466,600 rentable square feet in Morgan Hill, California, through an unconsolidated joint venture with TBI, in which we acquired a 50% interest from the Berg Group in



January 2003. We have a non-controlling limited partnership interest in this joint venture, which we account for using the equity method of accounting. For the years ended December 31, 2007 and 2006, equity in earnings from the unconsolidated joint venture was approximately $1.4 million and $2.0 million, respectively. Our equity in earnings from this unconsolidated joint venture decreased primarily due to a gain on sale of one R&D property in 2006 that did not recur in 2007. The occupancy rate for the properties owned by this joint venture at December 31, 2007 and 2006 was 100%.

The following table depicts the amounts of interest and dividend income from operations for the years ended December 31, 2007 and 2006.

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | $ Change |
| | (dollars in thousands) | | |
| Interest and dividend income | $3,086 | $2,344 | $742 |

Interest and dividend income increased by approximately $0.7 million, or 31.7%, from $2.3 million for the year ended December 31, 2006 to $3.0 million for the year ended December 31, 2007. The increase in interest and dividend income was primarily a result of higher interest rates. For the year ended December 31, 2007, interest income totaled approximately $3.0 million. For the year ended December 31, 2006, interest income totaled approximately $2.3 million.

The following table depicts the amounts of interest expense from operations for the years ended December 31, 2007 and 2006.

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | $ Change |
| | (dollars in thousands) | | |
| Interest | $20,131 | $20,708 | ($577) |
| Interest (related parties) | 724 | 755 | (31) |
| Total | $20,855 | $21,463 | ($608) |

Interest expense decreased by approximately ($0.6) million, or (2.8%). Interest expense (related parties) decreased by ($0.03) million, or (4.1%).

NET INCOME TO COMMON STOCKHOLDERS AND NET INCOME TO MINORITY INTERESTS

The following table depicts the amounts of earnings attributable to common stockholders and minority interests for the years ended December 31, 2007 and 2006.

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | $ Change |
| | (dollars in thousands) | | |
| Net income to common stockholders | $18,888 | $14,630 | $4,258 |
| Net income to minority interests | 76,960 | 66,358 | 10,602 |
| Total | $95,848 | $80,988 | $14,860 |

As of December 31, 2007 and 2006, we owned a controlling general partner interest of 19.94%, 21.78%, 16.26% and 12.48% and 19.71%, 21.78%, 16.26% and 12.48% in the four operating partnerships, Mission West Properties, L.P., Mission West Properties, L.P. I, Mission West Properties, L.P. II and Mission West Properties, L.P. III, respectively. We owned an 18.73% and 18.23% general partner interest in the operating partnerships, taken as a whole, on a consolidated weighted average basis as of December 31, 2007 and 2006, respectively. Net income to common stockholders in 2007 increased by approximately $4.3 million, or 29.1%, from December 31, 2006. Our net income attributable to minority interests in 2007 increased by approximately $10.6 million, or 16.0%, from December 31, 2006. The increase in net income attributable to common stockholders and minority interests resulted primarily due to higher lease termination fee income described above.

Minority interests represent the limited partners' ownership interest of 81.27% and 81.77% in the operating partnerships, on a weighted average basis, as of December 31, 2007 and 2006, respectively. The decrease in the minority interest ownership percentage resulted from the exchange of O.P. Units for shares of the Company's common stock.

INCOME FROM DISCONTINUED OPERATIONS

The following table depicts the amounts of income from discontinued operations for the years ended December 31, 2007 and 2006.

| | Year Ended D |
|---|---|
| | 2007 |
| | (dollars in t |
| Income attributable to discontinued operations | $6,620 |
| Minority interests in earnings attributable to discontinued operations | (5,489) |
| Income from discontinued operations | $1,131 |



In 2007, we sold two R&D properties and in accordance with our adoption of SFAS 144, classified the net gains on sale and operating results of the disposed properties as discontinued operations, and in 2006, we sold three R&D properties and classified the net gains on sale and operating results of the disposed properties as discontinued operations. SFAS 144 requires prior period results of operations for these properties to be retrospectively adjusted and presented in discontinued operations in prior consolidated statements of operations.

We recognized total income of approximately $6.6 million from discontinued operations, of which $1.1 million and $5.5 million were attributable to common stockholders and minority interests, respectively, for the year ended December 31, 2007. For the year ended December 31, 2006, we recognized total income from discontinued operations of approximately $19.6 million. The income to common stockholders and minority interests attributable to discontinued operations from these properties in 2006 was approximately $3.2 million and $16.4 million, respectively.

CHANGES IN FINANCIAL CONDITION

YEAR ENDED DECEMBER 31, 2008

The most significant changes in our financial condition in 2008 resulted from the acquisition of two R&D properties, the exercise of stock options and the exchange of O.P. Units for shares of the Company's common stock.

During 2008, we acquired two R&D properties representing approximately 186,000 rentable square feet for an aggregate gross purchase price of approximately $35.8 million. We acquired one R&D property in a tax-deferred exchange transaction plus cash and paid cash to members of the Berg Group to acquire the second R&D property.

Debt outstanding, including amounts due related parties, increased by approximately $6.0 million, or 1.7%, from $346.7 million as of December 31, 2007 to $352.7 million as of December 31, 2008. In 2008, we repaid the remaining

balance on the Prudential loan with proceeds from the $115 million Hartford loan, borrowed from our revolving line of credit and made recurring scheduled debt payments.

During the year ended December 31, 2008, stock options to purchase 70,487 shares of the Company's common stock were exercised at $10.00 per share and stock options to purchase 6,667 shares of the Company's common stock were exercised at $9.51 per share. The total proceeds to the Company of approximately $0.8 million increased additional paid-in-capital.

In 2008, three limited partners exchanged a total of 6,970 O.P. Units for 6,970 shares of the Company's common stock pursuant to the Exchange Rights Agreement resulting in a reclassification of approximately $0.07 million from minority interests to additional paid-in-capital.

The conversion of O.P. Units to shares of the Company's common stock was applied to increase our percentage interest as general partner in the operating partnerships.

YEAR ENDED DECEMBER 31, 2007

The most significant changes in our financial condition in 2007 resulted from the acquisition of four R&D properties, the acquisition of 55 acres of vacant land, the disposition of two R&D properties and the exchange of O.P. Units for shares of the Company's common stock.

During 2007, we acquired four R&D properties representing approximately 247,000 rentable square feet for an aggregate gross purchase price of approximately $26.3 million. We acquired three of the R&D properties in tax-deferred exchange transactions and paid cash and issued O.P. Units to members of the Berg Group to acquire the fourth property. We also acquired 55 acres of vacant land for approximately $27.8 million in a tax-deferred exchange transaction. In addition to those property acquisitions, we sold two R&D properties to unrelated third parties for a total gross sales price of approximately $16.0 million. Those property dispositions reduced approximately 87,000 rentable square feet. The proceeds were classified as restricted cash for use in tax-deferred property exchanges and were reflected on our consolidated balance sheet as restricted cash at December 31, 2007 (see Item 8, "Financial Statements and Supplementary Data - Note 6" for further discussion of this transaction).

Debt outstanding, including amounts due related parties, decreased by approximately ($11.1) million, or (3.1%), from $357.8 million as of December 31, 2006 to $346.7 million as of December 31, 2007 due to normal scheduled debt payments.

In 2007, two limited partners exchanged a total of 220,500 O.P. Units for 220,500 shares of common stock pursuant to the Exchange Rights Agreement resulting in a reclassification of approximately $2.9 million from minority interests to additional paid-in-capital.



The conversion of O.P. Units to shares of the Company's common stock was applied to increase our percentage interest as general partner in the operating partnerships.

LIQUIDITY AND CAPITAL RESOURCES

In 2009, we anticipate operating cash flows from our property portfolio to be lower compared to 2008. We are still experiencing weak demand for our R&D properties in certain areas of the Silicon Valley, principally the south San

Jose area. If we are unable to lease a significant portion of the approximately 370,000 rentable square feet scheduled to expire in 2009, as well as our currently available space, our operating cash flows will be affected adversely. We are also subject to risks of decreased occupancy through tenant defaults and bankruptcies, and potential reduction in rental rates upon renewal of properties, which would result in reduction in cash flows from operations beyond the level we are anticipating currently.

We expect our principal source of liquidity for distributions to stockholders and O.P. Unit holders, debt service, leasing commissions and recurring capital expenditures to come from cash provided by operations and/or future borrowings under our $17.5 million line of credit with the Heritage Bank of Commerce, which we obtained in early 2008. We expect these sources of liquidity to be adequate to meet projected distributions to stockholders and other presently anticipated liquidity requirements in 2009. We expect to meet our long-term liquidity requirements for the funding of property development, property acquisitions and other material non-recurring capital improvements through cash and investments, long-term secured and unsecured indebtedness and the issuance of additional equity securities by us. We have the ability to meet short-term obligations or other liquidity needs based on our existing cash reserves. In 2009, we will be obligated to make payments totaling approximately $25.7 million of debt principal under our existing mortgage notes and line of credit without regard to any debt refinancing or new debt obligations that we might incur, or optional payments of debt principal.

On March 4, 2008, we established a $10 million uncollateralized revolving line of credit with Heritage Bank of Commerce ("HBC"). We paid approximately $26,000 in loan and legal fees. On April 17, 2008, we entered into a "Change in Terms Agreement" with HBC that increased the facility from $10 million to $17.5 million. The line of credit bears an interest rate of LIBOR plus 1.75% and matures June 15, 2009. The HBC line of credit contains certain financial loan and reporting covenants as defined in the loan agreements. As of December 31, 2008, we were in compliance with these loan covenants. The proceeds from the HBC line of credit may be used to repay debt, complete acquisitions and finance other working capital requirements.

We expect to renew the HBC line of credit in June 2009 when it matures.

On October 1, 2008, we entered into a fixed rate term agreement and related contracts and instruments for a secured mortgage loan totaling $115 million from Hartford Life Insurance Company, Hartford Life and Accident Insurance Company and Hartford Life and Annuity Insurance Company (the "Hartford Loan"). The proceeds were used primarily to repay the remaining balance of an existing mortgage loan with Prudential Mortgage Capital Company and to provide other working capital needs. The Hartford Loan bears a fixed interest rate of 6.21%, with a 20-year amortization, and matures October 1, 2018, at which time any outstanding principal and interest will be due. Pursuant to the loan agreement, monthly principal and interest installment payments of approximately $0.84 million are due on the first day of each month. The Hartford Loan is secured by 20 properties consisting of approximately 1.6 million rentable square feet. In connection with the loan, we paid approximately $1.0 million in loan fees and financing costs, which are amortized over the ten year loan period. We have the option to prepay the Hartford Loan, subject to certain yield maintenance provisions, though generally no prepayment is permitted during the first 24 months of the loan term.

As of December 31, 2008, we were in compliance with loan covenants relating to the Allianz, Hartford, Northwestern mortgage loans and the HBC line of credit loan.

Cash and cash equivalents decreased by approximately ($23.7) million from $23.7 million as of December 31, 2007 to zero as of December 31, 2008.

Restricted cash totaled approximately $39.5 million as of December 31, 2008. The entire amount represents a balance we have consolidated due to our adoption of FIN 46R (see Item 8, "Financial Statements and Supplementary Data - Note 7" for further discussion of this transaction). We do not possess or control these funds or have any rights to receive them except as provided in the applicable agreements. Therefore, restricted cash is not available for distribution to stockholders.

Since 1999, we have elected to be taxed as a REIT under the Internal Revenue Code of 1986. We intend to continue operating as a REIT in 2009. As a REIT, we are subject to a number of organizational and operating requirements, including a requirement to distribute 90% of our taxable income to our stockholders. Also as a REIT, we generally will not be subject to federal income taxes on our taxable income.

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Generally, our objective is to meet our short-term liquidity requirement of funding the payment of our current level of quarterly common dividends to stockholders and O.P. Unit holders through our net cash flows provided by operating activities, less our recurring and nonrecurring property capital expenditures. These operating capital expenditures are the capital expenditures necessary to maintain the earnings capacity of our operating assets over time.

For 2009, we expect to maintain our quarterly dividend payment at the current rate of $0.20 per share to common stockholders and O.P. Unit holders. However, distributions are declared at the discretion of our Board of Directors and are subject to actual cash available for distribution, our financial condition, capital requirements and such other factors, as our Board of Directors deems relevant (see Item 1A, "Risk Factors - Stockholders are not assured of receiving cash distributions from us").

On January 8, 2009, we paid dividends of $0.20 per share of common stock to all common stockholders of record as of December 31, 2008. On the same date, the operating partnerships paid a distribution of $0.20 per O.P. Unit to all holders of O.P. Units, with the exception of the Berg Group. A short-term note payable, which bears interest at LIBOR plus 2%, in the amount of approximately $10.8 million was issued to the Berg Group and fully paid in February 2009. Aggregate dividends and distributions for the quarter ended December 31, 2008 amounted to approximately $21.1 million.

Funds available for distributions does not represent cash generated from operating activities and is not necessarily indicative of cash available to fund cash needs. The actual return that we will realize and the amount available for distributions to stockholders will be affected by a number of factors, including the revenues received from our properties, our operating expenses, debt service on borrowings, and planned and unanticipated capital expenditures.

We anticipate that cash available for distribution will exceed earnings and profits for federal income tax purposes, as the latter figure takes into account non-cash expenses such as depreciation and amortization that we will incur. Distributions other than capital gain distributions by us to the extent of our current and accumulated earnings and profits for federal income tax purposes most likely will be taxable to U.S. stockholders as ordinary dividend income unless a stockholder is a tax-exempt entity. Distributions in excess of earnings and profits generally will be treated as a non-taxable reduction of the U.S. stockholder's basis in the common stock to the extent of such basis, and thereafter as taxable gain. The percentage of such distributions in excess of earnings and profits, if any, may vary from period to period.

CONTRACTUAL OBLIGATIONS

The following table identifies the contractual obligations with respect to the maturities and scheduled principal repayments of our secured debt, Note, Credit Facility and scheduled interest payments of our fixed-rate and variable-rate debt at December 31, 2008 and provides information about our operating lease obligations that will impact our liquidity and cash flow in future periods.

| | 2009 | 2010 | 2011 | 2012 | |
|---|---|---|---|---|---|
| Principal payments(1) | $25,669 | $13,328 | $14,109 | $14,935 | $8 |
| Interest payments-fixed rate debt(2) | 19,170 | 18,433 | 17,651 | 16,825 | 1 |
| Interest payments-variable rate debt(3) | 166 | - | - | - | |
| Operating lease obligations(4) | 120 | 30 | - | - | |
| Total | $45,125 | $31,791 | $31,760 | $31,760 | $9 |

(1) As of December 31, 2008, 96.3% of our debt was contractually fixed and 3.7% of our debt bore interest at variable rates. Our debt obligations are set forth in detail in the table below.

(2) The information in the table above reflects our projected interest rate obligations for the fixed-rate payments based on the contractual interest rates, interest payment dates and scheduled maturity dates.

(3) The information in the table above reflects our projected interest rate obligations for the variable-rate payments based on LIBOR plus a 1.75% spread at December 31, 2008, the scheduled interest payment dates and maturity dates .

(4) Our operating lease obligations relate to a lease of our corporate office facility from a related party.

At December 31, 2008, we had total indebtedness of approximately $352.7 million. A table listing our indebtedness as of December 31, 2008 is set forth in Item 8, "Financial Statements and Supplementary Data - Note 8."

At December 31, 2008, our debt to total market capitalization ratio, which is computed as our total debt outstanding divided by the sum of total debt outstanding plus the market value of common stock (based upon the closing price of $7.65 per share on December 31, 2008) on a fully diluted basis, including the conversion of all O.P. Units into common stock, was approximately 30.4%. On December 31, 2008, the last trading day for the year, total market capitalization was approximately $1.16 billion. By comparison, on December 31, 2007 total debt as a percentage of market capitalization was 25.7% and total market capitalization was approximately $1.35 billion.



At December 31, 2008, the outstanding balance remaining under certain demand notes that we owed to the operating partnerships was approximately $2.1 million. The due date of the demand notes has been extended to September 30, 2010. The principal of the demand notes, along with the interest expense, which is interest income to the operating partnerships, is eliminated in consolidation and is not included in the corresponding line items within the consolidated financial statements. However, the interest income earned by the operating partnerships, which is interest expense to us, in connection with this debt, is

included in the calculation of minority interest as reported on the consolidated statements of operations, thereby reducing our net income by this same amount. At present, our only means for repayment of this debt is through distributions that we receive from the operating partnerships that are in excess of the amount of dividends to be paid to our stockholders or by raising additional equity capital.

HISTORICAL CASH FLOWS

The Company's cash flow activities are summarized as follows:

| | Year Ended December 31, | |
|---|---|---|
| | 2008 | 2007 |
| | (dollars in thousands) | |
| Cash flow provided by operating activities | $39,775 | $23,501 |
| Cash flow used in investing activities | ($29,605) | ($8,548) |
| Cash flow (used in) provided by financing activities | ($33,861) | ($25,047) |

COMPARISON OF THE YEAR ENDED DECEMBER 31, 2008 TO THE YEAR ENDED DECEMBER 31, 2007

Cash and cash equivalents were approximately zero at December 31, 2008 compared with $23.7 million at December 31, 2007.

Net cash provided by operating activities for the year ended December 31, 2008 was approximately $39.8 million, compared with approximately $23.5 million for the year ended December 31, 2007. The increase in cash provided by operating activities resulted primarily from a $16.9 million cash distribution received from our unconsolidated joint venture, TBI-MWP, from the sale of two R&D buildings.

Cash used in investing primarily consists of property acquisitions, improvements to our properties and investment in marketable securities. Net cash used in investing activities was approximately ($29.6) million for the year ended December 31, 2008 compared with approximately ($8.5) million for the prior year. In 2008, we acquired two properties for approximately $35.8 million, incurred capital expenditures relating to real estate improvements of approximately $6.5 million, invested approximately $3.1 million in marketable securities and transferred excess restricted cash of approximately $7.7 million to our general cash account. We used restricted cash totaling approximately $8.1 million for the acquisition of one R&D property in a tax-deferred exchange transaction involving our former R&D property at Morse Avenue in Sunnyvale, California. In 2007, we acquired six properties for approximately $47.5 million, incurred capital expenditures relating to real estate improvements of approximately $4.9 million and transferred excess restricted cash of approximately $0.6 million to our general cash account. We used restricted cash totaling approximately $43.2 million for the acquisition of three R&D properties and 55 acres of vacant land in tax-deferred exchange transactions involving our former R&D properties at Samaritan Drive in San Jose, California. We sold two R&D properties for approximately $15.4 million, net, as described above, the proceeds of which were reflected on our consolidated balance sheet as restricted cash at December 31, 2007.

Net cash used in financing activities was approximately ($33.9) million for the year ended December 31, 2008, compared with approximately ($25.0) million for the year ended December 31, 2007. During 2008, financing activities included

borrowing $115 million under a new collateralized mortgage loan, borrowing approximately $13.1 million under our line of credit, payments of approximately $122.1 million for outstanding debt, borrowing and payment of approximately $19.4 million for the purchase of an R&D building, borrowing and payment of $3 million for a short-term loan, payment of approximately $1.2 million in financing costs related to a new mortgage loan, refund of $1.5 million from a certificate of deposit related to a former loan escrow, receipt of approximately $0.8 million from stock option exercises, payments of approximately $15.0 million to common stockholders as dividends and paid approximately $25.9 million to O.P. Unit holders for distributions in excess of their share of earnings. During 2007, financing activities included payments of approximately $11.0 million for outstanding debt, payment of approximately $1.5 million for a certificate of deposit related to a current loan escrow and payments of approximately $12.5 million to common stockholders as dividends.

COMPARISON OF THE YEAR ENDED DECEMBER 31, 2007 TO THE YEAR ENDED DECEMBER 31, 2006

Cash and cash equivalents were approximately $23.7 million at December 31, 2007, a decrease of ($10.1) million from $33.8 million at December 31, 2006.

Net cash provided by operating activities for the year ended December 31, 2007 was approximately $23.5 million, compared with approximately $27.0 million for the prior year. The decrease in cash provided by operating activities resulted primarily from lower lease termination fee payment, lower deferred rental income and higher leasing commission payments (included in other assets) in 2007.



Cash used in investing primarily consists of property acquisitions, property sales and improvements to our properties. Net cash used in investing activities was approximately ($8.5) million for the year ended December 31, 2007 compared with approximately ($5.4) million for the prior year. In 2007, we acquired six properties for approximately $47.5 million, incurred capital expenditures relating to real estate improvements of approximately $4.9 million and transferred excess restricted cash of approximately $0.6 million to our general cash account. We used restricted cash totaling approximately $43.2 million for the acquisition of three R&D properties and 55 acres of vacant land in tax-deferred exchange transactions involving our former R&D properties at Samaritan Drive in San Jose, California. We sold two R&D properties for approximately $15.4 million, net, as described above, the proceeds of which are reflected on our consolidated balance sheet as restricted cash at December 31, 2007. In 2006, we sold three vacant R&D properties for approximately $42.6 million, net. We acquired three R&D properties for approximately $16.0 million, incurred capital expenditures relating to real estate improvements of approximately $4.3 million and transferred approximately $1.8 million of excess restricted cash to our general cash account. We used restricted cash totaling approximately $13.5 million to complete the acquisition of two R&D properties in a tax-deferred exchange transaction involving our former R&D property at Embedded Way in San Jose, California. Proceeds of approximately $43.0 million, which included earned interest, from the three vacant R&D property dispositions were classified as restricted cash for use in tax-deferred property exchanges and were reflected on our consolidated balance sheet as restricted cash at December 31, 2006.

Net cash used in financing activities was approximately ($25.0) million for the year ended December 31, 2007, compared with approximately ($19.3) million for the year ended December 31, 2006. During 2007, financing activities included payments of approximately $11.0 million for outstanding debt, payment of approximately $1.5 million for a certificate of deposit related to a loan escrow and payments of approximately $12.5 million to common stockholders as dividends. During 2006, financing activities included payments of approximately $9.8

million for outstanding debt, receipt of approximately $1.6 million from the refund of an appeal bond, receipt of approximately $1.0 million from stock option exercises and payments of approximately $12.1 million to common stockholders as dividends.

CAPITAL EXPENDITURES

Our properties require periodic investments of capital for tenant-related capital expenditures and for general capital improvements. For the years ended December 31, 2003 through December 31, 2007, the recurring tenant/building improvement costs and leasing commissions incurred with respect to new leases and lease renewals of the properties averaged approximately $6.2 million annually. We will have approximately 370,000 rentable square feet under expiring leases in 2009. We expect that the average annual cost of recurring tenant/building improvements and leasing commissions related to these properties will be approximately $5.0 million during 2009. We believe we will recover substantially all of these costs from the tenants under the new or renewed leases through contractual increases in rental rates. Until we actually sign the leases, however, we cannot assure you that this will occur. Capital expenditures may fluctuate in any given period subject to the nature, extent, and timing of improvements required to be made to the properties. Tenant/building improvements and leasing costs also may fluctuate in any given period year depending upon factors such as the property, the term of the lease, the type of lease and the overall market conditions. We expect to meet our long-term liquidity requirements for the funding of property acquisitions and other material non-recurring capital improvements through our currently available sources of capital, including operating cash flows, cash on hand, and our credit facility(see "Policies with Respect to Certain Activities - Financing Policies" below).

DISTRIBUTION POLICY

Distributions are determined by our Board of Directors and depend on actual cash available for distributions, our financial condition, capital requirements, the annual distribution requirements under the REIT provisions of the Code and such other factors as the Board of Directors deems relevant. For a discussion of the risk that we will not meet our distribution objectives, see Item 1A, "Risk Factors - Stockholders are not assured of receiving cash distributions from us."

POLICIES WITH RESPECT TO CERTAIN ACTIVITIES

We have adopted policies with respect to investment, financing, conflicts of interest and other activities. These policies have been formulated by our Board of Directors, are set forth in our charter, bylaws, operating partnership agreements or agreements with the Berg Group, and generally may be amended or revised from time to time, subject to applicable agreement terms, at the discretion of the Board of Directors without a vote of the stockholders. Among other things, these policies provide that:

- so long as the Berg Group members and their affiliates, other than us and the operating partnerships, beneficially own, in the aggregate, at least 15% of the outstanding shares of common stock on a Fully Diluted basis, the approval of a majority of our directors, including Carl E. Berg or his designee as a director, and of the holders of a majority of the O.P. Units is required for us to take title to assets, other than temporarily in connection with an acquisition prior to contributing such assets to the operating partnerships, or to conduct business other than through the operating partnerships, or for us or the operating partnerships to engage in any business other than the ownership, construction, development and operation of real estate properties, or for certain fundamental corporate actions, including amendments to our charter, bylaws or any operating

partnership agreement and any merger, consolidation or sale of all or substantially all of our assets or the assets of the operating partnerships;

- changes in certain policies with respect to conflicts of interest must be consistent with legal requirements;
- certain policies with respect to competition by and acquisitions from the Berg Group are imposed pursuant to provisions of the acquisition agreement that cannot be amended or waived without the approval of the Independent Directors Committee of our Board of Directors;
- we cannot take any action intended to terminate our qualification as a REIT without the approval of more than 75% of the entire Board of Directors; and
- we cannot undertake certain other specified transactions, including the issuance of debt securities, and borrowings in excess of specified limits, or the amendment of our charter and bylaws, without the approval of more than 75% of the entire Board of Directors.

INVESTMENT POLICIES

We expect to pursue our business and investment objectives principally through the direct ownership by the operating partnerships of our properties and future acquired properties. Development or investment activities are not limited to any specified percentage of our assets. We may also participate with other entities in property ownership, through joint ventures or other types of co-ownership. Equity investments may be subject to existing mortgage financing and other indebtedness that have priority over our equity interests.

While we will emphasize equity real estate investments, we may, in our discretion and subject to the percentage ownership limitations and gross income tests necessary for REIT qualification, invest in mortgage and other real estate interests, including securities of other real estate investment trusts. We have not previously invested in mortgages of other real estate investment trusts. In the fourth quarter of 2008, we invested approximately $3.6 million in securities of another real estate investment trust.

FINANCING POLICIES

To the extent that our Board of Directors determines to seek additional capital, we may raise such capital through additional equity offerings, debt financing or retention of cash flow, or through a combination of these sources, after consideration of provisions of the Code requiring the distribution by a REIT of a certain percentage of its taxable income and taking into account taxes that would be imposed on undistributed taxable income. It is our present intention that any additional borrowings will be made through the operating partnerships, although we may incur borrowings that would be re-loaned to the operating partnerships. Borrowings may be unsecured or may be secured by any or all of our assets, the operating partnerships or any existing or new property, and may have full or limited recourse to all or any portion of our assets, the operating partnerships or any existing or new property.

We have adopted a policy of maintaining a consolidated ratio of debt to total market capitalization, which includes for this purpose the market value of all shares of common stock for which outstanding O.P. Units are exchangeable, of less than 50%. This ratio may not be exceeded without the approval of more than 75% of our entire Board of Directors. We also may determine to finance acquisitions through the exchange of properties or the issuance of additional O.P. Units in the operating partnerships, shares of common stock or other securities.

In the event that the Board of Directors determines to raise additional equity capital, it has the authority, without stockholder approval, to issue additional shares of common stock, preferred stock or other capital stock, including securities senior to the common stock, in any manner and on such terms and for such consideration it deems appropriate, including in exchange for property. In the event that we issue any shares of common stock or securities convertible into or exchangeable or exercisable for, shares of common stock, subject to limited exceptions, such as the issuance of common stock pursuant to any stock incentive plan adopted by us or pursuant to limited partners' exercise of the exchange rights or the put rights, the limited partners will have the right to purchase common stock or such securities in order to maintain their respective percentage interests in us on a Fully Diluted basis. If the Board of Directors determines that we will raise additional equity capital to fund investments by the operating partnerships, we will contribute such funds to the operating partnerships as a contribution to capital and purchase of additional units of general partner interest; however, holders of O.P. Units will have the right to participate in such funding on a pro rata basis. In the event that holders of O.P. Units sell their O.P. Units to us upon exercise of their put rights, we are authorized to raise the funds for such purchase by issuing additional shares of common stock. Alternatively, we may issue additional shares of common stock in exchange for the tendered O.P. Units.

Our Board of Directors also has the authority to cause the operating partnerships to issue additional O.P. Units in any manner and on such terms and for such consideration, as it deems appropriate, including in exchange for property. In the event that the operating partnerships issue new O.P. Units for cash, but not property, the limited partners holding O.P. Units in an operating partnership will have the right to purchase O.P. Units in order, and to the extent necessary, to maintain their respective percentage interests in that operating partnership. The new O.P. Units will be exchangeable for common stock pursuant to the exchange rights or may be tendered to us pursuant to the put rights.



DISPOSITION POLICIES

From time to time we may dispose of properties in our portfolio, subject to the required approvals as set forth below. During the past two years we have sold vacant R&D properties that we did not believe were likely to earn the type of return on assets that we seek. We will continue to dispose of under-performing properties when we consider it appropriate.

A significant factor influencing our disposition policy is that the tax basis of the limited partners in the properties in the operating partnerships is substantially less than current fair market value. Accordingly, prior to the disposition of their O.P. Units, upon a disposition of any of the properties, a disproportionately large share of the gain for federal income tax purposes would be allocated to the limited partners.

In addition, the approval of a majority of our directors, including Carl E. Berg or his designee, will be required to sell all or substantially all of our assets. The consent of the holders of a majority of the O.P. Units will be required to effect a sale or sales of all, or substantially all, of the assets of any of the operating partnerships.

IMPACT OF NEW ACCOUNTING PRONOUNCEMENTS

For discussion of recent accounting pronouncements, see Item 8, "Financial

Statements and Supplementary Data - Note 2" to our consolidated financial statements included in this report.



ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We do not generally hold market risk sensitive instruments for trading purposes. We use fixed and variable rate debt to finance our operations. Our exposure to market risk for changes in interest rates relates primarily to our current variable rate debt and our future debt obligations. We are vulnerable to significant fluctuations of interest rates on our floating rate debt.

We manage our market risk by monitoring interest rates where we try to recognize the unpredictability of the financial markets and seek to reduce potentially adverse effects on the results of our operations. This takes frequent evaluation of available lending rates and examination of opportunities to reduce interest expense through new sources of debt financing. Several factors affecting the interest rate risk include governmental monetary and tax policies, domestic and international economics and other factors that are beyond our control. The following table provides information about the principal cash flows, weighted average interest rates, and expected maturity dates for debt outstanding as of December 31, 2008. The current terms of our outstanding debt are described in Item 8, "Financial Statements and Supplementary Data - Note 8." For fixed rate debt, we estimate fair value by using discounted cash flow analyses based on borrowing rates for similar kinds of borrowing arrangements. We estimated that the fair value of fixed rate debt at December 31, 2008 was approximately $496.3 million.

For fixed rate debt, the table presents the assumption that the outstanding principal balance at December 31, 2008 will be paid according to scheduled principal payments and that we will not prepay any of the outstanding principal balance.

For variable rate debt, the table presents the assumption that the outstanding principal balance at December 31, 2008 will be paid upon maturity.

| | 2009 | 2010 | 2011 | 2012 | 2013 | The |
|---|---|---|---|---|---|---|
| | | | | (dollars in thousands) | | |
| FIXED RATE DEBT: | | | | | | |
| Secured notes payable | $12,591 | $13,327 | $14,109 | $14,935 | $81,269 | $2 |
| Weighted average interest rate | 5.86% | 5.86% | 5.86% | 5.86% | 5.86% | |
| VARIABLE RATE DEBT: | | | | | | |
| Unsecured debt | $13,079 | - | - | - | - | |
| Weighted average interest rate | 3.17% | - | - | - | - | |

The fixed rate debt represented 96.3% and 100% and the variable rate debt represented 3.7% and 0% of all debt outstanding for the years ended December 31, 2008 and 2007, respectively.

All of our debt is denominated in United States dollars. The weighted average interest rate for the fixed rate debt was approximately 5.86% and 5.85% for the years ended December 31, 2008 and 2007, respectively. The increase in interest

expense attributable to the average interest rate difference between 2007 and 2008 was approximately $0.3 million, which was a result of new debt obtained in 2008.

The primary market risk we face is the risk of interest rate fluctuations. The Heritage Bank of Commerce line of credit, which is tied to a LIBOR based interest rate, was approximately $13.1 million, or 3.7%, of the total $352.7 million of debt as of December 31, 2008. With a floating interest rate we could pay lower rates of interest in periods of decreasing interest rates and higher rates of interest in periods of increasing interest rates. As of December 31, 2008 and 2007, we did not have any derivative instruments.

The following discussion of market risk is based solely on a possible hypothetical change in future market conditions related to our variable rate debt. It includes "forward-looking statements" regarding market risk, but we are not forecasting the occurrence of these market changes. Based on the amount of variable debt outstanding as of December 31, 2008, a 1% increase or decrease in interest rates on our $13.1 million of floating rate debt would decrease or increase, respectively, annual earnings and cash flows by approximately $0.1 million, as a result of the increased or decreased interest expense associated with the change in rate, and would not have an impact on the fair value of the floating rate debt. This amount is determined by considering the impact of hypothetical interest rates on our borrowing cost. Due to the uncertainty of fluctuations in interest rates and the specific actions that might be taken by us to mitigate any such fluctuations and their possible effects, the foregoing sensitivity analysis assumes no changes on our financial structure.



ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

MISSION WEST PROPERTIES, INC.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

Report of Independent Registered Public Accounting Firm
Report of Independent Registered Public Accounting Firm on Internal Control over Financial Report
Consolidated Balance Sheets as of December 31, 2008 and 2007
Consolidated Statements of Operations for the years ended December 31, 2008, 2007 and 2006
Consolidated Statements of Stockholders' Equity for the years ended December 31, 2008, 2007 and 2
Consolidated Statements of Cash Flows for the years ended December 31, 2008, 2007 and 2006
Notes to Consolidated Financial Statements
Supplemental Financial Information
Report of Independent Registered Public Accounting Firm on Financial Statement Schedule
Schedule III: Real Estate and Accumulated Depreciation as of December 31, 2008
Schedule III: Real Estate and Accumulated Depreciation as of December 31, 2007

## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders
Mission West Properties, Inc.
Cupertino, California

We have audited the accompanying consolidated balance sheets of Mission West Properties, Inc. (the "Company") as of December 31, 2008 and 2007, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2008. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Mission West Properties, Inc. at December 31, 2008 and 2007, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2008, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2008, based on the criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 13, 2009 expressed an unqualified opinion thereon.

\S\ Burr, Pilger & Mayer, LLP

San Francisco, California
March 13, 2009



## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Board of Directors and Stockholders
Mission West Properties, Inc.
Cupertino, California

We have audited Mission West Properties, Inc.'s (the Company) internal control over financial reporting as of December 31, 2008, based on criteria established in Internal Control--Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the "COSO criteria"). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect that transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Mission West Properties, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2008, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Mission West Properties, Inc. as of December 31, 2008 and 2007, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2008, and the related financial statement schedules listed in the Index at Item 15(a), and our reports dated March 13, 2009 expressed an unqualified opinion thereon.

\S\ Burr, Pilger & Mayer, LLP

San Francisco, California
March 13, 2009



MISSION WEST PROPERTIES, INC.
CONSOLIDATED BALANCE SHEETS
(dollars in thousands, except per share data)

ASSETS

| | Dece |
|---|---|
| | 2008 |
| Investments in real estate: | |
| Land | $320,911 |
| Buildings and improvements | 799,471 |
| Real estate related intangible assets | 3,240 |
| Total investments in properties | 1,123,622 |
| Accumulated depreciation and amortization | (180,043) |
| Net investments in properties | 943,579 |
| Investment in unconsolidated joint venture | 3,768 |
| Net investments in real estate | 947,347 |
| Cash and cash equivalents | - |
| Restricted cash | 39,478 |
| Investment in marketable securities | 3,368 |
| Deferred rent receivables | 17,841 |
| Other assets, net | 26,251 |
| Total assets | $1,034,285 |

LIABILITIES AND STOCKHOLDERS' EQUITY

| | |
|---|---|
| Liabilities: | |
| Mortgage notes payable | $330,908 |
| Mortgage note payable (related parties) | 8,761 |
| Revolving line of credit | 13,079 |
| Interest payable | 1,596 |
| Security deposits | 5,272 |
| Deferred rental income | 3,964 |
| Dividends and distributions payable | 21,055 |
| Accounts payable and accrued expenses | 17,747 |
| Total liabilities | 402,382 |

| | |
|---|---|
| Commitments and contingencies (Note 16) | |
| Minority interests in operating partnerships | 497,485 |
| Stockholders' equity: | |
| Preferred stock, $.001 par value, 20,000,000 shares authorized, none issued and outstanding | - |
| Common stock, $.001 par value, 200,000,000 shares authorized, 19,748,211 and 19,664,087 shares issued and outstanding at December 31, 2008 and 2007 | 20 |
| Additional paid-in capital | 154,412 |
| Distributions in excess of accumulated earnings | (20,014) |
| Total stockholders' equity | 134,418 |
| Total liabilities and stockholders' equity | $1,034,285 |

See notes to consolidated financial statements.



MISSION WEST PROPERTIES, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(dollars in thousands, except per share data)

| | Year Ended De | |
|---|---|---|
| | 2008 | 2007 |
| Operating revenues: | | |
| Rental revenue from real estate | $79,075 | $80,3 |
| Above market lease intangible asset amortization | - | (4,0 |
| Tenant reimbursements | 16,406 | 13,3 |
| Other income, including lease terminations and settlements | 4,223 | 61,9 |
| Total operating revenues | 99,704 | 151,5 |
| Operating expenses: | | |
| Property operating, maintenance and real estate taxes | 23,460 | 20,3 |
| General and administrative | 2,635 | 3,0 |
| Depreciation and amortization of real estate | 23,224 | 22,5 |
| Total operating expenses | 49,319 | 45,9 |
| Operating income | 50,385 | 105,5 |
| Other income (expenses): | | |
| Equity in earnings of unconsolidated joint venture | 19,617 | 1,4 |
| Interest and dividend income | 1,735 | 3,0 |
| Unrealized loss from investment | (278) | |
| Interest expense | (19,787) | (20,1 |

| | | |
|---|---|---|
| Interest expense - related parties | (1,332) | (7 |
| Income from continuing operations before minority interests | 50,340 | 89,2 |
| Minority interests from continuing operations | (40,206) | (71,4 |
| Income from continuing operations | 10,134 | 17,7 |
| Discontinued operations, net of minority interests: | | |
| Gain from disposal of properties classified as discontinued operations | - | 1,1 |
| Income attributable to discontinued operations | - | |
| Income from discontinued operations | - | 1,1 |
| Net income to common stockholders | $10,134 | $18, |
| Net income to minority interests | $40,206 | $76, |
| Income per share from continuing operations: | | |
| Basic | $0.51 | $0. |
| Diluted | $0.51 | $0. |
| Income per share from discontinued operations: | | |
| Basic | - | $0. |
| Diluted | - | $0. |
| Net income per share to common stockholders: | | |
| Basic | $0.51 | $0. |
| Diluted | $0.51 | $0. |
| Weighted average shares of common stock (basic) | 19,714,414 | 19,627 |
| Weighted average shares of common stock (diluted) | 19,996,349 | 19,854 |
| Weighted average O.P. Units | 85,528,329 | 85,162 |
| Outstanding common stock | 19,748,211 | 19,664 |
| Outstanding O.P. Units | 85,526,965 | 85,533 |

See notes to consolidated financial statements.



MISSION WEST PROPERTIES, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(dollars in thousands, except per share data)

Additional

| | Shares of Common Stock Outstanding | Common Stock | Paid-in Capital |
|---|---|---|---|
| Balance, December 31, 2005 | 18,448,791 | $18 | $138,038 |
| Net income | | | |
| Dividends declared at $0.64 per share | | | |
| Issuance of common stock upon O.P. Unit conversion | 881,896 | 1 | 10,279 |
| Issuance of common stock upon option exercise | 112,900 | | 1,014 |
| Stock-based compensation | | | 210 |
| Balance, December 31, 2006 | 19,443,587 | 19 | 149,541 |
| Net income | | | |
| Dividends declared at $0.64 per share | | | |
| Issuance of common stock upon O.P. Unit conversion | 220,500 | 1 | 2,854 |
| Stock-based compensation | | | 629 |
| Balance, December 31, 2007 | 19,664,087 | 20 | 153,024 |
| Net income | | | |
| Dividends declared at $0.80 per share | | | |
| Issuance of common stock upon O.P. Unit conversion | 6,970 | | 66 |
| Issuance of common stock upon option exercise | 77,154 | | 852 |
| Stock-based compensation | | | 470 |
| Balance, December 31, 2008 | 19,748,211 | $20 | $154,412 |

See notes to consolidated financial statements.



MISSION WEST PROPERTIES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(dollars in thousands)

| | Year Ended | |
|---|---|---|
| | 2008 | |
| Cash flows from operating activities (including discontinued operations): | | |
| Net income | $10,134 | $ |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Minority interests in operating partnerships and discontinued operations | 40,206 | |
| Minority interests distributions | (40,206) | ( |
| Depreciation and amortization of real estate and in-place leases | 23,224 | |
| Amortization of above market lease | - | |
| Gain from disposal of properties classified as discontinued operations | - | |
| Equity in earnings of unconsolidated joint venture | (19,617) | |
| Distributions from unconsolidated joint venture | 18,584 | |
| Interest earned on restricted cash | (977) | |

| | | |
|---|---|---|
| Lease termination fee income related to restricted cash | 9,741 | ( |
| Stock-based compensation expense | 553 | |
| Other | 142 | |
| Change in operating assets and liabilities, net of liabilities assumed: | | |
| Deferred rent receivable | (3,008) | |
| Other assets | (2,575) | |
| Interest payable | 265 | |
| Security deposits | 518 | |
| Deferred rental income | 662 | |
| Accounts payable and accrued expenses | 2,129 | |
| Net cash provided by operating activities | 39,775 | |
| Cash flows from investing activities: | | |
| Improvements to investments in real estate | (6,468) | |
| Net proceeds from sale of properties | - | |
| Acquisition of properties | (35,764) | ( |
| Restricted cash held in escrow | - | ( |
| Restricted cash released for purchase of properties | 8,082 | |
| Proceeds from release of restricted cash | 7,654 | |
| Investment in marketable securities | (3,109) | |
| Net cash used in investing activities | (29,605) | |
| Cash flows from financing activities: | | |
| Proceeds from mortgage loan payable | 115,000 | |
| Principal payments on mortgage notes payable | (121,612) | ( |
| Principal payments on mortgage notes payable (related parties) | (463) | |
| Real estate purchase financing (related parties) | 19,429 | |
| Payment on real estate purchase financing (related parties) | (19,429) | |
| Proceeds from note payable (related parties) | 3,000 | |
| Payment on note payable (related parties) | (3,000) | |
| Net borrowings on revolving line of credit | 13,079 | |
| Debt issuance costs | (1,231) | |
| Loan escrow refund (deposit) | 1,500 | |
| Refund of appeal bond | - | |
| Net proceeds from exercise of stock options | 768 | |
| Minority interests distributions in excess of earnings | (25,923) | |
| Dividends paid | (14,979) | ( |
| Net cash used in financing activities | (33,861) | ( |
| Net (decrease)/increase in cash and cash equivalents | (23,691) | ( |
| Cash and cash equivalents, beginning of year | 23,691 | |
| Cash and cash equivalents, end of year | $ - | $ |

See notes to consolidated financial statements.



MISSION WEST PROPERTIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in thousands, except per share data)

1. ORGANIZATIONS AND FORMATION OF THE COMPANY

Mission West Properties, Inc. ("the Company") is a fully integrated, self-administered and self-managed real estate company that acquires and manages research and development ("R&D")/office properties in the portion of the San Francisco Bay Area commonly referred to as Silicon Valley. In July 1998, the Company purchased an approximate 12.11% interest in each of four existing limited partnerships (referred to collectively as the "operating partnerships") and obtained control of these partnerships by becoming the sole general partner in each one effective July 1, 1998 for financial accounting and reporting purposes. At that time, all limited partnership interests in the operating partnerships were converted into 59,479,633 Operating Partnership Units ("O.P. Units"), which represented a limited partnership ownership interest of approximately 87.89% of the operating partnerships. The operating partnerships are the vehicles through which the Company holds its real estate investments, makes real estate acquisitions, and generally conducts its business.

As of December 31, 2008, the Company owns a controlling general partner interest of 20.02%, 21.85%, 16.31% and 12.52% in Mission West Properties, L.P., Mission West Properties, L.P. I, Mission West Properties, L.P. II and Mission West Properties, L.P. III, respectively, for an 18.73% general partner interest in the operating partnerships, taken as a whole, on a consolidated weighted average basis.

The Company, through the operating partnerships, owns interests in 111 R&D properties at December 31, 2008, all of which are located in the Silicon Valley.

BUSINESS SEGMENT INFORMATION

The Company's primary business is the ownership and management of R&D/office real estate with a geographic concentration in the Silicon Valley of the San Francisco Bay Area. Accordingly, the Company has concluded that it currently has a single reportable segment for Statement of Financial Accounting Standards ("SFAS") 131 purposes.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

PRINCIPLES OF CONSOLIDATION AND FINANCIAL STATEMENT PRESENTATION

The accompanying consolidated financial statements include the accounts of the Company and its controlled subsidiaries, the operating partnerships (the "Company"). All significant intercompany transactions have been eliminated in consolidation.

The Company consolidates all variable interest entities in which it is deemed to be the primary beneficiary in accordance with Financial Accounting Standard Board ("FASB") Interpretation No. 46 (Revised December 2003), "Consolidation of Variable Interest Entities" ("FIN 46R").

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenue and expenses during the reporting periods. Accounting and disclosure decisions with respect to material transactions that are subject to significant management judgments or estimates include impairment of long lived assets, realizability of deferred rent receivables, and allocation of purchase price relating to property acquisitions and the related depreciable lives assigned. Actual results could differ materially from those estimates.

REAL ESTATE ASSETS AND RELATED INTANGIBLE ASSETS

Real estate assets are stated at cost. Cost includes expenditures for improvements or replacements. Maintenance and repairs are charged to expense as incurred.

According to SFAS 141, "Business Combinations," the fair value of the real estate acquired is allocated to the acquired tangible assets, consisting of land, building and tenant improvements, and identified intangible assets and liabilities, consisting of the value of above-market and below-market leases, other value of in-place leases and value of tenant relationships, based in each case on their relative fair values. SFAS 141 was revised in December 2007. The fair value of the tangible assets of an acquired property, which includes land, building and tenant improvements, is determined by valuing the property as if it were vacant, and the "as-if-vacant" value is then allocated to land, building and tenant improvements based on management's determination of the relative fair values of these assets. Factors considered by management in performing these analyses include certain costs during the lease-up periods considering current market conditions and costs to execute similar leases. These costs include estimates of lost rental revenue, leasing commissions, and tenant improvements.





In allocating the fair value of the identified intangible assets of the acquired property, above-market in-place lease value is recorded based on the present value, using an interest rate which reflects the risks associated with the lease acquired, of the difference between (i) the contractual amounts to be paid pursuant to the in-place lease and (ii) management's estimate of fair market lease rate for the corresponding in-place lease, measured over a period equal to the remaining non-cancelable lease term. The capitalized above-market lease value, included in real estate related intangible assets, is amortized as an offset to rental revenue from real estate over the remaining non-cancelable lease term. The value of in-place leases, exclusive of the value of above-market in-place lease, is amortized to expense over the remaining non-cancelable periods of the respective leases. If a lease were to be terminated prior to its stated expiration, all unamortized amounts relating to that lease would be written off in the period that the lease is terminated.

DEPRECIATION AND AMORTIZATION

Depreciation and amortization are computed using the straight-line method over estimated useful lives as follows:

| | | |
|---|---|---|
| Building shell and base building improvements of newly acquired properties | - | Weighted average |
| Base building improvements made subsequent to initial property acquisition | - | 25 years |
| Tenant improvements and furniture and fixtures | - | Lesser of life o<br>or term of lease |
| Above-market and in-place lease value | - | Term of lease |

IMPAIRMENT OF LONG-LIVED ASSETS

The Company reviews real estate assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable in accordance with SFAS 144, "Accounting for the Impairment and Disposal of Long-Lived Assets." If the carrying amount of the asset, including any intangible assets associated with that asset, exceeds its estimated

undiscounted net cash flow, before interest, the Company will recognize an impairment loss equal to the difference between its carrying amount and its estimated fair value. If impairment is recognized, the reduced carrying amount of the asset will be accounted for as its new cost. For a depreciable asset, the new cost will be depreciated over the asset's remaining useful life. Generally, fair values are estimated using discounted cash flow, replacement cost or market comparison analyses. The analysis that the Company prepares in connection with determining if there may be any asset impairment loss under SFAS 144 considers several assumptions: holding period of ten years, 36 months lease up period and cap rate ranging from 8% to 9%. The process of evaluating for impairment requires estimates as to future events and conditions, which are subject to varying market and economic factors, such as the vacancy rates, rental rates and operating costs for R&D facilities in the Silicon Valley area and related submarkets. Therefore, it is reasonably possible that a change in estimate resulting from judgments as to future events could occur which would affect the recorded amounts of the property. No impairment losses were recorded for the years ended December 31, 2008 and 2007.

ASSETS HELD FOR SALE AND DISCONTINUED OPERATIONS

In accordance with SFAS 144, the results of operations and gains or losses on the sale of property are presented as discontinued operations if both the following criteria are met: (a) the operation and cash flows of the property have been (or will be) eliminated from the ongoing operations of the Company as a result of the disposal transaction; and (b) the Company will not have any significant involvement in the operations of the property after the disposal transaction. SFAS 144 also requires prior period results of operations for these properties to be retrospectively adjusted and presented in discontinued operations in prior consolidated statements of operations.

An asset is generally classified as held for sale once management has committed to an action to sell the asset, the asset is available for immediate sale in its present condition (subject to terms that are usual and customary for sales of such assets), an active program to locate a buyer is initiated, the sale is probable, the asset is being actively marketed for sale at a price that is reasonable in relation to its current fair value and actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn. Properties for sale with significant contingencies that may prevent their sale, such as obtaining rezoning approval from the city, are not classified as assets held for sale. Upon the classification of a real estate asset as held for sale, the carrying value of the asset is reduced to the lower of its net book value or its fair value, less costs to sell the asset. Subsequent to the classification of assets as held for sale, no further depreciation expense is recorded. Real estate assets held for sale are stated separately on the accompanying consolidated balance sheets. The operating results of real estate assets held for sale and sold are reported as discontinued operations in the accompanying consolidated statements of operations. The income/(loss) from discontinued operations includes the revenues and expenses, including depreciation, associated with the assets. This classification of operating results as discontinued operations applies retroactively for all periods presented for assets designated as held for sale. Additionally, gains and losses on assets designated as held for sale are classified as part of discontinued operations.

CASH AND CASH EQUIVALENTS

The Company considers highly liquid short-term investments with initial maturities of three months or less to be cash equivalents. Cash and cash equivalents are primarily held in one or more financial institutions, and at times, such balances may be in excess of the Federal Deposit Insurance Corporation insurance limit.

MISSION WEST PROPERTIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, CONTINUED
(Dollars in thousands, except per share data)

RESTRICTED CASH
Restricted cash totaled approximately $39,478 as of December 31, 2008. The entire amount represents a balance the Company has consolidated due to its adoption of FIN 46R, The Company does not possess or control these funds or have any rights to receive them except as provided in the applicable agreements. Therefore, restricted cash is not available for distribution to stockholders.

FUNDS HELD AT QUALIFIED INTERMEDIARY FOR 1031 EXCHANGE
Periodically, the Company enters into exchange agreements with qualified intermediaries to facilitate the exchange of real property pursuant to Section 1031 of the Code ("Section 1031 Exchange"). A Section 1031 Exchange generally allows for the deferral of income taxes related to the gain attributable to the sale of property if qualified replacement properties are identified within 45 days and such qualified replacement properties are acquired within 180 days from the initial sale. During the replacement period, the Company may direct the proceeds from a disposition to be held at a qualified intermediary for the sole purpose of completing a Section 1031 Exchange. The proceeds are generally classified as restricted cash.

INVESTMENT IN MARKETABLE SECURITIES
Marketable securities reported in the Company's consolidated balance sheet represent investments traded in the open market. The marketable securities are adjusted to fair value at the end of each accounting period, with the corresponding losses and gains recorded in unrealized losses or gains from investment. For the year ended December 31, 2008, the Company recorded net unrealized losses of approximately $278 related to the decrease in fair value of the marketable securities, which was reported in unrealized loss from investment in the Company's consolidated statement of operations.

OTHER ASSETS
Included in other assets are costs associated with obtaining debt financing and commissions associated with new leases. Such debt financing costs are being amortized over the term of the associated debt, by a method that approximates the effective interest method and such lease commissions are amortized straight-line over the term of the related lease. If the lease is terminated prior to the end of the lease term, the Company charges any unamortized capitalized lease commission cost to expense in the period that the lease is terminated. Also included in other assets are commitments from the Berg Group of approximately $7,494 to construct a building at 245 Caspian Drive in Sunnyvale, California (see Note 13 below).

MINORITY INTERESTS
Minority interests in the operating partnerships represent the proportionate share of the equity in the operating partnerships of the limited partners. Minority interests in net income is calculated by taking the net income of the operating partnerships (on a stand-alone basis) multiplied by the respective minority interests' ownership percentage.

REVENUE RECOGNITION
Rental income is derived from operating leases and recognized on the straight-line method of accounting required by GAAP under which contractual rent payment increases are recognized evenly over the lease term. The difference between recognized rental income and rental cash receipts is recorded as "Deferred rent receivable" on the consolidated balance sheets. Certain lease agreements contain terms that provide for additional rents based on reimbursement of certain costs including property operating expenses, maintenance and real estate taxes. These additional rents from tenant

reimbursements are reflected on the accrual basis.

Rental revenue is affected if existing tenants terminate or amend their leases. The Company tries to identify tenants who may be likely to declare bankruptcy, cease operations or otherwise terminate leases prior to the end of the lease term, such as tenants who do not occupy all or a large portion of the property being leased. By anticipating these events in advance, the Company expects to take steps to minimize their impact on its reported results of operations through lease renegotiations and other appropriate measures. Reserves against "Deferred rent receivable" are estimated by management based on known financial conditions of tenants and management's estimate of net realizability of such receivables based on existing or expected negotiations with tenants. The Company's judgments and estimations about tenants' capacity to continue to meet their lease obligations will affect the rental revenue recognized. To date, actual reductions in revenue as a result of early terminations and the tenants' inability to pay have been within management's estimates. However, material differences may result in the amount and timing of the Company's rental revenue for any period if it made different judgments or estimations.

Lease termination fees are recognized in operating revenues when there is a signed termination letter agreement, all of the conditions of the agreement have been met, the tenant is no longer occupying the property and the termination consideration is probable of collection. These fees are paid by tenants who want to terminate their lease obligations before the end of the contractual term of the lease by agreement with us. There is no way of predicting or forecasting the timing or amounts of future lease termination fees.





The Company recognizes income from rent, tenant reimbursements and lease termination fees and other income once all of the following criteria are met in accordance with SEC Staff Accounting Bulletin 104, "Revenue Recognition":

- the agreement has been fully executed and delivered;
- services have been rendered;
- the amount is fixed and determinable; and
- the collectability is reasonably assured.

INCOME TAXES

The Company has been taxed as a real estate investment trust ("REIT") under the Internal Revenue Code of 1986, as amended, (the "Code") commencing with the taxable year ended December 31, 1999. In order for the Company to qualify as a REIT, it must distribute annually at least 90% of its REIT taxable income, as defined in the Code, to its stockholders and comply with certain other requirements. Accordingly, for the years ended December 31, 2008, 2007 and 2006, no provision for federal income taxes has been included in the accompanying consolidated financial statements.

For the year ended December 31, 2008, the Company's total dividends paid or payable to the stockholders represented approximately 73.3% ordinary income, 22.2% capital gain and 4.5% unrecaptured section 1250 gain for income tax purposes (unaudited). For the year ended December 31, 2007, the Company's total dividends paid or payable to the stockholders represented approximately 97% ordinary income, 2% capital gain and 1% unrecaptured section 1250 gain for income tax purposes (unaudited). For the year ended December 31, 2006, the Company's total dividends paid or payable to the stockholders represented 100% ordinary income for income tax purposes (unaudited).

NET INCOME PER SHARE
The computation of net income per share is based on the weighted average number of common shares outstanding during the period. Diluted earnings per share amounts are based upon the weighted average of common and common equivalent shares outstanding during the year.

ACCOUNTING FOR STOCK-BASED COMPENSATION
SFAS 123 (Revised 2004), "Share-Based Payment" ("SFAS 123R"), addresses the accounting for employee, director and consultant stock options. SFAS 123R requires that the cost of stock options, as well as other equity-based compensation arrangements, be reflected in the consolidated financial statements based on the estimated fair value of the awards. SFAS 123R is an amendment to SFAS 123 and supersedes Accounting Principles Board Opinion 25, "Accounting for Stock Issued to Employees" ("APB 25"). SFAS 123R is applicable to any award that is settled or measured in stock, including stock options, restricted stock, stock appreciation rights, stock units, and employee stock purchase plans. As of December 31, 2008, the Company had one stock-based compensation plan.

The Company measures compensation cost for its stock options at fair value on the date of grant and recognizes compensation expense relating to the remaining unvested portion of outstanding stock options at the time of adoption ratably over the vesting period, generally four years. The fair value of the Company's stock options is determined using the Black-Scholes option pricing model. Compensation expense related to the Company's share-based awards is included in general and administrative expenses in the Company's accompanying consolidated statements of operations. For the year ended December 31, 2008, under SFAS 123R, the Company recorded approximately $553 of expense for share-based compensation relating to stock options.

As of December 31, 2008, there was approximately $564 of total unrecognized compensation cost related to unvested share-based compensation arrangements granted under the compensation plan. That cost is expected to be recognized over a weighted-average period of approximately four years.

In January 2008, stock options to purchase 1,025,000 shares of common stock were granted to employees, non-employee directors and consultants. The options vest monthly for 48 months from date of grant, subject to continued employment or other service to the Company. Each option grant has a term of six years from the date of grant subject to earlier termination in certain events related to termination of employment or service. The options were granted at an exercise price of $9.51 per share. The estimated fair value of the options granted was $0.57 per share on the date of grant using the Black-Scholes option pricing model with the following assumptions: dividend yield of 8.41%, volatility of 20.43%, risk free rates of 3.45% and an expected life of six years. All options were granted at fair market value on the date of grant.

In July 2008, stock options to purchase 52,500 shares of common stock were granted to an employee and a non-employee director. The options vest monthly for 48 months from date of grant, subject to continued employment or other service to the Company. Each option grant has a term of six years from the date of grant subject to earlier termination in certain events related to termination of





employment or service. The options were granted at an exercise price of $11.36 per share. The estimated fair value of the options granted was $0.99 per share on the date of grant using the Black-Scholes option pricing model with the following assumptions: dividend yield of 7.04%, volatility of 22.07%, risk free

rates of 3.20% and an expected life of six years. All options were granted at fair market value on the date of grant.

In November 2008, stock options to purchase 705,000 shares of common stock were granted to employees, non-employee directors and consultants. The options vest monthly ranging from 36-48 months from date of grant, subject to continued employment or other service to the Company. Each option grant has a term of six years from the date of grant subject to earlier termination in certain events related to termination of employment or service. The options were granted at an exercise price of $6.14 per share. The estimated fair value of the options granted was $0.12 per share on the date of grant using the Black-Scholes option pricing model with the following assumptions: dividend yield of 13.03%, volatility of 22.39%, risk free rates of 2.08% and an expected life of six years. All options were granted at fair market value on the date of grant.

In 2007, stock options to purchase 710,000 shares of common stock were granted to employees, non-employee directors and consultants. The options vest monthly for 48 months from date of grant, subject to continued employment or other service to the Company. Each option grant has a term of six years from the date of grant subject to earlier termination in certain events related to termination of employment or service. The options were granted at an exercise price of $12.09 per share. The estimated fair value of the options granted in 2007 was $1.45 per share on the date of grant using the Black-Scholes option pricing model with the following assumptions: dividend yield of 5.29%, volatility of 18.94%, risk free rates of 4.53% and an expected life of six years. All options were granted at fair market value on the date of grant.

There were no stock options granted in 2006.

In April 2005, the Company's Compensation Committee of the Board of Directors, in accordance with the provisions of the 2004 Equity Incentive Plan, unanimously approved the following awards of dividend equivalent rights ("DERs"), each such DER representing the current right to receive the dividend paid on one share of the Company's common stock, when paid by the Company:

- The three non-employee outside directors each received 45,000 DERs effective as of the second quarter of 2005, which will remain in effect as long as the individual continues to serve on the Board of Directors; and
- Key employees of the Company received a total of 155,000 DERs effective as of the second quarter of 2005, which will remain in effect for each key employee as long as they continue to be employed by the Company.

In April 2005, a total of 290,000 DERs were awarded by the Company's Board of Directors. In 2008, one director and one employee forfeited 45,000 and 15,000 DERs, respectively, when they resigned from the Company. A new non-employee outside director was awarded 45,000 DERs when he joined the Company's Board of Directors. As of December 31, 2008, there was a total of 275,000 DERs. The Company recorded DER compensation expense of approximately $217, $186 and $186 in 2008, 2007 and 2006, respectively.

FAIR VALUE

On January 1, 2008, the Company adopted the provisions of SFAS 157, "Fair Value Measurements" ("SFAS 157") for its financial assets and liabilities measured at fair value on a recurring basis. SFAS 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. SFAS 157 also specifies a three-level hierarchy of valuation techniques based upon whether the inputs reflect assumptions other market participants would use based upon market data obtained from independent sources (observable inputs) or reflect its own assumptions of market participant valuation (unobservable inputs) and requires the use of observable inputs if such data is available without undue cost and effort. At December 31, 2008, the Company had approximately $3.4 million of financial

assets classified as Level 1 and thus measured at fair value using quoted market prices for identical instruments in active markets from an independent third party source.

The only financial asset or liability recorded at fair value in the Company's consolidated financial statements is the marketable securities. The Company determined the fair value for the marketable securities using quoted prices in active markets for identical securities.

In February 2007, the FASB issued SFAS 159, "The Fair Value Option for Financial Assets and Financial Liabilities" ("SFAS 159"). SFAS 159 provides companies with an option to report selected financial assets and liabilities at fair value and establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities. SFAS 159 was effective January 1, 2008. On January 1, 2008, the Company did not elect to apply the fair value option to any specific financial assets or liabilities.





The Company's financial instruments include cash and cash equivalents, accounts receivable, accounts payable, and debt. Considerable judgment is required in interpreting market data to develop estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts that the Company could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts. Cash and cash equivalents, accounts receivable, and accounts payable are carried at amounts that approximate their fair values due to their short-term maturities. For fixed rate debt, the Company estimates fair value by using discounted cash flow analyses based on borrowing rates for similar kinds of borrowing arrangements. The fair value of the Company's fixed rate debt at December 31, 2008 was approximately $496,320 compared with its carrying value of approximately $339,669.

RECLASSIFICATIONS
Certain amounts from prior year's consolidated financial statements have been reclassified to conform to the presentation of the current year's consolidated financial statements.

CONCENTRATION OF CREDIT RISK
The Company's properties are not geographically diverse, and its tenants operate primarily in the information technology industry. Additionally, because the properties are leased to 75 tenants at December 31, 2008, default by any major tenant could significantly impact the results of the consolidated total. One tenant, Microsoft Corporation, accounted for approximately 16.5%, 15.1% and 12.5% of the Company's total cash rental income for the years ended December 31, 2008, 2007 and 2006, respectively. Cash rental income from Microsoft Corporation was approximately $12,576, $12,288 and $11,728 for the years ended December 31, 2008, 2007 and 2006, respectively. Future minimum rents from this tenant are approximately $76,467. One other tenant accounted for approximately 9.8%, 10.8% and 10.0% of the Company's total cash rental income for the years ended December 31, 2008, 2007 and 2006, respectively. During 2008, 11 of the Company's tenants relocated or ceased operations.

NEW ACCOUNTING PRONOUNCEMENTS
In September 2006, the FASB issued SFAS 157, "Fair Value Measurements" ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. SFAS 157 applies

under other accounting pronouncements that require or permit fair value measurements. Accordingly, this statement does not require any new fair value measurements. This guidance was issued to increase consistency and comparability in fair value measurements and to expand disclosures about fair value measurements. SFAS establishes and requires disclosure of fair value hierarchy that distinguishes between data obtained from sources independent of the reporting entity and the reporting entity's own assumptions about market participant assumptions. The three levels of hierarchy are 1) using quoted prices in active markets for identical assets and liabilities, 2) "significant other observable inputs" and 3) "significant unobservable inputs". "Significant other observable inputs" can include quoted prices for similar assets or liabilities in active markets, as well as inputs that are observable for the asset or liability, such as interest rates, foreign exchange rates and yield curves that are observable at commonly quoted intervals. "Significant unobservable inputs" are typically based on an entity's own assumptions, as there is little, if any, related market activity. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. Adoption of SFAS 157 by the Company on January 1, 2008 did not have a material effect on the Company's consolidated financial statements. The FASB has approved a one-year deferral for the implementation of the statement for non-financial assets and non-financial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis. The Company believes that the impact of these items will not be material to its consolidated financial statements.

In February 2007, the FASB issued SFAS 159, "The Fair Value Option for Financial Assets and Financial Liabilities" ("SFAS 159"). SFAS 159 provides companies with an option to report selected financial assets and liabilities at fair value. SFAS 159's objective is to reduce both complexity in accounting for financial instruments and the volatility in earnings caused by measuring related assets and liabilities differently. SFAS 159 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The adoption of SFAS 159 did not have a material impact on the Company's consolidated financial statements since the Company elected not to apply the fair value option for any of its eligible financial instruments or other items.

In December 2007, the FASB issued SFAS 141 (Revised 2007), "Business Combinations" ("SFAS 141R"). SFAS 141R will change the accounting for business combinations. Under SFAS 141R, an acquiring entity will be required to recognize all the assets acquired and liabilities assumed in a transaction at the acquisition date fair value with limited exceptions. SFAS 141R will change the accounting treatment and disclosure for certain specific items in a business combination. Under SFAS 141R, certain transaction costs that have historically been capitalized as acquisition costs will be expensed. SFAS 141R applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. Early adoption is prohibited. Based on historical acquisition costs and activity levels, the adoption of SFAS 141R will not have a significant impact on the Company's results of operations and financial position.





In December 2007, the FASB issued SFAS 160, "Noncontrolling Interests in Consolidated Financial Statements" ("SFAS 160"). SFAS 160 requires that noncontrolling interests be presented as a component of consolidated stockholders' equity, eliminates "minority interest accounting" such that the amount of net income attributable to the noncontrolling interests will be presented as part of consolidated net income on the consolidated statement of

operations and not as a separate component of income and expenses. SFAS 160 is effective for fiscal years beginning on or after December 15, 2008. Early adoption is prohibited. The adoption of SFAS 160 will have a significant impact on the Company's computation of net income and its presentation of the balance sheet and statement of stockholders' equity.

3. DEFERRED RENT RECEIVABLE, NET

The following table represents activity in the allowance against deferred rent receivable, net for the years ended December 31, 2008, 2007 and 2006.

| | Beginning Balance | Provision Against Revenue | Charge-off | Ending Balance |
|---|---|---|---|---|
| | | (dollars in thousands) | | |
| Year ended December 31, 2006 | $2,000 | $1,216 | $1,216 | $2,000 |
| Year ended December 31, 2007 | $2,000 | $4,457 | $2,707 | $250 |
| Year ended December 31, 2008 | $250 | $259 | $259 | $250 |

4. STOCK TRANSACTIONS

As of December 31, 2008 and 2007, approximately $2,117 and $1,970 remained outstanding under notes issued in connection with the Company's purchase of its general partner interests in 1998 (the "demand notes"), respectively. The demand notes which accrue interest at 7.25%, along with the interest expense (interest income to the operating partnerships), are eliminated in consolidation and are not included in the corresponding line items within the consolidated financial statements. However, the interest income earned by the operating partnerships, which is interest expense to the Company, in connection with this debt, is included in the calculation of minority interest as reported on the consolidated statements of operations, thereby reducing the Company's net income by this same amount. The Company and the operating partnerships have agreed to extend the due date of the demand notes to September 30, 2010. At present, the Company's only means for repayment of this debt is through distributions received from the operating partnerships in excess of the amount of dividends to be paid to the Company's stockholders or by raising additional equity capital.

The limited partners of the operating partnerships have the right to tender their O.P. Units to the Company for shares of common stock or, at the Company's election, for cash. Each of the limited partners of the operating partnerships (other than Carl E. Berg and Clyde J. Berg) has the annual right to exercise put rights and cause the operating partnerships to purchase a portion of the limited partner's O.P. Units at a purchase price based on the average market value of the common stock for the 10-trading day period immediately preceding the date of tender, generally limited to one-third of the aggregate number of O.P. Units owned by each limited partner. Upon the exercise of any such right by a limited partner, the Company will have the option to purchase the tendered O.P. Units with available cash, borrowed funds or the proceeds of an offering of newly issued shares of common stock. These put rights are available once a year. If the total purchase price of the O.P. Units tendered by all of the eligible limited partners in one year exceeds $1 million, the Company or the operating partnerships is entitled in its discretion to reduce proportionately the number of O.P. Units to be acquired from each tendering limited partner so that the total purchase price does not exceed $1 million.

During the year ended December 31, 2008, stock options to purchase 70,487 shares of the Company's common stock were exercised at $10.00 per share and stock

options to purchase 6,667 shares of the Company's common stock were exercised at $9.51 per share. Total proceeds to the Company were approximately $768.

There were no stock option exercises in 2007.

During the year ended December 31, 2006, stock options to purchase 80,000 shares of the Company's common stock were exercised at $8.25 per share and stock options to purchase 32,900 shares of the Company's common stock were exercised at $10.00 per share. Total proceeds to the Company were approximately $989.

In 2008, 2007 and 2006, 6,970, 220,500 and 881,896 O.P. Units were exchanged for 6,970, 220,500 and 881,896 shares of the Company's common stock, respectively, under the terms of the Exchange Rights Agreement among the Company and all limited partners of the operating partnerships. Neither the Company nor the operating partnerships received any proceeds from the issuance of the common stock in exchange for O.P. Units.





5. MINORITY INTERESTS

Minority interests represent the separate private ownership of the operating partnerships, by the Berg Group and other non-affiliate interests. In total, these interests account for 81.27%, on a weighted average basis, of the ownership interests in the real estate operations of the Company as of December 31, 2008 and 2007. Minority interests in earnings have been calculated by taking the net income of the operating partnerships (on a stand-alone basis) multiplied by the respective minority interests' ownership percentage.

The operating partnerships have ownership interests of 83.33%, 75% and 50% and act as the managing member in three separate joint ventures, which were established to hold properties. The operating partnerships control the joint ventures, and accordingly, these joint ventures are consolidated in the Company's consolidated financial statements. The minority interests in the joint ventures are reflected as a component of minority interests of the operating partnerships. For the years ended December 31, 2008, 2007 and 2006, income associated with the minority interests held by third parties of the three consolidated joint ventures was approximately $368, $502 and $499, respectively.

6. REAL ESTATE

PROPERTY ACQUISITIONS

On January 1, 2008, the Company acquired an approximately 110,500 rentable square foot newly constructed R&D building located at 5981 Optical Court in San Jose, California from the Berg Group under the Berg Land Holdings Option Agreement. The total acquisition price for this property was approximately $19,068. The Company acquired this property by issuing a short-term note payable to the Berg Group, which was fully paid off in July 2008. The Company allocated the purchase price to land and building based upon the estimated relative fair values of such assets. Because the acquired property was vacant, there was no purchase price allocation to lease intangible assets. The property was leased within several days after the acquisition date.

On February 29, 2008, the Company acquired a fully leased office/R&D building comprised of approximately 75,300 rentable square feet at 2904 Orchard Parkway in San Jose, California from an unrelated party for approximately $16,696. The acquisition was partially funded from the proceeds received from the 1170 Morse Avenue property sale (see below under "Property Dispositions"), which were held

by a third party and classified as restricted cash as of December 31, 2007. The purchase price of 2904 Orchard Parkway was allocated to long-lived assets and the value of an in-place lease. The in-place lease was valued at fair market so there was no intangible asset allocated to above-or-below market lease value. The Company recorded approximately $1,121 of the purchase price as real estate related intangible asset in the accompanying consolidated balance sheet for the value of an in-place lease. The intangible asset is amortized over the applicable remaining lease term. Amortization expense of approximately $187 was recorded for the year ended December 31, 2008.

In March 2007, the Company acquired approximately 50 acres of vacant land in Morgan Hill, California, which could support approximately 725,000 rentable square feet of space. The land is currently zoned for industrial use and a portion has the potential to be rezoned for residential use. The acquisition price for this property was approximately $25,543 and was funded from a portion of the proceeds received from the Samaritan property sale, which were held by a third party and classified as restricted cash as of December 31, 2006.

In April 2007, the Company acquired three office/R&D buildings comprised of approximately 149,000 rentable square feet at Montague Expressway in Milpitas, California for approximately $15,351. The acquisition was funded from a portion of the proceeds received from the Samaritan property sale, which were held by a third party. With the exception of one lease, the property was purchased without any long-term tenants. The Company allocated the purchase price to land and building based upon the estimated relative fair values of such assets. There was no purchase price allocation to lease intangible assets.

In April 2007, the Company acquired approximately five acres of vacant land in Morgan Hill, California, which could support approximately 73,000 rentable square feet of space. The land is currently zoned for industrial use. The acquisition price for this property was approximately $2,297 and was funded from the remaining proceeds received from the Samaritan property sale, which were held by a third party.

In September 2007, the Company acquired an approximately 98,500 rentable square foot newly constructed R&D building located at 5845 Hellyer Avenue in San Jose, California from the Berg Group under the Berg Land Holdings Option Agreement. The total acquisition price for this property was approximately $10,903. The Company acquired this property by issuing 548,236 O.P. Units to the Berg Group and $4,300 in cash, which was paid in the fourth quarter of 2007. The Company allocated the purchase price to land





and building based upon the estimated relative fair values of such assets. Since the property was vacant when acquired, there was no purchase price allocation to lease intangible assets.

The purchase price allocation for these property acquisitions was determined in accordance with the following principles under SFAS 141:

- The fair value of the tangible assets of an acquired property, which includes land, building and tenant improvements, is determined by valuing the property as if it were vacant, and the "as-if-vacant" value is then allocated to land, building and tenant improvements based on management's determination of the relative fair values of these assets. Factors considered by management in performing these analyses include certain costs during the lease-up periods considering current market conditions and costs

to execute similar leases. These costs include estimates of lost rental revenue, leasing commissions and tenant improvements.

- The capitalized in-place lease value, included in real estate related intangible assets in the accompanying consolidated balance sheets, is amortized to expense as amortization of real estate over the remaining non-cancelable lease term. If a lease were to be terminated prior to its stated expiration, all unamortized amounts relating to that lease would be written off in the period that the lease is terminated.

PROPERTY DISPOSITIONS

In August 2007, the Company disposed of one R&D property located at 45700 Northport Loop in Fremont, California consisting of approximately 39,000 rentable square feet. A total net gain of approximately $1,699 was recognized and classified as discontinued operations, net of minority interests, on the total sales price of approximately $7,742. Proceeds from the sale were classified as restricted cash to be used in tax-deferred property exchanges as of December 31, 2007. In 2008, the entire proceeds from the sale were transferred to the Company's general cash account since it was unable to complete a tax-deferred property exchange.

In September 2007, the Company disposed of one R&D property located at 1170 Morse Avenue in Sunnyvale, California consisting of approximately 48,000 rentable square feet. A total net gain of approximately $4,830 was recognized and classified as discontinued operations, net of minority interests, on the total sales price of approximately $8,301. Proceeds from the sale were classified as restricted cash to be used in tax-deferred property exchanges as of December 31, 2007.

BERG LAND HOLDINGS OPTION AGREEMENT

Under the terms of the Berg Land Holdings Option Agreement, the Company, through the operating partnerships, has the option to acquire any future R&D property developed by the Berg Group on land currently owned or optioned, or acquired for these purposes in the future, directly or indirectly, by Carl E. Berg or Clyde J. Berg. This agreement will expire on December 31, 2010, after which the Company will no longer have the right to acquire properties from the Berg Group on the pre-determined terms provided in that agreement. At present, there are approximately 84 acres of Silicon Valley land, including land under development, owned directly or under 50% joint venture entities by certain members of the Berg Group that are subject to the terms of the Berg Land Holdings Option Agreement. The owners of the future R&D property developments may obtain cash or, at their option, O.P. Units valued at the average closing price of the shares of common stock over the 30-trading-day period preceding the acquisition date. To date, the Company has completed 23 acquisitions under the Berg Land Holdings Option Agreement representing approximately 2,243,000 rentable square feet. The acquired properties cost approximately $237,775, for which the Company issued 8,482,085 O.P Units and assumed debt of approximately $141,410. Upon the Company's exercise of an option to purchase any of the future R&D property developments, the acquisition price will equal the sum of (a) the full construction cost of the building; plus (b) 10% of the full construction cost of the building; plus (c) interest at LIBOR (London Interbank Offered Rate) plus 1.65% on the amount of the full construction cost of the building for the period from the date funds were disbursed by the developer to the close of escrow; plus (d) the original acquisition cost of the parcel on which the improvements will be constructed, which range from $8.50 to $20.00 per square foot for land currently owned; plus (e) 10% per annum of the amount of the original acquisition cost of the parcel from the later of January 1, 1998 or the seller's acquisition date to the close of escrow; minus (f) the aggregate principal amount of all debt encumbering the acquired property, or a lesser amount as approved by the members of the Independent Directors committee of the Company's Board of Directors. Generally, the Company will not acquire any projects until they are fully completed and leased.

No estimate can be given at this time as to the total cost to the Company to acquire future projects under the Berg Land Holdings Option Agreement, or the timing as to when the Company will acquire such projects. In addition to any projects currently under development, the Company has the right to acquire future developments by the Berg Group on up to 84 additional acres of land currently controlled by the Berg Group, which could support approximately 1.4 million square feet of new developments. Under the Berg Land Holdings Option Agreement, as long as the Berg Group ownership in the Company and the operating partnerships taken as a whole is at least 65%, or until December 31, 2010, whichever occurs first, the Company also has an option to purchase all land





acquired, directly or indirectly, by Carl E. Berg or Clyde J. Berg in the future which has not been improved with completed buildings and which is zoned for, intended for or appropriate for R&D, office and/or industrial development or use in the states of California, Oregon, and Washington.

Although the Company has the right to acquire the new properties available to it under the terms of the Berg Land Holdings Option Agreement, there can be no assurance that the Company actually will consummate any intended transactions. Furthermore, the Company has not yet determined the means by which it would acquire and pay for any such properties or the impact of any of the acquisitions on its business, results of operations, financial condition or available cash for distribution.

7. VARIABLE INTEREST ENTITY

Under FIN 46R, a variable interest entity ("VIE") must be consolidated by a company if that company is subject to a majority of the entity's expected losses or entitled to receive a majority of the entity's expected residual returns or both. FIN 46R requires disclosures about variable interest entities that a company is not required to consolidate, but in which it has a significant variable interest.

Under FIN 46R, for an entity to qualify as a VIE one or more of the following three characteristics must exist:

1. The equity investment at risk is not sufficient to permit the entity to finance its activities without additional subordinated financial support by any parties, including the equity holders.
2. The equity investors lack one or more of the following essential characteristics of a controlling financial interest: a. the direct or indirect ability to make decisions about the entity's activities through voting or similar rights; b. the obligation to absorb the expected loss of the entity; c. the right to receive the expected residual returns of the entity; or
3. The equity investors have voting rights that are not proportionate to their economic interests, and the activities of the entity involve or are conducted on behalf of an investor with a disproportionately small voting interest.

In August 2007, one of the Company's tenants, Ciena Corporation, entered into an assignment of lease agreement with an unrelated party, M&M Real Estate Control & Restructuring, LLC ("M&M"), in connection with leases for approximately 445,000 rentable square feet located in San Jose, California. As a result of the assignment, M&M assumed all of Ciena's remaining obligations under these leases

and received a payment from Ciena of $53,000, of which $7,000 was reserved for tenant improvements. At the same time, the Company entered into a consent for assignment of lease with both parties and a mutual release agreement with Ciena, pursuant to which all of Ciena's obligations under these leases were effectively transferred to M&M. M&M is obligated to continue to perform all of the obligations under the assumed Ciena leases and has the right to sublease any or all of the 444,500 rentable square feet vacated by Ciena for the remainder of the current lease term, which expires in 2011. Under the terms of the assignment of lease agreement, the Company received monthly rent payments of approximately $789 from July 2007 through June 2008, and will receive $818 from July 2008 through June 2009, $849 from July 2009 through June 2010, $881 from July 2010 through June 2011 and $915 from July 2011 through December 2011. Based upon FIN 46R, the Company determined that M&M is a VIE. The Company further determined that it is the primary beneficiary of this VIE and therefore has consolidated this entity for financial reporting purposes. Upon consolidation, the Company recognized a gross lease termination fee of $46,000 in August 2007.

Factors considered by the Company in determining whether M&M should be considered a VIE for financial reporting purposes included the following:

- No equity was contributed by the partners in the formation of M&M.
- At present, the assigned leases are the only properties under management by M&M.
- Because M&M does not have an operating history that demonstrates its ability to finance its activities without additional subordinated financial support.
- All revenues, other than interest income, are generated by M&M from the Company in the form of fees or commissions.

The Company remains at risk with respect to the assigned leases because if M&M's operating expenses exceed its interest income, fees and commissions there would be insufficient funds to meet the assigned lease obligation without additional financial support from equity holders or other parties. The Company, which had released the original tenant from its obligations under the lease, would have to absorb the majority of any loss, making it the primary beneficiary of M&M's activities.





8. DEBT

The following table sets forth certain information regarding debt outstanding as of December 31, 2008 and 2007.

| Debt Description | Collateral Properties | Balance December |
|---|---|---|
| | | 2008 |
| | | (dollars in |
| Line of Credit: | | |
| Heritage Bank of Commerce(1) | Not Applicable | $13,079 |

| | | |
|---|---|---|
| Mortgage Notes Payable (related parties): | 5300-5350 Hellyer Avenue, San Jose, CA | 8,761 |
| | | ------------- |
| Mortgage Notes Payable:(2) | | |
| Hartford Life Insurance Company(3) | 5981 Optical Court, San Jose, CA | 114,513 |
| Hartford Life and Accident Ins. Co. | 5500 Hellyer Avenue, San Jose, CA | |
| Hartford Life and Annuity Ins. Co. | 5550 Hellyer Avenue, San Jose, CA | |
| (collectively known as the "Hartford Loan") | 4050 Starboard Drive, Fremont, CA | |
| | 45738 Northport Loop, Fremont, CA | |
| | 233 South Hillview Drive, Milpitas, CA | |
| | 10300 Bubb Road, Cupertino, CA | |
| | 1230 E. Arques, Sunnyvale, CA | |
| | 1250-1280 E. Arques, Sunnyvale, CA | |
| | 1212 Bordeaux Lane, Sunnyvale, CA | |
| | 2904 Orchard Parkway, San Jose, CA | |
| | 3236 Scott Blvd, Santa Clara, CA | |
| | 6311 San Ignacio Avenue, San Jose, CA | |
| | 6321-6325 San Ignacio Avenue, San Jose, CA | |
| | 6331 San Ignacio Avenue, San Jose, CA | |
| | 6341-6351 San Ignacio Avenue, San Jose, CA | |
| | 3540-3580 Bassett Street, Santa Clara, CA | |
| Prudential Mortgage Capital Company(4) | Not Applicable | - |
| Northwestern Mutual Life Insurance Co.(5) | 1750 Automation Parkway, San Jose, CA | 81,308 |
| | 1756 Automation Parkway, San Jose, CA | |
| | 1762 Automation Parkway, San Jose, CA | |
| | 6320 San Ignacio Avenue, San Jose, CA | |
| | 6540-6541 Via Del Oro, San Jose, CA | |
| | 6385-6387 San Ignacio Avenue, San Jose, CA | |
| | 20605-20705 Valley Green Drive, Cupertino, CA | |
| | 2001 Walsh Avenue, Santa Clara, CA | |
| | 2220 Central Expressway, Santa Clara, CA | |
| | 2300 Central Expressway, Santa Clara, CA | |
| | 2330 Central Expressway, Santa Clara, CA | |
| Allianz Life Insurance Company(I)(6) | 5900 Optical Court, San Jose, CA | 23,009 |
| Allianz Life Insurance Company(II)(6) | 5325-5345 Hellyer Avenue, San Jose, CA | 112,078 |
| | 1768 Automation Parkway, San Jose, CA | |
| | 2880 Scott Boulevard, Santa Clara, CA | |
| | 2890 Scott Boulevard, Santa Clara, CA | |
| | 2800 Scott Boulevard, Santa Clara, CA | |
| | 10450-10460 Bubb Road, Cupertino, CA | |
| | 6800-6810 Santa Teresa Blvd., San Jose, CA | |
| | 6850 Santa Teresa Blvd., San Jose, CA | |
| | 4750 Patrick Henry Drive, Santa Clara, CA | |
| | | ------------- |
| | | 330,908 |
| | | ------------- |
| Total | | $352,748 |
| | | ============= |

(1) The Heritage Bank of Commerce ("HBC") line of credit was obtained in March 2008. Interest rate for the HBC line of credit is LIBOR plus 1.75%. The interest rate for the HBC line of credit at December 31, 2008 was 3.17%. In April 2008, the Company entered into a "Change in Terms Agreement" with HBC that increased the facility from $10 million to $17.5 million. The HBC line of credit contains certain financial loan and reporting covenants as

defined in the loan agreement. As of December 31, 2008, the Company was in compliance with these loan covenants.

(2) Mortgage notes payable generally require monthly installments of interest and principal ranging from approximately $177 to $840 over various terms extending through the year 2025. The weighted average interest rate of mortgage notes payable was 5.86% and 5.85% at December 31, 2008 and 2007, respectively.

(3) The Hartford loan is payable in monthly installments of approximately $838, which includes principal (based upon a 20-year amortization) and interest. Costs and fees incurred with obtaining this loan aggregated approximately $1,058, which were deferred and amortized over the loan period. The Hartford loan contains certain customary covenants as defined in the loan agreement. As of December 31, 2008, the Company was in compliance with these loan covenants.

(4) Proceeds from the Hartford loan were used to repay the remaining balance of the Prudential loan in October 2008.

(5) The Northwestern loan is payable in monthly installments of approximately $696, which includes principal (based upon a 20-year amortization) and interest. Costs and fees incurred with obtaining this loan aggregated approximately $664, which were deferred and amortized over the loan period. The Northwestern loan contains certain customary covenants as defined in the loan agreement. As of December 31, 2008, the Company was in compliance with these loan covenants.





(6) The Allianz loans are payable in monthly installments of approximately $1,017, which includes principal (based upon a 20-year amortization) and interest. Costs and fees incurred with obtaining these loans aggregated approximately $1,125, which were deferred and amortized over the loan periods. The Allianz loans contain certain customary covenants as defined in the loan agreements. As of December 31, 2008, the Company was in compliance with these loan covenants.

On March 4, 2008, the Company established a $10,000 uncollateralized revolving line of credit with Heritage Bank of Commerce ("HBC"). The Company paid approximately $26 in loan and legal fees. On April 17, 2008, the Company entered into a "Change in Terms Agreement" with HBC that increased the facility from $10,000 to $17,500. The line of credit bears an interest rate of LIBOR plus 1.75% and matures June 15, 2009. The HBC line of credit contains certain financial loan and reporting covenants as defined in the loan agreements. As of December 31, 2008, the Company was in compliance with these loan covenants. The proceeds from the HBC line of credit may be used to repay debt, complete acquisitions and finance other working capital requirements.

On October 1, 2008, the Company entered into a fixed rate term agreement and related contracts and instruments for a secured mortgage loan totaling $115,000 from Hartford Life Insurance Company, Hartford Life and Accident Insurance Company and Hartford Life and Annuity Insurance Company (the "Hartford Loan"). The proceeds were used primarily to repay the remaining balance of an existing mortgage loan with Prudential Mortgage Capital Company and to provide other working capital needs. The Hartford Loan bears a fixed interest rate of 6.21%, with a 20-year amortization, and matures October 1, 2018, at which time any

outstanding principal and interest will be due. Pursuant to the loan agreement, monthly principal and interest installment payments of approximately $838 are due on the first day of each month. The Hartford Loan is secured by 20properties consisting of approximately 1.6 million rentable square feet. The Company paid approximately $1,058 in loan fees and financing costs, which are amortized over the ten year loan period. The Company has the option to prepay the Hartford Loan, subject to certain yield maintenance provisions, though generally no prepayment is permitted during the first 24 months of the loan term.

During 2008, the Company issued multiple short-term notes payable to the Berg Group in connection with a property acquisition, quarterly dividend distributions and a cash loan. The interest rates on these notes were LIBOR plus 2%. The aggregate loan amount totaled approximately $50,588 and was fully repaid as of December 31, 2008.

Scheduled principal payments on debt as of December 31, 2008 are as follows:

| | Total Debt (Including Related Parties) |
|---|---|
| December 31, 2009 | $25,670 |
| December 31, 2010 | 13,327 |
| December 31, 2011 | 14,109 |
| December 31, 2012 | 14,935 |
| December 31, 2013 | 81,269 |
| Thereafter | 203,438 |
| Total | $352,748 |

9. OPERATING PARTNERSHIP AND STOCKHOLDER DISTRIBUTIONS

Holders of the Company's common stock and O.P. Units are entitled to dividend distributions as determined and declared by the Company's Board of Directors. Under the Exchange Rights Agreement limited partners have the right to tender O.P. Units to the Company, and, at the Company's election, to receive common stock on a one-for-one basis at then-current market value, an equivalent amount of cash, or a combination of cash and common stock in exchange for the O.P. Units tendered, subject to the 9% overall ownership limit imposed on non-Berg Group stockholders under the Company's charter document, or the overall 20% Berg Group ownership limit, as the case may be. O.P. Unit holders are entitled to vote when their O.P. Units are converted to shares of the Company's common stock. Once in each 12-month period beginning each December 29, the limited partners, other than Carl E. Berg and Clyde J. Berg, may exercise a put right to sell their O.P. Units to the operating partnerships at a price equal to the average market price of the common stock for the 10-trading day period immediately preceding the date of tender. Upon any exercise of the put rights, the Company will have the opportunity for a period of 15 days to elect to fund the purchase of the O.P. Units and purchase additional general partner interests in the operating partnerships for cash, unless the purchase price exceeds $1 million in the aggregate for all tendering limited partners, in which case, the operating partnerships or the Company will be entitled, but not required, to reduce proportionally the number of O.P. Units to be acquired from each tendering limited partner so that the total purchase price is not more than $1 million.

MISSION WEST PROPERTIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, CONTINUED
(Dollars in thousands, except per share data)

During 2008, the Company, as general partner of the operating partnerships, declared quarterly dividends/distributions aggregating $0.80 per common share and O.P. Unit for total dividends/distributions of approximately $84,204, including $21,055 payable in January 2009. Total distributions attributable to O.P. Units owned by various members of the Berg Group were approximately $63,040.

During 2007, the Company, as general partner of the operating partnerships, declared quarterly dividends/distributions aggregating $0.64 per common share and O.P. Unit for total dividends/distributions of approximately $67,152, including $16,832 payable in January 2008. Total distributions attributable to O.P. Units owned by various members of the Berg Group were approximately $50,271.

During 2006, the Company, as general partner of the operating partnerships, declared quarterly dividends/distributions aggregating $0.64 per common share and O.P. Unit for total dividends/distributions of approximately $66,948, including $16,745 payable in January 2007. Total distributions attributable to O.P. Units owned by various members of the Berg Group were approximately $50,151.

10. EQUITY-BASED COMPENSATION AND RETIREMENT INVESTMENT PLANS

The Company's 1997 Stock Option Plan ("1997 Plan") was approved by the Company's stockholders on November 10, 1997. On November 24, 2004, the 2004 Equity Incentive Plan ("2004 Plan") was approved by the Company's stockholders and replaced the 1997 Plan. The Company's board of directors approved the 2004 Plan in September 2004. No further options are available or will be granted under the 1997 Plan. In replacing the 1997 Plan, the 2004 Plan:

- transferred up to 3,991,089 remaining shares available for issuance under the Company's 1997 Plan and terminated the 1997 Plan for any new grants;
- transferred up to an additional 767,000 shares subject to outstanding options under the 1997 Plan if they expire without being exercised, of which 272,000 shares had been transferred as of December 31, 2008; and
- includes the ability to grant restricted stock, restricted stock units, performance units, dividend equivalent rights, and other stock-based compensation, including O.P. Units of the Operating Partnerships, as well as incentive and non-statutory stock options.

The 2004 Plan was adopted so that the Company may attract and retain the high quality employees, directors and consultants necessary to build the Company's infrastructure and to provide ongoing incentives to the Company's employees in the form of options to purchase the Company's common stock by enabling them to participate in the Company's success.

The 2004 Plan provides for the granting to employees, including officers (whether or not they are directors) of "incentive stock options" within the meaning of Section 422 of the Code, and for the granting of non-statutory options to employees, directors and consultants of the Company. 1,180,535 and 2,843,089 shares of common stock were available for future option or award grants under the 2004 Plan as of December 31, 2008 and 2007, respectively.

In January 2008, stock options to purchase 1,025,000 shares of common stock were granted to employees, non-employee directors and consultants. The options vest monthly for 48 months from date of grant, subject to continued employment or

other service to the Company. Each option grant has a term of six years from the date of grant subject to earlier termination in certain events related to termination of employment or service. The options were granted at an exercise price of $9.51 per share. The estimated fair value of the options granted was $0.57 per share on the date of grant using the Black-Scholes option pricing model with the following assumptions: dividend yield of 8.41%, volatility of 20.43%, risk free rates of 3.45% and an expected life of six years. All options were granted at fair market value on the date of grant.

In July 2008, stock options to purchase 52,500 shares of common stock were granted to an employee and a non-employee director. The options vest monthly for 48 months from date of grant, subject to continued employment or other service to the Company. Each option grant has a term of six years from the date of grant subject to earlier termination in certain events related to termination of employment or service. The options were granted at an exercise price of $11.36 per share. The estimated fair value of the options granted was $0.99 per share on the date of grant using the Black-Scholes option pricing model with the following assumptions: dividend yield of 7.04%, volatility of 22.07%, risk free rates of 3.20% and an expected life of six years. All options were granted at fair market value on the date of grant.

In November 2008, stock options to purchase 705,000 shares of common stock were granted to employees, non-employee directors and consultants. The options vest monthly ranging from 36-48 months from date of grant, subject to continued employment or other





service to the Company. Each option grant has a term of six years from the date of grant subject to earlier termination in certain events related to termination of employment or service. The options were granted at an exercise price of $6.14 per share. The estimated fair value of the options granted was $0.12 per share on the date of grant using the Black-Scholes option pricing model with the following assumptions: dividend yield of 13.03%, volatility of 22.39%, risk free rates of 2.08% and an expected life of six years. All options were granted at fair market value on the date of grant.

In 2007, stock options to purchase 710,000 shares of common stock were granted to employees, non-employee directors and consultants, which options vest monthly for 48 months from date of grant, subject to continued employment or other service to the Company. Each option grant has a term of six years from the date of grant subject to earlier termination in certain events related to termination of employment or service. The options were granted at an exercise price of $12.09 per share. The estimated fair value of the options was $1.45 per share on the date of grant using the Black-Scholes option pricing model with the following assumptions: dividend yield of 5.29%, volatility of 18.94%, risk free rates of 4.53% and an expected life of six years. All options were granted at fair market value on the date of grant.

No options were granted in year 2006.

The remaining contractual lives of unexercised option grants range from April 2009 to November 2014.

The following table shows the activity and detail for the 2004 Plan for each of the three years in the period ended December 31, 2008.

| | Options Outstanding | Weighted Average Exercise Price Per Share |
|---|---|---|
| Balance, December 31, 2005 | 1,422,000 | $10.83 |
| Options exercised | (112,900) | $8.76 |
| Options forfeited | (272,000) | $13.00 |
| Balance, December 31, 2006 | 1,037,100 | $10.48 |
| Options granted | 710,000 | $12.09 |
| Balance, December 31, 2007 | 1,747,100 | $11.13 |
| Options granted | 1,782,500 | $8.23 |
| Options exercised | (77,154) | $9.96 |
| Options forfeited | (119,946) | $10.81 |
| Balance, December 31, 2008 | 3,332,500 | $9.62 |
| Available for grant at December 31, 2008 | 1,180,535 | |
| Available for grant at December 31, 2007 | 2,843,089 | |

The following table summarizes information regarding options outstanding for the 2004 Plan at December 31, 2008:

| | Options Outstanding | | | Options Exercisable | | Op |
|---|---|---|---|---|---|---|
| Range of Exercise Prices | Options | Weighted Average Remaining Contractual Life in Years | Weighted Average Exercise Price | Options | Weighted Average Exercise Price | |
| $6.14 | 705,000 | 5.92 | $6.14 | 148,438 | $6.14 | |
| $9.51 | 960,000 | 5.00 | $9.51 | 265,833 | $9.51 | |
| $10.00 | 590,000 | 2.33 | $10.00 | 590,000 | $10.00 | |
| $11.33 | 375,000 | 0.33 | $11.33 | 375,000 | $11.33 | |
| $11.36 | 52,500 | 5.50 | $11.36 | 5,469 | $11.36 | |
| $12.09 | 650,000 | 4.00 | $12.09 | 311,458 | $12.09 | |
| $6.14 to $12.09 | 3,332,500 | 4.01 | $9.62 | 1,696,198 | $10.27 | |

None of the options granted are contingent upon the attainment of performance goals or subject to other restrictions. As of December 31, 2008 and 2007, "in-the-money" outstanding options to purchase 148,438 and zero shares of common stock, respectively, were exercisable.

The 2004 Plan allows the Company to grant to employees and directors a wider range of awards than is permitted under the 1997 Plan, including restricted stock, stock grants, restricted stock units, performance units, other stock-based compensation, including O.P. Units exchangeable for shares of common stock, and dividend equivalent rights, which will help the Company achieve its

goal of attracting,





retaining and motivating its personnel which is necessary to build the Company's infrastructure, achieve the Company's business goals and enhance stockholder value. No options or awards may be granted under the 2004 Plan after November 24, 2014.

Awards and options granted under the 2004 Plan may be granted to any employees, non-employee directors or consultants of the Company and any corporation or other entity affiliated with the Company, including the Operating Partnerships. Only employees of the Company or a corporate subsidiary may receive incentive stock options. Options can be granted to non-employee directors and consultants of the Company and to employees of the Company or a corporate subsidiary. No individual may receive in any one calendar year options for more than 500,000 of the total number of shares of stock.

The options generally are granted at the fair market value of the Company's common shares at the date of grant, vest over a four-to-six year period, are exercisable upon vesting and expire six-to-eight years from the date of grant. The exercise price for all incentive stock options under the 2004 Plan shall not be less than the fair market value of the underlying common shares at the time the option was granted.

Under the 2004 Plan, each non-employee member of the board of directors who became or becomes a member of the board of the directors after November 24, 2004, the date on which the Plan was approved by the Company's stockholders, will receive automatically a grant of an option to purchase 50,000 shares of common stock at an exercise price equal to 100% of the fair market value of the common stock at the date of grant of such option. Such options become exercisable cumulatively with respect to 1/48th of the underlying shares on the first day of each month following the date of grant. Generally, the options must be exercised while the optionee remains a director. In addition, the board of directors may authorize annual option grants or awards to non-employee directors in the board's discretion as long as the number of shares or equivalent number of underlying shares of common stock in the case of certain awards, does not exceed 50,000 per year. A disinterested majority of the board also may authorize additional options and awards to a director serving as a Committee chair or providing other extraordinary service to the Board. The 2004 Plan further provides that upon an acquisition of the Company in which more than 50% of the total voting power of the Company's outstanding securities is transferred to the acquirer or acquiring parties, options and awards held by non-employee directors will vest in full and become exercisable prior to their expiration.

The board of directors may terminate the 2004 Plan at any earlier time or make modifications of the 2004 Plan as it deems advisable. Awards and options granted at any time during the term of the 2004 Plan will not expire solely because of the termination of the 2004 Plan, and no amendment or modification of the 2004 Plan shall affect the terms of any outstanding award unless the board expressly provides otherwise. Termination or amendment of the 2004 Plan may not adversely affect the rights of the recipient of an award without his or her consent. The Compensation Committee of the Board of Directors may amend the terms of any option or award previously granted, but such amendment may not impair the rights of the recipient without his or her consent.

A total of 4,263,089 shares of common stock are reserved for issuance under the 2004 Plan, in addition to 375,000 shares subject to outstanding options under

the 1997 Plan if they expire unexercised. At no time may the number of shares issued pursuant to or subject to outstanding awards granted under the 2004 Plan exceed this number, subject to the provisions for increase and adjustment set forth in the 2004 Plan. If any option or award expires, terminates or is cancelled without being exercised in full, or any other award is forfeited, the shares forfeited or not purchased will be available for future grant of awards.

The Company has adopted an employee investment plan (the "Plan"), under Section 401(k) of the Internal Revenue Code. Employees who are at least 21 years old and who have completed six months of eligibility service may become participants in the Plan. Each participant may make contributions to the Plan through salary deferrals in amounts of at least 1% to a maximum of 15% of the participant's compensation, subject to certain limitations imposed by the Internal Revenue Code. The Company contributes an amount up to 15% of the participant's compensation, based upon management's discretion. A participant's contribution to the Plan is 100% vested and non-forfeitable. A participant will become vested in 100% of the Company's contributions after two years of eligible service. For the years ended December 31, 2008, 2007 and 2006, the Company recognized approximately $118, $123 and $103 of expense for employer contributions made in connection with this Plan, respectively.

## 11. NET INCOME PER SHARE

Basic net income per share is computed by dividing net income by the weighted-average number of common shares outstanding for the period. Diluted net income per share is computed by dividing net income by the sum of weighted-average number of common shares outstanding for the period plus the assumed exercise of all dilutive securities.

The following table provides a reconciliation of net income to common stockholders and the number of shares used in the computations of "basic" net income per share to common stockholders and "diluted" net income per share to common stockholders.





| | Year Ended December 31, 2008 | Year Ende December 31, |
|---|---|---|
| | (dollars in thousands, exc | |
| Numerator: | | |
| Income from continuing operations | $10,134 | $17,75 |
| Income from discontinued operations | - | 1,13 |
| Net income to common stockholders | $10,134 | $18,88 |
| Denominator: | | |
| Weighted average shares of common stock (basic) | 19,714,414 | 19,627,23 |
| Effect of dilutive securities: | | |
| Incremental shares from assumed stock options exercise | 281,935 | 227,17 |
| Weighted average shares of common stock (diluted) | 19,996,349 | 19,854,41 |

| | | |
|---|---|---|
| Per share data: | | |
| Basic net income per share: | | |
| Net income to common stockholders before discontinued operations | $0.51 | $0.9 |
| Discontinued operations | - | 0.0 |
| Net income to common stockholders | $0.51 | $0.9 |
| Diluted net income per share: | | |
| Net income to common stockholders before discontinued operations | $0.51 | $0.8 |
| Discontinued operations | - | 0.0 |
| Net income to common stockholders | $0.51 | $0.9 |

Outstanding options to purchase 2,627,500 shares in 2008 were excluded from the computation of diluted net income per share under the treasury stock method because the option exercise price was greater than the weighted average exercise price of the Company's common stock during the period. The outstanding O.P. Units have been excluded from the diluted net income per share calculation as there would be no effect on the diluted net income per share since the minority interests' share of income would also be added back to net income. O.P. Units outstanding at December 31, 2008, 2007 and 2006 were 85,526,965, 85,533,935 and 85,206,199, respectively.

12. OTHER INCOME

Other income from continuing operations was approximately $4,223, $61,982 and $18,222 for the years ended December 31, 2008, 2007 and 2006, respectively. For the year ended December 31, 2008, termination fees, management fee income and miscellaneous income accounted for approximately $3,007, $967 and $249, respectively, of other income. For the year ended December 31, 2007, termination fees, prior tenant bankruptcy settlements, management fee income, security deposit forfeitures and miscellaneous income accounted for approximately $57,515, $300, $982, $1,799 and $1,386, respectively, of other income. For the year ended December 31, 2006, termination fees, prior tenant bankruptcy settlements, management fee income, security deposit forfeitures and miscellaneous income accounted for approximately $16,068, $183, $1,070, $104 and $797, respectively, of other income. Management fee is paid by the tenant to the landlord for the administration and supervision of the property.

13. RELATED PARTY TRANSACTIONS

As of December 31, 2008 and 2007, the Berg Group owned 77,902,384 O.P. Units of the total 85,526,965 and 85,533,935 O.P. Units issued and outstanding, respectively. The Berg Group's interest in the Company represents 74.0% and 74.1% of the Company as of December 31, 2008 and 2007, respectively, assuming conversion of the O.P. Units into common shares of the Company.

The Company periodically acquires non-leased properties, which include land, the building shell and base building improvements, from the Berg Group under the Berg Group Land Holdings Options Agreement. These acquisitions from the Berg Group are made for properties where the Company has previously identified a tenant, and in conjunction with the acquisition, the Company executes a lease agreement with the tenant. In many of the acquisitions from the Berg Group, lease commissions relating to these leasing activities conducted by the Company are paid by the Berg Group and reimbursed by the Company in connection with the acquisition. These lease commissions are recorded separately in "Other assets" on the Company's consolidated balance sheets.

PROPERTY ACQUISITION
In January 2008, the Company acquired an approximately 111,500 rentable square foot newly constructed R&D building located at 5981 Optical Court in San Jose, California from the Berg Group under the Berg Land Holdings Option Agreement. The total acquisition price for this property was approximately $19,068. The Company acquired this property by issuing a short-term note





payable to the Berg Group, which was fully repaid in July 2008. The transaction was approved by the Independent Directors Committee of the Company's Board of Directors.

In September 2007, the Company acquired an approximately 98,500 rentable square foot newly constructed R&D building located at 5845 Hellyer Avenue in San Jose, California from the Berg Group under the Berg Land Holdings Option Agreement. The total acquisition price for this property was approximately $10,903. The Company acquired this property by issuing 548,236 O.P. Units and paying $4,300 in cash to the selling members of the Berg Group. The transaction was approved by the Independent Directors Committee of the Company's Board of Directors.

DEBT WITH THE BERG GROUP
As of December 31, 2008 and 2007, debt in the amount of approximately $8,761 and $9,224, respectively, was due the Berg Group under a mortgage note established May 15, 2000 in connection with the acquisition of a 50% interest in Hellyer Avenue Limited Partnership, the obligor under the mortgage note. The mortgage note bears interest at 7.65%, and is due in ten years with principal payments amortized over 20 years. In the fourth quarter of 2008, the Company and the Berg Group agreed to extend the loan maturity date to June 2013. Interest expense incurred in connection with the Berg Group mortgage note was approximately $690, $724 and $755 for the years ended December 31, 2008, 2007 and 2006, respectively.

During 2008, the Company issued multiple short-term notes payable to the Berg Group in connection with a property acquisition, quarterly dividend distributions and a cash loan. The interest rates on these notes were LIBOR plus 2%. The aggregate loan amount totaled approximately $50,588 and was fully repaid as of December 31, 2008. For the year ended December 31, 2008, interest expense incurred in connection with those short-term notes payable was approximately $643.

TRANSFER OF INTEREST TO BERG GROUP IN CONSOLIDATED JOINT VENTURE
In July 2000, the Hellyer Avenue Limited Partnership ("Hellyer LP") was formally organized as a California limited partnership between Mission West Properties, L.P. ("MWP"), of which the Company as the managing general partner, and Republic Properties Corporation ("RPC"), an unaffiliated third party, as general partner and limited partners. MWP was designated as the managing general partner of Hellyer LP. For a 50% ownership interest in Hellyer LP, RPC agreed to cause Stellex Microwave Systems, Inc. ("Stellex") to provide a 15-year lease on approximately 160,000 square foot R&D buildings to be constructed by Berg & Berg Enterprises, Inc. ("BBE") on land owned by another Berg Group member.

As part of the transaction, MWP acquired the underlying land pursuant to the Berg Land Holdings Option Agreement for a price of $5.7 million by issuing 659,223 O.P. Units to the Berg Group entity that owned the property. Further, under the terms of the Hellyer LP partnership agreement MWP then contributed the land to the partnership at an agreed value of $9.6 million, which amount was to

be amortized and paid to MWP in the form of income and cash flow preferences. The transaction was reviewed and approved by the Independent Directors Committee of the Company's Board of Directors.

In connection with the transaction, BBE built and paid for all improvements on the land. The total cost of the R&D buildings, exclusive of specified tenant improvements obligations, was approximately $11.4 million. Hellyer LP issued a note for the amount of those construction costs to BBE, which note was secured by the buildings.

Because RPC's interest in Hellyer LP was attributable solely to its commitment to obtain Stellex as a tenant for the property, the partnership agreement provided that if a payment default occurred within the first five years of the Stellex lease, RPC would lose 100% of its interest in the partnership, and if a payment default occurred during the second five year period under the lease, RPC would lose 50% of its interest in Hellyer LP.

Pursuant to RPC's commitment to Hellyer LP, Stellex executed a lease agreement obligating Stellex, among other things, to pay monthly rent starting at $1.60 per square foot on a triple net basis for 15 years and to reimburse BBE for the tenant improvement obligations, which ultimately totaled approximately $10.5 million.

Under the lease terms, Stellex was obligated to reimburse BBE in full for the tenant improvement costs no later than August 25, 2000. Several days before the due date, representatives of Stellex met with representatives of MWP and informed them that Stellex could not pay the balance due BBE. Stellex requested MWP immediately to draw down the letter of credit as a result of default on the tenant improvement payment required under the lease.

On September 1, 2000, MWP, as the general partner of Hellyer LP, ceased all allocations of income and cash flow to RPC and exercised the right under the partnership agreement to cancel RPC's entire interest in the partnership. Following discussions with and approval by the Independent Directors Committee, the Company authorized the transfer of RPC's interest in Hellyer LP to BBE.





Under the Berg Land Holdings Option Agreement and the Acquisition Agreement dated as of May 14, 1998, the Independent Directors Committee of the Board of Directors had the right, but not the obligation, to reacquire on behalf of the Company the property interest and the related distributions related to the property interest at any time. The transfer was effective as of September 1, 2000.

In January 2002, Stellex was acquired through its bankruptcy proceeding by a division of Tyco Corporation. In connection with the acquisition of Stellex, the purchaser assumed the lease with Hellyer LP, agreed to comply with all terms of lease and reimbursed BBE for the tenant improvements, as required under the lease agreement and the Bankruptcy Court order.

Since the inception of Hellyer LP, the Company has accounted for the properties owned by the partnership on a consolidated basis, with reductions for the minority interest held by the minority partner (first RPC and then BBE). In each period, the Company has accrued amounts payable by Hellyer LP to the minority interest partner, including BBE prior to payment. BBE's share of earnings allocated to its 50% minority interest was approximately $0.8 million, $0.7 million and $0.8 million in 2008, 2007 and 2006, respectively. As of December

31, 2008, accumulated cash flow distributions from Hellyer LP totaling approximately $5.3 million were accrued and distributed to BBE. If the Company's litigation with RPC (as described under Note 16 below) is ultimately decided in RPC's favor, the Company anticipates that BBE may be required to return RPC's former interest in Hellyer LP and all prior distributions to RPC. As a result of this uncertainty, in October 2003, the Company recorded such distributions as an account receivable from BBE, which is included in "Other assets" on the Company's consolidated balance sheets, with an offsetting account payable to BBE.

The Independent Directors Committee of the Board of Directors has exercised the right to acquire on behalf of the Company the former RPC interest and related distributions from BBE under the terms of the Berg Land Holdings Option Agreement between the Company and the Berg Group if the litigation is ultimately decided in favor of the Company.

ACQUISITION OF CARL E. BERG'S INTEREST IN UNCONSOLIDATED JOINT VENTURE

In July 1999, TBI, an unrelated party, advised Carl E. Berg that TBI had an option to purchase approximately 78.89 acres of unimproved land zoned for R&D development in Morgan Hill at $2.50 per square foot that would expire in approximately six months. TBI offered Mr. Berg a 50% interest in the development of this land if Mr. Berg provided 100% financing for the land at 0% interest for three years. Mr. Berg advised TBI of his obligation to offer all R&D development opportunities on the West Coast to the Company and further advised TBI that the Company's Independent Directors Committee must approve the acquisition of any properties and that the Company's policy was only to acquire properties that are leased pursuant to the Berg Land Holdings Option Agreement. The development joint venture between TBI and the Berg Group proceeded on that basis. Building construction was financed through loans facilitated by the Berg Group. In early 2003, TBI formed TBI-MWP, a new limited partnership, to own all the leased buildings. The Berg Group offered its 50% non-controlling limited partnership interest in TBI-MWP to the Company at cost plus an annual interest rate of 7% on the funds advanced by the Berg Group which amounted to $1.8 million. The Independent Directors Committee and the Berg Group agreed to use a 7% interest rate instead of the rate and fees specified in the Berg Land Holdings Option Agreement because the transaction differed from the standard build-to-suit development specified under that agreement. TBI-MWP owned four fully leased buildings totaling approximately 593,000 rentable square feet. The buildings were subject to mortgage loans totaling approximately $53.6 million. The Independent Directors Committee approved the Company's acquisition of the Berg Group's 50% interest in the joint venture effective January 1, 2003. The development joint venture between the Berg Group and TBI retained two vacant shell R&D buildings and five unimproved lots. In April 2003, Comcast, Inc. offered to purchase one of the vacant buildings and two acres of adjoining land from the development joint venture for net proceeds of $2.8 million, after debt repayment. Prior to sale of the property, TBI-MWP acquired this property at no cost under the terms of the Berg Land Holdings Option Agreement, and the Company received a net distribution of $1.4 million from the sale. The transaction was approved by the Independent Directors Committee. The Berg Group continues to own a 50% interest in the remaining vacant building and five unimproved lots. In July 2006, TBI-MWP sold one R&D property with approximately 126,400 rentable square feet for approximately $8.5 million. The total gain on the sale was approximately $0.9 million of which $0.45 million was the Company's share. In November 2008, TBI-MWP sold two R&D properties with approximately 311,200 rentable square feet for approximately $65 million. The total gain on the sale was approximately $40.9 million of which approximately $20.5 million was the Company's share. TBI-MWP currently owns one fully leased R&D building totaling approximately 155,500 rentable square feet.

BERG CONTROLLED ENTITIES HAVE FINANCIAL INTERESTS IN CERTAIN TENANTS THAT LEASE SPACE FROM THE COMPANY

During the years ended December 31, 2008, 2007 and 2006, Carl E. Berg or

entities controlled by Mr. Berg held financial interests in several companies that lease space from the operating partnerships, which include companies where Mr. Berg has a greater than 10% ownership interest. These related party tenants contributed approximately $1,218, $1,227 and $1,875 in rental revenue in 2008, 2007 and 2006, respectively. Under the Company's Charter, bylaws and agreements with the Berg Group, the individual members of the Berg Group are prohibited from acquiring shares of the Company's common stock if such acquisition would result in their beneficial





ownership percentage of the Company's common stock causing the Company to violate any REIT qualification requirement, and currently their share ownership is below a level at which rent from related party tenants would be excluded in determining compliance with REIT qualification tests.

BERG GROUP COMMITMENT TO COMPLETE FUTURE IMPROVEMENTS AND BUILDING IN CONNECTION WITH CERTAIN ACQUISITIONS FROM THE BERG GROUP UNDER THE BERG LAND HOLDINGS Option Agreement In connection with the Company's 2002 acquisition of 5345 Hellyer Avenue in San Jose, California the Berg Group made an approximately $2,529 commitment to the Company to complete certain tenant improvements. The Company recorded this portion of its purchase consideration paid to the Berg Group in "Other assets" on its consolidated balance sheets. The Berg Group satisfied this commitment in late 2008. The Company reclassified approximately $2,529 from "Other assets" to tenant improvements and will start depreciation of the asset over the remaining lease term effective January 1, 2009.

The Berg Group has an approximately $7,494 commitment to complete an approximately 75,000 to 90,000 square foot building in connection with the Company's 2001 acquisition of 245 Caspian Drive in Sunnyvale, California which is comprised of approximately three acres of unimproved land. The Company recorded this portion of its purchase consideration paid to the Berg Group in "Other assets" on its consolidated balance sheets. The Berg Group plans to satisfy this commitment to construct a building when requested by the Company following the approval of the Independent Directors Committee.

LAND LEASE RENT REIMBURSEMENT TO CARL E. BERG
In 2007, one tenant was leasing four R&D buildings from the Company and was also leasing raw land from Carl E. Berg. Total rent from the tenant was paid directly to the Company, which included the land rent. The Company reimbursed Carl E. Berg $85 per month for the land rent. That tenant terminated its lease obligations with the Company effective July 1, 2007, and the Company acquired the land in connection with a completed 98,500 rentable square feet shell building (see "Property Acquisitions" above under Note 6) and after July 1, 2007 no further rent was paid to Carl E. Berg.

LEASING AND OVERHEAD REIMBURSEMENTS PROVIDED BY BERG CONTROLLED ENTITY
The Company currently leases office space owned by Berg & Berg Enterprises for the Company's headquarters. Rental amount and overhead reimbursements paid to Berg & Berg Enterprises, Inc. were approximately $114, $95 and $90 for the years ended December 31, 2008, 2007 and 2006.

14. FUTURE MINIMUM RENTS

The Company, through the operating partnerships, owns interests in 111 R&D properties that are leased to tenants under net operating leases with initial terms extending to the year 2020, and are typically subject to fixed increases. Generally, the leases grant tenants renewal options. Future minimum rentals

under non-cancelable operating leases as of December 31, 2008, excluding tenant reimbursements of expenses, are as follows:

| Year | Minimum Rent |
|---|---|
| | (dollars in thousands) |
| 2009 | $ 81,905 |
| 2010 | 80,862 |
| 2011 | 71,499 |
| 2012 | 55,548 |
| 2013 | 45,028 |
| Thereafter | 71,800 |
| Total | $406,642 |

15. SUPPLEMENTAL CASH FLOW INFORMATION

Cash paid for interest was approximately $20,712, $20,617 and $20,137 for the years ended December 31, 2008, 2007 and 2006, respectively.

In connection with a property acquisition from the Berg Group, the Company issued a short-term note payable for approximately $19,068 for the year ended December 31, 2008. The Company fully repaid the balance as of December 31, 2008.

In connection with a property acquisition from the Berg Group, the Company issued 548,236 O.P. Units for a total acquisition value of approximately $6,603 for the year ended December 31, 2007.





Amounts of approximately $59,888, $50,189 and $50,166 were paid to the Berg Group for distributions declared to O.P. Unit holders during the years ended December 31, 2008, 2007 and 2006, respectively.

For the years ended December 31, 2008, 2007 and 2006, 6,970, 220,500 and 881,896 O.P. Units were exchanged for 6,970, 220,500 and 881,896 shares of the Company's common stock, respectively, under the terms of the Exchange Rights Agreement among the Company and all limited partners of the operating partnerships. These non-cash transactions were valued at approximately $66, $2,855 and $10,280 for the years ended December 31, 2008, 2007 and 2006, respectively, based on the market closing price on the day of the transactions.

16. COMMITMENTS AND CONTINGENCIES

The Company and the operating partnerships, from time to time, are parties to litigation arising out of the normal course of business. The Company is currently involved in the following legal proceedings, and does not believe the ultimate outcome of any of these proceedings will have a material adverse effect on its financial condition or operating results.

Mission West Properties, L.P. v. Republic Properties Corporation, et al. Santa Clara County Superior Court, Case No. CV 796249. In February 2001, while a related case in Maryland was pending, the Company filed a suit against Republic

Properties Corporation ("RPC") in the Superior Court of the State of California for the County of Santa Clara, Case No. CV 796249. The case was stayed pending resolution of the Maryland case, and the Company dismissed its suit on March 4, 2005. In April 2005, RPC submitted a motion asking the Superior Court to reinstate the case, which the Court granted on May 25, 2005. In April 2006, the Maryland case was dismissed by the highest court in Maryland for lack of personal jurisdiction. On July 5, 2006, RPC filed a cross-complaint in the case seeking partnership distributions to which the Company demurred. The Court sustained the Company's demurrer with leave to amend. Subsequently, RPC filed an amended complaint and the Company submitted another demurrer seeking dismissal of the claims on statute of limitations grounds. On February 20, 2007, the Court overruled the Company's demurrer. The Company sought a writ from the California State Court of Appeal for the Sixth District to direct the lower court to reverse its decision, but the petition for the writ was denied. In April 2008, the Company filed a motion for summary judgment in the California Superior Court which was denied. In October 2008, a motion filed by RPC for summary judgment in the California Superior Court was denied. A trial in the California Superior Court commenced in February 2009.

GUARANTEES

Under its articles of incorporation and bylaws, the Company has agreed to indemnify its officers and directors for certain events or occurrences arising as a result of the officer or director's serving in such capacity. The maximum potential amount of future payments the Company could be required to make under these indemnification agreements is unlimited. The Company believes the estimated fair value of these indemnification agreements is minimal and has recorded no liabilities for these agreements as of December 31, 2008.

The Company also enters into indemnification provisions under its agreements with other companies in its ordinary course of business, typically with lenders, joint venture partners, contractors, and tenants. Under these provisions the Company typically agrees to indemnify and hold harmless the indemnified party for losses suffered or incurred by the indemnified party as a result of certain kinds of activities or inactions of the Company. These indemnification provisions generally survive termination of the underlying agreement. The maximum potential amount of future payments the Company could be required to make under these indemnification provisions is unlimited. The Company has not incurred material costs to defend lawsuits or settle claims related to these indemnification agreements. As a result, the Company believes the estimated fair value of these agreements is minimal. Accordingly, the Company has recorded no liabilities for these agreements as of December 31, 2008.

SEISMIC ACTIVITY

The Company's properties are located in an active seismic area of Silicon Valley. Insurance policies currently maintained by the Company do not cover seismic activity, although they do cover losses from fires after an earthquake.

ENVIRONMENTAL ISSUES

The environmental investigations that have been conducted on the Company's properties have not revealed any environmental liability that it believes would have a material adverse effect on its financial condition, results of operations and assets, and the Company is not aware of any such liability. Nonetheless, it is possible that there are material environmental liabilities of which the Company is unaware. The Company cannot assure you that future laws, ordinances, or regulations will not impose any material environmental liability, or that the current environmental condition of the properties has not been, or will not be, affected by tenants and occupants of the properties, by the condition of properties in the vicinity of the properties, or by third parties unrelated to the Company.

MISSION WEST PROPERTIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, CONTINUED
(Dollars in thousands, except per share data)

ASSET DISPOSITION SUBJECT TO CERTAIN CONDITIONS
The Company has entered into a sales agreement with unrelated parties subject to numerous material conditions, including but not limited to re-zoning of the property and negotiating certain agreements with the local municipality acceptable to the buyer. As a result of the conditions agreed to by the Company and the respective buyers, these assets do not meet the criteria set forth in SFAS 144 to be classified as assets held for sale. The following summarizes the assets for which the Company has executed a sales contract as of December 31, 2008 that are subject to material conditions as previously described:

| Property | Number of Buildings | Rentable Square Feet | Acres |
|---|---|---|---|
| McCandless Drive<br>Milpitas, California | 8 | 427,000 | 23.03 |

17. REAL ESTATE ASSET HELD FOR SALE AND DISCONTINUED OPERATIONS

The Company follows SFAS 144, which addresses financial accounting and reporting for the impairment and disposal of long lived assets. In general, income or loss attributable to the operations and sale of property and the operations related to property held for sale are classified as discontinued operations in the consolidated statements of operations. Prior period consolidated statements of operations presented in this report have been reclassified to reflect the income or loss related to properties that were held for sale or sold and presented as discontinued operations for the years ended December 31, 2008, 2007 and 2006. Additionally, all periods presented in this report will likely require further reclassification in future periods if additional properties are held for sale or property sales occur.

As of December 31, 2008, there were no properties under contract to be sold or otherwise disposed of which would qualify as assets held for sale.

In 2007, the Company sold two R&D properties for a total sales price of approximately $16,043 resulting in a net gain of approximately $6,529. In 2006, the Company sold three R&D properties for a total sales price of approximately $43,271 resulting in a net gain of approximately $18,102. Results of operations for these properties for the years ended December 31, 2007 and 2006 are as follows:

| | Year Ended December 31, | |
|---|---|---|
| | 2007 | 2006 |
| | (dollars in thousands) | |
| Revenues: | | |
| Rental revenue from real estate | $389 | $2,271 |
| Tenant reimbursements | 83 | 317 |
| Other income | 1 | 291 |

| | | |
|---|---|---|
| Total revenues | 473 | 2,879 |
| Expenses: | | |
| Property operating, maintenance and real estate taxes | 233 | 683 |
| Depreciation of real estate | 148 | 694 |
| Total expenses | 381 | 1,377 |
| Operating income | 92 | 1,502 |
| Other income (expenses): | | |
| Interest | (1) | (1) |
| Income from discontinued operations | 91 | 1,501 |
| Gain from disposal of discontinued operations | 6,529 | 18,102 |
| Minority interests in earnings from discontinued operations | (5,489) | (16,431) |
| Income from discontinued operations | $1,131 | $3,172 |

For the years ended December 31, 2007 and 2006, income from discontinued operations included results of operations from two R&D properties sold in 2007 and three R&D properties sold in 2006.





18. ACQUISITION-RELATED INTANGIBLE ASSETS

In February 2008, the Company acquired a fully leased office/R&D building at 2904 Orchard Parkway in San Jose, California for approximately $16,696 from an unrelated party. The purchase price was allocated to long-lived assets and the value of an in-place lease as follows:

| | |
|---|---|
| Land | $4,704 |
| Buildings and improvements | 10,871 |
| In-place lease | 1,121 |
| Total cash purchase price | $16,696 |

The result of operations for this property acquisition has been included in the Company's consolidated statements of operations since the date of acquisition. The intangible assets are being amortized over the applicable remaining lease term. Amortization expense related to in-place leases of approximately $600, $2,153 and $1,613 was recorded for the years ended December 31, 2008, 2007 and 2006, respectively.

Details of real estate related intangible assets at December 31, 2008 and 2007 are as follows:

| | December 31, | |
|---|---|---|
| | 2008 | 2007 |
| | (dollars in thousands) | |
| Amortizable intangible assets: | | |
| In-place leases | $3,240 | $2,119 |
| Accumulated amortization | (1,341) | (741) |
| Net real estate related intangible assets | $1,899 | $1,378 |

The estimated aggregate amortization expense for the real estate related intangible assets for each of the five succeeding fiscal years is as follows:

| Year | Estimated In-place Lease Amortization (expense) |
|---|---|
| | (dollars in thousands) |
| 2009 | $637 |
| 2010 | 637 |
| 2011 | 363 |
| 2012 | 224 |
| 2013 | 38 |
| Total | $1,899 |

19. FAIR VALUE

The only financial asset or liability recorded at fair value in the Company's consolidated financial statements is the marketable securities. The Company determined the fair value for the marketable securities using quoted prices in active markets for identical securities (Level 1 - see Note 2 under New Accounting Pronouncements). As of December 31, 2008, the fair value of the marketable securities totaled approximately $3,368 and the cost thereof was approximately $3,646. The marketable securities are adjusted to fair value at the end of each accounting period, with the corresponding losses and gains recorded in unrealized losses or gains from investment. For the year ended December 31, 2008, the Company recorded net unrealized losses of approximately $278 related to the decrease in fair value of the marketable securities, which was reported in unrealized loss from investment in the Company's consolidated statement of operations.

(Dollars in thousands, except per share data)

20. SUPPLEMENTAL FINANCIAL INFORMATION (Unaudited)

Quarterly financial information for the year ended December 31, 2008 (1) is as follows:

| | For the Three Months En | | |
|---|---|---|---|
| | March 31, | June 30, (Unaudited) | Septe |
| Rental revenue from continuing operations, net | $18,996 | $19,359 | $ |
| Operating income from continuing operations | $13,545 | $11,452 | $ |
| Income from continuing operations | $1,882 | $1,359 | |
| Net income to common stockholders | $1,882 | $1,359 | |
| Per share data: | | | |
| Basic net income per share | $0.10 | $0.07 | |
| Diluted net income per share | $0.10 | $0.07 | |
| Weighted average shares of common stock(basic) | 19,667,605 | 19,695,988 | 19,7 |
| Weighted average shares of common stock(diluted) | 19,667,605 | 19,902,304 | 19,7 |

Quarterly financial information for the year ended December 31, 2007 (1) is as follows:

| | For the Three Months En | | |
|---|---|---|---|
| | March 31, | June 30, (Unaudited) | Septem |
| Rental revenue from continuing operations, net | $17,111 | $21,148 | $ |
| Operating income from continuing operations | $21,235 | $14,402 | $ |
| Income from continuing operations (2) | $3,366 | $2,001 | $ |
| Income from discontinued operations (2) | $9 | $3 | |
| Net income to common stockholders | $3,375 | $2,004 | $ |
| Per share data: | | | |
| Basic net income per share | $0.17 | $0.10 | |
| Diluted net income per share | $0.17 | $0.10 | |
| Weighted average shares of common stock(basic) | 19,582,787 | 19,639,928 | 19,6 |
| Weighted average shares of common stock(diluted) | 19,889,453 | 20,020,596 | 19,8 |

(1) The summation of the quarterly financial data may not equal the annual number reported on the consolidated statements of operations due to rounding differences.

(2) The quarterly financial data may not equal previously reported results on the Company's quarterly reports on Form 10-Q due to reclassification of revenues and expenses to discontinued operations in accordance with SFAS 144.

21. SUBSEQUENT EVENTS

On January 7, 2009, one limited partner exchanged a total of 2,000,000 O.P. Units for 2,000,000 shares of the Company's common stock under the terms of the Exchange Rights Agreement among the Company and all limited partners of the

operating partnerships. Neither the Company nor the operating partnerships received any proceeds from the issuance of the common stock in exchange for O.P. Units.

On January 8, 2009, the Company paid dividends of $0.20 per share of common stock to all common stockholders of record as of December 31, 2008. On the same date, the operating partnerships paid a distribution of $0.20 per O.P. Unit to all holders of O.P. Units, with the exception of the Berg Group. Aggregate dividends and distributions amounted to approximately $21,055.

On January 8, 2009, a short-term note payable in the amount of approximately $10,760 was issued to the Berg Group in connection with the fourth quarter 2008 dividend distributions. The note payable bears interest at LIBOR plus 2% and was fully repaid in February 2009.



Report of Independent Registered Public Accounting Firm on Financial Statement Schedule

Board of Directors and Stockholders
Mission West Properties, Inc.
Cupertino, California

The audit referred to in our report dated March 13, 2009 relating to the consolidated financial statements of Mission West Properties, Inc., which is contained in Item 8 of this Form 10-K, included the audit of the financial statement schedule listed in the accompanying index as of December 31, 2008 and 2007. This financial statement schedule is the responsibility of the Company's management. Our responsibility is to express an opinion on this financial statement schedule based upon our audit.

In our opinion such financial statement schedule as of December 31, 2008 and 2007 presents fairly, in all material respects, the information set forth therein.

\S\ Burr, Pilger & Mayer, LLP

San Francisco, California
March 13, 2009



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MISSION WEST PROPERTIES, INC.
Schedule III
Real Estate and Accumulated Depreciation and Amortization
December 31, 2008
(dollars in thousands)

| Property Name | City | | December 31, 2008 Encumbrances | Initial Cost Land | Initial Cost Buildings and Improvements |
|---|---|---|---|---|---|
| 5300-5350 Hellyer Avenue | San Jose | C | $8,761 | $5,742 | $11,442 |
| 10401-10411 Bubb Road | Cupertino | A | | 633 | 3,078 |
| 45365 Northport Loop | Fremont | | | 2,447 | 5,711 |
| 45738 Northport Loop | Fremont | F | | 891 | 4,338 |
| 4050 Starboard Drive | Fremont | F | | 1,329 | 6,467 |
| 3501 W. Warren Ave/Fremont Blvd | Fremont | | | 1,866 | 9,082 |
| 48800 Milmont Blvd | Fremont | | | 1,013 | 4,932 |
| 4750 Patrick Henry Drive | Santa Clara | H | | 1,604 | 7,805 |
| 3520 Bassett Street | Santa Clara | D | | 1,104 | 5,371 |
| 3530 Bassett Street | Santa Clara | B,D | | 849 | 4,133 |
| 5850-5870 Hellyer Avenue | San Jose | | | 2,787 | 6,502 |
| 5750 Hellyer Avenue | San Jose | | | 3,266 | 3,354 |
| 800 Embedded Way | San Jose | K | | 1,794 | - |
| 5500 Hellyer Avenue | San Jose | F | | 4,735 | 12,485 |
| 5550 Hellyer Avenue | San Jose | F | | 3,261 | 3,478 |
| 5400 Hellyer Avenue | San Jose | | | 3,238 | 5,007 |
| 5325 Hellyer Avenue | San Jose | H | | 4,684 | 10,230 |
| 5345 Hellyer Avenue | San Jose | H | | 4,866 | 5,822 |
| 5905-5965 Silver Creek Valley Rd | San Jose | | | 8,437 | 17,316 |
| 5905-5965 Silver Creek Valley Rd | San Jose | | | 3,438 | 2,727 |
| 5845 Hellyer Avenue | San Jose | | | 6,090 | 5,029 |
| 855 Embedded Way | San Jose | | | 3,289 | 6,521 |
| 1065-1105 La Avenida Street | Mountain View | | | 46,832 | 109,275 |
| 1875 Charleston Road | Mountain View | M | | - | 2,615 |
| 1750 Automation Parkway | San Jose | G | | 4,789 | 11,174 |
| 1756 Automation Parkway | San Jose | G | | 4,378 | 10,216 |
| 1762 Automation Parkway | San Jose | G | | 4,804 | 12,224 |
| 1768 Automation Parkway | San Jose | H | | 8,195 | 19,121 |
| 255 Caspian Drive | Sunnyvale | | | 3,491 | 7,160 |
| 245 Caspian Drive | Sunnyvale | | | 5,894 | - |
| 5981 Optical Court | San Jose | F | | 4,054 | 14,938 |
| 5970 Optical Court | San Jose | | | 2,758 | 8,395 |
| 5900 Optical Court | San Jose | | | 3,634 | 12,677 |
| 2630 Orchard Parkway | San Jose | | | 2,932 | 5,863 |
| 2610 Orchard Parkway | San Jose | J | | 2,615 | 5,231 |
| 55 West Trimble Road | San Jose | J | | 4,435 | 8,869 |

| | | | | |
|---|---|---|---|---|
| 2001 Walsh Avenue | Santa Clara | E,G,I | 4,610 | 3,887 |
| 2880 Scott Blvd | Santa Clara | E,H,I | 14,501 | 22,555 |
| 2890 Scott Blvd | Santa Clara | E,H,I | 3,081 | 9,696 |
| 2770-2800 Scott Blvd | Santa Clara | E,H | 7,138 | 7,075 |
| 2300 Central Expressway | Santa Clara | E,G,I | 2,390 | 2,459 |
| 2220 Central Expressway | Santa Clara | E,G,I | 3,305 | 3,427 |
| 2330 Central Expressway | Santa Clara | E,G | 3,673 | 3,932 |
| 233 South Hillview Drive | Milpitas | F,N | 3,335 | 10,076 |
| 2251 Lawson Lane | Santa Clara | | 1,952 | 9,498 |
| 1230 East Arques | Sunnyvale | F | 540 | 2,628 |
| 1250 East Arques | Sunnyvale | F | 1,335 | 6,499 |
| 20400 Mariani Avenue | Cupertino | | 1,670 | 8,125 |
| 10500 De Anza Blvd | Cupertino | | 7,666 | 37,304 |
| 20605-20705 Valley Green Drive | Cupertino | G | 3,490 | 16,984 |
| 10300 Bubb Road | Cupertino | F | 635 | 3,090 |
| 10440 Bubb Road | Cupertino | | 434 | 2,112 |
| 10460 Bubb Road | Cupertino | H | 994 | 4,838 |
| 1135 Kern Avenue | Sunnyvale | | 407 | 1,982 |
| 450 National Avenue | Mountain View | | 611 | 2,973 |
| 3301 Olcott Street | Santa Clara | | 1,846 | 8,984 |
| 2800 Bayview Avenue | Fremont | | 1,070 | 5,205 |
| 5521 Hellyer Avenue | San Jose | | 4,534 | 9,650 |
| 6850 Santa Teresa Blvd | San Jose | H | 377 | 1,836 |

| | | | Total Cost | | | |
|---|---|---|---|---|---|---|
| Property Name | City | | Land | Buildings and Improvements | Total | Accu Depre & Amor |
| 5300-5350 Hellyer Avenue | San Jose | C | $5,742 | $11,442 | $17,184 | $2 |
| 10401-10411 Bubb Road | Cupertino | A | 633 | 3,078 | 3,711 | |
| 45365 Northport Loop | Fremont | | 2,447 | 5,722 | 8,169 | 1 |
| 45738 Northport Loop | Fremont | F | 891 | 4,343 | 5,234 | 1 |
| 4050 Starboard Drive | Fremont | F | 1,329 | 6,475 | 7,804 | 1 |
| 3501 W. Warren Ave/Fremont Blvd | Fremont | | 1,866 | 10,464 | 12,330 | 3 |
| 48800 Milmont Blvd | Fremont | | 1,013 | 4,932 | 5,945 | 1 |
| 4750 Patrick Henry Drive | Santa Clara | H | 1,604 | 8,210 | 9,814 | 2 |
| 3520 Bassett Street | Santa Clara | D | 1,104 | 5,371 | 6,475 | 1 |
| 3530 Bassett Street | Santa Clara | B,D | 849 | 4,133 | 4,982 | 1 |
| 5850-5870 Hellyer Avenue | San Jose | | 2,787 | 6,633 | 9,420 | 1 |
| 5750 Hellyer Avenue | San Jose | | 3,266 | 6,152 | 9,418 | 1 |
| 800 Embedded Way | San Jose | K | 1,794 | - | 1,794 | |
| 5500 Hellyer Avenue | San Jose | F | 4,735 | 14,060 | 18,795 | 2 |
| 5550 Hellyer Avenue | San Jose | F | 3,261 | 7,233 | 10,494 | |
| 5400 Hellyer Avenue | San Jose | | 3,238 | 5,222 | 8,460 | 1 |
| 5325 Hellyer Avenue | San Jose | H | 4,684 | 10,270 | 14,954 | 2 |
| 5345 Hellyer Avenue | San Jose | H | 4,866 | 8,351 | 13,217 | 1 |
| 5905-5965 Silver Creek Valley Rd | San Jose | | 8,437 | 17,316 | 25,753 | 3 |
| 5905-5965 Silver Creek Valley Rd | San Jose | | 3,438 | 2,727 | 6,165 | |
| 5845 Hellyer Avenue | San Jose | | 6,090 | 5,029 | 11,119 | |
| 855 Embedded Way | San Jose | | 3,289 | 6,671 | 9,960 | 1 |

| | | | | | | |
|---|---|---|---|---|---|---|
| 1065-1105 La Avenida Street | Mountain View | | 46,832 | 109,340 | 156,172 | 26 |
| 1875 Charleston Road | Mountain View | M | - | 2,615 | 2,615 | |
| 1750 Automation Parkway | San Jose | G | 4,789 | 11,489 | 16,278 | 2 |
| 1756 Automation Parkway | San Jose | G | 4,378 | 10,920 | 15,298 | 2 |
| 1762 Automation Parkway | San Jose | G | 4,804 | 13,556 | 18,360 | 2 |
| 1768 Automation Parkway | San Jose | H | 8,195 | 19,339 | 27,534 | 3 |
| 255 Caspian Drive | Sunnyvale | | 3,491 | 8,818 | 12,309 | 2 |
| 245 Caspian Drive | Sunnyvale | | 5,894 | - | 5,894 | |
| 5981 Optical Court | San Jose | F | 4,054 | 15,236 | 19,290 | |
| 5970 Optical Court | San Jose | | 2,758 | 8,395 | 11,153 | 1 |
| 5900 Optical Court | San Jose | | 3,634 | 12,760 | 16,394 | 2 |
| 2630 Orchard Parkway | San Jose | | 2,932 | 5,885 | 8,817 | 1 |
| 2610 Orchard Parkway | San Jose | J | 2,615 | 5,231 | 7,846 | |
| 55 West Trimble Road | San Jose | J | 4,435 | 8,869 | 13,304 | 1 |
| 2001 Walsh Avenue | Santa Clara | E,G,I | 4,610 | 3,887 | 8,497 | |
| 2880 Scott Blvd | Santa Clara | E,H,I | 14,501 | 23,026 | 37,527 | 3 |
| 2890 Scott Blvd | Santa Clara | E,H,I | 3,081 | 9,721 | 12,802 | 1 |
| 2770-2800 Scott Blvd | Santa Clara | E,H | 7,138 | 7,245 | 14,383 | 1 |
| 2300 Central Expressway | Santa Clara | E,G,I | 2,390 | 2,459 | 4,849 | |
| 2220 Central Expressway | Santa Clara | E,G,I | 3,305 | 4,243 | 7,548 | |
| 2330 Central Expressway | Santa Clara | E,G | 3,673 | 4,609 | 8,282 | |
| 233 South Hillview Drive | Milpitas | F,N | 3,335 | 10,076 | 13,411 | 1 |
| 2251 Lawson Lane | Santa Clara | | 1,952 | 9,999 | 11,951 | 2 |
| 1230 East Arques | Sunnyvale | F | 540 | 2,667 | 3,207 | |
| 1250 East Arques | Sunnyvale | F | 1,335 | 6,499 | 7,834 | 1 |
| 20400 Mariani Avenue | Cupertino | | 1,670 | 9,071 | 10,741 | 2 |
| 10500 De Anza Blvd | Cupertino | | 7,666 | 37,304 | 44,970 | 9 |
| 20605-20705 Valley Green Drive | Cupertino | G | 3,490 | 16,984 | 20,474 | 4 |
| 10300 Bubb Road | Cupertino | F | 635 | 3,090 | 3,725 | |
| 10440 Bubb Road | Cupertino | | 434 | 2,226 | 2,660 | |
| 10460 Bubb Road | Cupertino | H | 994 | 6,117 | 7,111 | 1 |
| 1135 Kern Avenue | Sunnyvale | | 407 | 1,982 | 2,389 | |
| 450 National Avenue | Mountain View | | 611 | 3,045 | 3,656 | |
| 3301 Olcott Street | Santa Clara | | 1,846 | 9,021 | 10,867 | 2 |
| 2800 Bayview Avenue | Fremont | | 1,070 | 5,265 | 6,335 | 1 |
| 5521 Hellyer Avenue | San Jose | | 4,534 | 9,650 | 14,184 | 1 |
| 6850 Santa Teresa Blvd | San Jose | H | 377 | 2,655 | 3,032 | |



| | | | | Initial Cost | |
|---|---|---|---|---|---|
| Property Name | City | | December 31, 2008 Encumbrances | Land | Buildings and Improvements |
| 6810 Santa Teresa Blvd | San Jose | H | | 2,567 | 5,991 |
| 140-160 Great Oaks Blvd | San Jose | | | 1,402 | 6,822 |
| 6541 Via del Oro/6385 San Ignacio | San Jose | G | | 1,039 | 5,057 |
| 6311-6351 San Ignacio Avenue | San Jose | F | | 6,246 | 30,396 |
| 6320-6360 San Ignacio Avenue | San Jose | G | | 2,616 | 12,732 |
| 75 E. Trimble Rd/2610 N. First St | San Jose | | | 3,477 | 16,919 |
| 2904 Orchard Parkway | San Jose | F,O | | 4,704 | 11,992 |
| 3236 Scott Blvd | Santa Clara | F | | 1,234 | 6,005 |
| 1212 Bordeaux Lane | Sunnyvale | F | | 2,250 | 10,948 |
| 1325-1810 McCandless Drive | Milpitas | | | 13,994 | 66,213 |

| | | | | | |
|---|---|---|---|---|---|
| 1600 Memorex Drive | Santa Clara | | | 1,221 | 5,940 |
| 1688 Richard Avenue | Santa Clara | | | 1,248 | 2,913 |
| 1700 Richard Avenue | Santa Clara | | | 1,727 | 4,030 |
| Morgan Hill Land | Morgan Hill | | | 25,543 | - |
| Morgan Hill Land | Morgan Hill | | | 2,297 | - |
| 300 Montague Expressway | Milpitas | | | 2,609 | 2,499 |
| 337 Trade Zone Blvd | Milpitas | | | 2,264 | 2,168 |
| 324-368 Montague Expressway | Milpitas | | | 2,968 | 2,843 |
| 3506-3510 Bassett Street | Santa Clara | D | | 943 | 4,591 |
| 3540-3544 Bassett Street | Santa Clara | F,D | | 1,565 | 7,616 |
| 3550 Bassett Street | Santa Clara | F,D | | 1,079 | 5,251 |
| 3560 Bassett Street | Santa Clara | F,D | | 1,075 | 5,233 |
| 3570-3580 Bassett Street | Santa Clara | F,D | | 1,075 | 5,233 |
| Hartford Loan | | F | 114,513 | | |
| Northwestern Mutual Life Ins. Co. | | G | 81,308 | | |
| Allianz Life Insurance Company | | H | 135,087 | | |
| | | | $339,669 | $320,911 | $774,795 |

| Property Name | City | | Total Cost: Land | Total Cost: Buildings and Improvements | Total | Accu Depre & Amor |
|---|---|---|---|---|---|---|
| 6810 Santa Teresa Blvd | San Jose | H | 2,567 | 6,763 | 9,330 | |
| 140-160 Great Oaks Blvd | San Jose | | 1,402 | 7,576 | 8,978 | |
| 6541 Via del Oro/6385 San Ignacio | San Jose | G | 1,039 | 5,138 | 6,177 | |
| 6311-6351 San Ignacio Avenue | San Jose | F | 6,246 | 30,566 | 36,812 | |
| 6320-6360 San Ignacio Avenue | San Jose | G | 2,616 | 13,171 | 15,787 | |
| 75 E. Trimble Rd/2610 N. First St | San Jose | | 3,477 | 17,004 | 20,481 | |
| 2904 Orchard Parkway | San Jose | F,O | 4,704 | 11,992 | 16,696 | |
| 3236 Scott Blvd | Santa Clara | F | 1,234 | 6,005 | 7,239 | |
| 1212 Bordeaux Lane | Sunnyvale | F | 2,250 | 10,948 | 13,198 | |
| 1325-1810 McCandless Drive | Milpitas | | 13,994 | 67,668 | 81,662 | 1 |
| 1600 Memorex Drive | Santa Clara | | 1,221 | 5,951 | 7,172 | |
| 1688 Richard Avenue | Santa Clara | | 1,248 | 2,919 | 4,167 | |
| 1700 Richard Avenue | Santa Clara | | 1,727 | 4,030 | 5,757 | |
| Morgan Hill Land | Morgan Hill | | 25,543 | - | 25,543 | |
| Morgan Hill Land | Morgan Hill | | 2,297 | - | 2,297 | |
| 300 Montague Expressway | Milpitas | | 2,609 | 2,499 | 5,108 | |
| 337 Trade Zone Blvd | Milpitas | | 2,264 | 2,168 | 4,432 | |
| 324-368 Montague Expressway | Milpitas | | 2,968 | 2,843 | 5,811 | |
| 3506-3510 Bassett Street | Santa Clara | D | 943 | 4,773 | 5,716 | |
| 3540-3544 Bassett Street | Santa Clara | F,D | 1,565 | 7,811 | 9,376 | |
| 3550 Bassett Street | Santa Clara | F,D | 1,079 | 5,284 | 6,363 | |
| 3560 Bassett Street | Santa Clara | F,D | 1,075 | 5,241 | 6,316 | |
| 3570-3580 Bassett Street | Santa Clara | F,D | 1,075 | 5,233 | 6,308 | |
| Hartford Loan | | F | | | | |
| Northwestern Mutual Life Ins. Co. | | G | | | | |
| Allianz Life Insurance Company | | H | | | | |
| | | | $320,911 | $802,711 | $1,123,622 | $18 |

(A) 16.67% of this property's ownership is held by unaffiliated parties outside the operating partnerships of the Company.
(B) 25% of this property's ownership is held by unaffiliated parties outside the operating partnerships of the Company.
(C) 50% of this property's ownership is held by an affiliated party since September 2000.
(D) Part of the property group referred to as the Triangle Technology Park.
(E) Part of the property group referred to as the San Tomas Technology Park.
(F) Encumbered by the $114,513 Hartford loan - full amount of loan shown at the bottom of the schedule.
(G) Encumbered by the $81,308 Northwestern Mutual Life Insurance Company loan - full amount of loan shown at the bottom of the schedule.
(H) Encumbered by the $135,087 Allianz Life Insurance Company loan - full amount of loan shown at the bottom of the schedule.
(I) Purchase price allocated to real estate related intangible assets pursuant to SFAS 141 amounted to $18,284. Approximately $17,410 and $874 was fully amortized in 2007 and 2005, respectively, and the asset cost and its related accumulated amortization was removed from the accounts.
(J) Purchase price allocated to real estate related intangible assets pursuant to SFAS 141 amounted to $1,367. The amount was fully amortized in 2004 and the asset cost and its related accumulated amortization was removed from the accounts.
(K) This property was sold in October 2005. The Company retained 32.5%, or approximately 7.9 acres, of raw land.
(L) Depreciation is computed based on the following estimated lives:
    1. Building shell and base building tenant improvements of newly acquired properties are being depreciated on a weighted average composite useful life of 40 years.
    2. Real estate intangible assets allocated pursuant to SFAS 141 are being amortized over the remaining life of the underlying leases.
    3. Tenant improvements, furniture and fixtures are being depreciated over their estimated useful lives ranging from 5 to 10 years.
(M) Purchase price allocated to real estate related intangible assets pursuant to SFAS 141 amounted to $745.
(N) Purchase price allocated to real estate related intangible assets pursuant to SFAS 141 amounted to $1,374.
(O) Purchase price allocated to real estate related intangible assets pursuant to SFAS 141 amounted to $1,121.



MISSION WEST PROPERT
Schedule II
Real Estate and Accumulated Deprec
December 31, 2
(dollars in thou

| Property Name | City | December 31, 2007 Encumbrances | Initial Cost: Land | Initial Cost: Buildings and Improvements |
| --- | --- | --- | --- | --- |

| | | | | | |
|---|---|---|---|---|---|
| 5300-5350 Hellyer Avenue | San Jose | C | $9,224 | $5,742 | $11,442 |
| 10401-10411 Bubb Road | Cupertino | A | | 633 | 3,078 |
| 45365 Northport Loop | Fremont | | | 2,447 | 5,711 |
| 45738 Northport Loop | Fremont | F | | 891 | 4,338 |
| 4050 Starboard Drive | Fremont | F | | 1,329 | 6,467 |
| 3501 W. Warren Ave/Fremont Blvd | Fremont | | | 1,866 | 9,082 |
| 48800 Milmont Blvd | Fremont | | | 1,013 | 4,932 |
| 4750 Patrick Henry Drive | Santa Clara | | | 1,604 | 7,805 |
| 3520 Bassett Street | Santa Clara | D | | 1,104 | 5,371 |
| 3530 Bassett Street | Santa Clara | B,D | | 849 | 4,133 |
| 5850-5870 Hellyer Avenue | San Jose | | | 2,787 | 6,502 |
| 5750 Hellyer Avenue | San Jose | | | 3,266 | 3,354 |
| 800 Embedded Way | San Jose | K | | 1,794 | - |
| 5500 Hellyer Avenue | San Jose | | | 4,735 | 12,485 |
| 5550 Hellyer Avenue | San Jose | | | 3,261 | 3,478 |
| 5400 Hellyer Avenue | San Jose | | | 3,238 | 5,007 |
| 5325 Hellyer Avenue | San Jose | H | | 4,684 | 10,230 |
| 5345 Hellyer Avenue | San Jose | H | | 4,866 | 5,822 |
| 5905-5965 Silver Creek Valley Rd | San Jose | | | 8,437 | 17,316 |
| 5905-5965 Silver Creek Valley Rd | San Jose | | | 3,438 | 2,727 |
| 5845 Hellyer Avenue | San Jose | | | 6,090 | 5,029 |
| 855 Embedded Way | San Jose | | | 3,289 | 6,521 |
| 1065-1105 La Avenida Street | Mountain View | | | 46,832 | 109,275 |
| 1875 Charleston Road | Mountain View | M | | - | 2,615 |
| 1750 Automation Parkway | San Jose | G | | 4,789 | 11,174 |
| 1756 Automation Parkway | San Jose | G | | 4,378 | 10,216 |
| 1762 Automation Parkway | San Jose | G | | 4,804 | 12,224 |
| 1768 Automation Parkway | San Jose | H | | 8,195 | 19,121 |
| 255 Caspian Drive | Sunnyvale | | | 3,491 | 7,160 |
| 245 Caspian Drive | Sunnyvale | | | 5,894 | - |
| 5970 Optical Court | San Jose | | | 2,758 | 8,395 |
| 5900 Optical Court | San Jose | H | | 3,634 | 12,677 |
| 2630 Orchard Parkway | San Jose | | | 2,931 | 5,863 |
| 2610 Orchard Parkway | San Jose | J | | 2,615 | 5,231 |
| 55 West Trimble Road | San Jose | J | | 4,435 | 8,869 |
| 2001 Walsh Avenue | Santa Clara | E,I | | 4,610 | 3,887 |
| 2880 Scott Blvd | Santa Clara | E,H,I | | 14,501 | 22,555 |
| 2890 Scott Blvd | Santa Clara | E,H,I | | 3,081 | 9,696 |
| 2770-2800 Scott Blvd | Santa Clara | E,H | | 7,138 | 7,075 |
| 2300 Central Expressway | Santa Clara | E,I | | 2,390 | 2,459 |
| 2220 Central Expressway | Santa Clara | E,I | | 3,304 | 3,427 |
| 2330 Central Expressway | Santa Clara | E | | 3,673 | 3,932 |
| 233 South Hillview Drive | Milpitas | N | | 3,335 | 10,076 |
| 2251 Lawson Lane | Santa Clara | G | | 1,952 | 9,498 |
| 1230 East Arques | Sunnyvale | F | | 540 | 2,628 |
| 1250 East Arques | Sunnyvale | F | | 1,335 | 6,499 |
| 20400 Mariani Avenue | Cupertino | H | | 1,670 | 8,125 |
| 10500 De Anza Blvd | Cupertino | F | | 7,666 | 37,304 |
| 20605-20705 Valley Green Drive | Cupertino | G | | 3,490 | 16,984 |
| 10300 Bubb Road | Cupertino | F | | 635 | 3,090 |
| 10440 Bubb Road | Cupertino | | | 434 | 2,112 |
| 10460 Bubb Road | Cupertino | H | | 994 | 4,838 |
| 1135 Kern Avenue | Sunnyvale | F | | 407 | 1,982 |
| 450 National Avenue | Mountain View | F | | 611 | 2,973 |
| 3301 Olcott Street | Santa Clara | | | 1,846 | 8,984 |
| 2800 Bayview Avenue | Fremont | | | 1,070 | 5,205 |
| 5521 Hellyer Avenue | San Jose | | | 4,534 | 9,650 |
| 6850 Santa Teresa Blvd | San Jose | | | 377 | 1,836 |

| Property Name | City | | Total Cost: Land | Total Cost: Buildings and Improvements | Total Cost: Total | Accu Depre & Amor |
|---|---|---|---|---|---|---|
| 5300-5350 Hellyer Avenue | San Jose | C | $5,742 | $11,442 | $17,184 | $ |
| 10401-10411 Bubb Road | Cupertino | A | 633 | 3,078 | 3,711 | |
| 45365 Northport Loop | Fremont | | 2,447 | 5,722 | 8,169 | |
| 45738 Northport Loop | Fremont | F | 891 | 4,343 | 5,234 | |
| 4050 Starboard Drive | Fremont | F | 1,329 | 6,475 | 7,804 | |
| 3501 W. Warren Ave/Fremont Blvd | Fremont | | 1,866 | 10,464 | 12,330 | |
| 48800 Milmont Blvd | Fremont | | 1,013 | 4,932 | 5,945 | |
| 4750 Patrick Henry Drive | Santa Clara | | 1,604 | 8,210 | 9,814 | |
| 3520 Bassett Street | Santa Clara | D | 1,104 | 5,371 | 6,475 | |
| 3530 Bassett Street | Santa Clara | B,D | 849 | 4,133 | 4,982 | |
| 5850-5870 Hellyer Avenue | San Jose | | 2,787 | 6,633 | 9,420 | |
| 5750 Hellyer Avenue | San Jose | | 3,266 | 6,481 | 9,747 | |
| 800 Embedded Way | San Jose | K | 1,794 | - | 1,794 | |
| 5500 Hellyer Avenue | San Jose | | 4,735 | 12,524 | 17,259 | |
| 5550 Hellyer Avenue | San Jose | | 3,261 | 3,478 | 6,739 | |
| 5400 Hellyer Avenue | San Jose | | 3,238 | 5,222 | 8,460 | |
| 5325 Hellyer Avenue | San Jose | H | 4,684 | 10,270 | 14,954 | |
| 5345 Hellyer Avenue | San Jose | H | 4,866 | 5,822 | 10,688 | |
| 5905-5965 Silver Creek Valley Rd | San Jose | | 8,437 | 17,316 | 25,753 | |
| 5905-5965 Silver Creek Valley Rd | San Jose | | 3,438 | 2,727 | 6,165 | |
| 5845 Hellyer Avenue | San Jose | | 6,090 | 5,029 | 11,119 | |
| 855 Embedded Way | San Jose | | 3,289 | 6,589 | 9,878 | |
| 1065-1105 La Avenida Street | Mountain View | | 46,832 | 109,340 | 156,172 | 2 |
| 1875 Charleston Road | Mountain View | M | - | 2,615 | 2,615 | |
| 1750 Automation Parkway | San Jose | G | 4,789 | 11,489 | 16,278 | |
| 1756 Automation Parkway | San Jose | G | 4,378 | 10,920 | 15,298 | |
| 1762 Automation Parkway | San Jose | G | 4,804 | 13,556 | 18,360 | |
| 1768 Automation Parkway | San Jose | H | 8,195 | 19,263 | 27,458 | |
| 255 Caspian Drive | Sunnyvale | | 3,491 | 8,818 | 12,309 | |
| 245 Caspian Drive | Sunnyvale | | 5,894 | - | 5,894 | |
| 5970 Optical Court | San Jose | | 2,758 | 8,395 | 11,153 | |
| 5900 Optical Court | San Jose | H | 3,634 | 12,760 | 16,394 | |
| 2630 Orchard Parkway | San Jose | | 2,931 | 5,885 | 8,816 | |
| 2610 Orchard Parkway | San Jose | J | 2,615 | 5,231 | 7,846 | |
| 55 West Trimble Road | San Jose | J | 4,435 | 8,869 | 13,304 | |
| 2001 Walsh Avenue | Santa Clara | E,I | 4,610 | 3,887 | 8,497 | |
| 2880 Scott Blvd | Santa Clara | E,H,I | 14,501 | 22,555 | 37,056 | |
| 2890 Scott Blvd | Santa Clara | E,H,I | 3,081 | 9,721 | 12,802 | |
| 2770-2800 Scott Blvd | Santa Clara | E,H | 7,138 | 7,245 | 14,383 | |
| 2300 Central Expressway | Santa Clara | E,I | 2,390 | 2,459 | 4,849 | |
| 2220 Central Expressway | Santa Clara | E,I | 3,304 | 4,243 | 7,547 | |
| 2330 Central Expressway | Santa Clara | E | 3,673 | 4,609 | 8,282 | |
| 233 South Hillview Drive | Milpitas | N | 3,335 | 10,076 | 13,411 | |
| 2251 Lawson Lane | Santa Clara | G | 1,952 | 9,498 | 11,450 | |
| 1230 East Arques | Sunnyvale | F | 540 | 2,667 | 3,207 | |
| 1250 East Arques | Sunnyvale | F | 1,335 | 6,499 | 7,834 | |
| 20400 Mariani Avenue | Cupertino | H | 1,670 | 8,991 | 10,661 | |

| | | | | | |
|---|---|---|---|---|---|
| 10500 De Anza Blvd | Cupertino | F | 7,666 | 37,304 | 44,970 |
| 20605-20705 Valley Green Drive | Cupertino | G | 3,490 | 16,984 | 20,474 |
| 10300 Bubb Road | Cupertino | F | 635 | 3,090 | 3,725 |
| 10440 Bubb Road | Cupertino | | 434 | 2,226 | 2,660 |
| 10460 Bubb Road | Cupertino | H | 994 | 6,117 | 7,111 |
| 1135 Kern Avenue | Sunnyvale | F | 407 | 1,982 | 2,389 |
| 450 National Avenue | Mountain View | F | 611 | 3,045 | 3,656 |
| 3301 Olcott Street | Santa Clara | | 1,846 | 9,021 | 10,867 |
| 2800 Bayview Avenue | Fremont | | 1,070 | 5,265 | 6,335 |
| 5521 Hellyer Avenue | San Jose | | 4,534 | 9,650 | 14,184 |
| 6850 Santa Teresa Blvd | San Jose | | 377 | 2,655 | 3,032 |



MISSION WEST PROPERTIES, INC.
Schedule III
Real Estate and Accumulated Depreciation and Amortization
December 31, 2007
(dollars in thousands)

| | | | | Initial Cost | |
|---|---|---|---|---|---|
| Property Name | City | | December 31, 2007 Encumbrances | Land | Buildings and Improvements |
| 6810 Santa Teresa Blvd | San Jose | | | 2,567 | 5,991 |
| 140-160 Great Oaks Blvd | San Jose | | | 1,402 | 6,822 |
| 6541 Via del Oro/6385 San Ignacio | San Jose | G | | 1,039 | 5,057 |
| 6311-6351 San Ignacio Avenue | San Jose | F | | 6,247 | 30,396 |
| 6320-6360 San Ignacio Avenue | San Jose | G | | 2,616 | 12,732 |
| 75 E. Trimble Rd/2610 N.First St | San Jose | | | 3,477 | 16,919 |
| 3236 Scott Blvd | Santa Clara | F | | 1,234 | 6,005 |
| 1212 Bordeaux Lane | Sunnyvale | F | | 2,250 | 10,948 |
| 1325-1810 McCandless Drive | Milpitas | G | | 13,994 | 66,213 |
| 1600 Memorex Drive | Santa Clara | F | | 1,221 | 5,940 |
| 1688 Richard Avenue | Santa Clara | F | | 1,248 | 2,913 |
| 1700 Richard Avenue | Santa Clara | F | | 1,727 | 4,030 |
| Morgan Hill Land | Morgan Hill | | | 25,543 | - |
| Morgan Hill Land | Morgan Hill | | | 2,297 | - |
| 300 Montague Expressway | Milpitas | | | 2,609 | 2,499 |
| 337 Trade Zone Blvd | Milpitas | | | 2,264 | 2,168 |
| 324-368 Montague Expressway | Milpitas | | | 2,968 | 2,843 |
| 3506-3510 Bassett Street | Santa Clara | D | | 943 | 4,591 |
| 3540-3544 Bassett Street | Santa Clara | F,D | | 1,565 | 7,616 |
| 3550 Bassett Street | Santa Clara | F,D | | 1,079 | 5,251 |
| 3560 Bassett Street | Santa Clara | F,D | | 1,075 | 5,233 |
| 3570-3580 Bassett Street | Santa Clara | F,D | | 1,075 | 5,233 |
| Prudential Mortgage Capital Co. | | F | 112,543 | | |
| Northwestern Mutual Life Ins. Co. | | G | 84,959 | | |
| Allianz Life Insurance Company | | H | 140,018 | | |
| | | | $346,744 | $312,152 | $747,865 |

| Property Name | City | | Total Cost Land | Buildings and Improvements | Total | Accu Depre & Amor |
|---|---|---|---|---|---|---|
| 6810 Santa Teresa Blvd | San Jose | | 2,567 | 6,765 | 9,332 | |
| 140-160 Great Oaks Blvd | San Jose | | 1,402 | 7,576 | 8,978 | |
| 6541 Via del Oro/6385 San Ignacio | San Jose | G | 1,039 | 5,138 | 6,177 | |
| 6311-6351 San Ignacio Avenue | San Jose | F | 6,247 | 30,566 | 36,813 | |
| 6320-6360 San Ignacio Avenue | San Jose | G | 2,616 | 13,171 | 15,787 | |
| 75 E. Trimble Rd/2610 N.First St | San Jose | | 3,477 | 17,004 | 20,481 | |
| 3236 Scott Blvd | Santa Clara | F | 1,234 | 6,005 | 7,239 | |
| 1212 Bordeaux Lane | Sunnyvale | F | 2,250 | 10,948 | 13,198 | |
| 1325-1810 McCandless Drive | Milpitas | G | 13,994 | 67,668 | 81,662 | 1 |
| 1600 Memorex Drive | Santa Clara | F | 1,221 | 5,951 | 7,172 | |
| 1688 Richard Avenue | Santa Clara | F | 1,248 | 2,919 | 4,167 | |
| 1700 Richard Avenue | Santa Clara | F | 1,727 | 4,030 | 5,757 | |
| Morgan Hill Land | Morgan Hill | | 25,543 | - | 25,543 | |
| Morgan Hill Land | Morgan Hill | | 2,297 | - | 2,297 | |
| 300 Montague Expressway | Milpitas | | 2,609 | 2,499 | 5,108 | |
| 337 Trade Zone Blvd | Milpitas | | 2,264 | 2,168 | 4,432 | |
| 324-368 Montague Expressway | Milpitas | | 2,968 | 2,843 | 5,811 | |
| 3506-3510 Bassett Street | Santa Clara | D | 943 | 4,773 | 5,716 | |
| 3540-3544 Bassett Street | Santa Clara | F,D | 1,565 | 7,811 | 9,376 | |
| 3550 Bassett Street | Santa Clara | F,D | 1,079 | 5,284 | 6,363 | |
| 3560 Bassett Street | Santa Clara | F,D | 1,075 | 5,241 | 6,316 | |
| 3570-3580 Bassett Street | Santa Clara | F,D | 1,075 | 5,233 | 6,308 | |
| Prudential Mortgage Capital Co. | | F | | | | |
| Northwestern Mutual Life Ins. Co. | | G | | | | |
| Allianz Life Insurance Company | | H | | | | |
| | | | $312,152 | $766,784 | $1,078,936 | $15 |

(A) 16.67% of this property's ownership is held by unaffiliated parties outside the operating partnerships of the Company.
(B) 25% of this property's ownership is held by unaffiliated parties outside the operating partnerships of the Company.
(C) 50% of this property's ownership is held by an affiliated party since September 2000.
(D) Part of the property group referred to as the Triangle Technology Park.
(E) Part of the property group referred to as the San Tomas Technology Park.
(F) Encumbered by the $112,543 Prudential Mortgage Capital Company loan - full amount of loan shown at the bottom of the schedule.
(G) Encumbered by the $84,959 Northwestern Mutual Life Insurance Company loan - full amount of loan shown at the bottom of the schedule.
(H) Encumbered by the $140,018 Allianz Life Insurance Company loan - full amount of loan shown at the bottom of the schedule.
(I) Purchase price allocated to real estate related intangible assets pursuant to SFAS 141 amounted to $18,284. Approximately $17,410 and $874 was fully amortized in 2007 and 2005, respectively, and the asset cost and its related accumulated amortization was removed from the accounts.
(J) Purchase price allocated to real estate related intangible assets pursuant

to SFAS 141 amounted to $1,367. The amount was fully amortized in 2004 and the asset cost and its related accumulated amortization was removed from the accounts.

(K) This property was sold in October 2005. The Company retained 32.5%, or approximately 7.9 acres, of raw land.

(L) Depreciation is computed based on the following estimated lives:

1. Building shell and base building tenant improvements of newly acquired properties are being depreciated on a weighted average composite useful life of 40 years.
2. Real estate intangible assets allocated pursuant to SFAS 141 are being amortized over the remaining life of the underlying leases.
3. Tenant improvements, furniture and fixtures are being depreciated over their estimated useful lives ranging from 5 to 10 years.

(M) Purchase price allocated to real estate related intangible assets pursuant to SFAS 141 amounted to $745. (N) Purchase price allocated to real estate related intangible assets pursuant to SFAS 141 amounted to $1,374.



MISSION WEST PROPERTIES, INC.
NOTE TO SCHEDULE III
December 31, 2008, 2007 and 2006
(dollars in thousands)

1. Reconciliation of real estate and accumulated depreciation and amortization:

| | 2008 | 2007 |
|---|---|---|
| Real estate investments: | | |
| Balance at beginning of year | $1,078,936 | $1,048,348 |
| Additions | 42,157 | 58,972 |
| Dispositions | - | (10,974) |
| Reclassification | 2,529 | (17,410) |
| Balance at end of year | $1,123,622 | $1,078,936 |
| Accumulated depreciation and amortization: | | |
| Balance at beginning of year | $156,819 | $149,459 |
| Additions | 23,224 | 26,826 |
| Dispositions | - | (2,056) |
| Reclassification | - | (17,410) |
| Balance at end of year | $180,043 | $156,819 |
| Net investments in real estate | $943,579 | $922,117 |

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures

As required by SEC Rule 13a-15(b) we conducted an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer, President and Vice President of Finance, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(f) or Rule 15d-15(f) of the Securities Exchange Act of 1934). Based upon that evaluation, the Chief Executive Officer, President and Vice President of Finance concluded that as of December 31, 2008 our disclosure controls and procedures were effective such that the information required to be disclosed in our reports filed with the Securities and Exchange Commission is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms such information is accumulated and communicated to our management, including our Chief Executive Officer, President and Vice President of Finance, as appropriate, to allow for timely decisions regarding required disclosure.

(b) Management's Report on Internal Control over Financial Reporting

Management of Mission West Properties, Inc. is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934. Management assessed the effectiveness of Mission West Properties, Inc.'s internal control over financial reporting as of December 31, 2008. Management based this assessment on the criteria for effective internal control over financial reporting established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Management's assessment included an evaluation of the design of Mission West Properties, Inc.'s internal control over financial reporting and testing of the operational effectiveness of its internal control over financial reporting. Management reviewed the results of its assessment with the Audit Committee of the Board of Directors. Based on this assessment, management determined that Mission West Properties, Inc. maintained effective internal control over financial reporting as of December 31, 2008.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect the possibility of human error, misstatements and the circumvention or overriding of controls. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Burr, Pilger & Mayer, LLP, our independent registered public accounting firm, has audited our consolidated financial statements included in this Annual Report on Form 10-K and has issued a report on the effectiveness of our internal control over financial reporting.

(c) Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting during the fourth fiscal quarter of 2008 that has materially affected, or is reasonably likely to material affect, our internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None.



PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information required by Item 10 is incorporated by reference from the sections titled "Management - Directors and Executive Officers," "Corporate Governance" and "Code of Ethics" and "Section 16(a) Beneficial Ownership Reporting Compliance" in the Company's definitive proxy statement to be filed with respect to the 2009 annual stockholders' meeting.

ITEM 11. EXECUTIVE COMPENSATION

The information required by Item 11 is incorporated by reference from the section titled "Executive Compensation" in the Company's definitive proxy statement to be filed with respect to the 2009 annual stockholders' meeting, excluding, however, the sections titled "Executive Compensation - Performance Graph" and "Executive Compensation - Report on Executive Compensation by the Compensation Committee of the Board of Directors," none of which are incorporated by reference in response to this item.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information required by Item 12 is incorporated by reference from the sections titled "Share Ownership" and "Securities Authorized for Issuance Under Equity Compensation Plans" in the Company's definitive proxy statement to be filed with respect to the 2009 annual stockholders' meeting.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information required by Item 13 is incorporated by reference from the sections titled "Certain Relationships and Related Transactions" and "Corporate Governance" in the Company's definitive proxy statement to be filed with respect to the 2009 annual stockholders' meeting.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information required by Item 14 is incorporated by reference from the sections titled "Principal Accountant Fees and Services" in the Company's definitive proxy statement to be filed with respect to the 2009 annual stockholders' meeting.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) The following documents are filed as part of this report:

1. The consolidated financial statements are set forth in Item 8 of this Annual Report on Form 10-K.

   The following financial statement schedules should be read in conjunction with the consolidated financial statements included in Item 8 of this Annual Report on Form 10-K.

2. Schedule III - Real Estate and Accumulated Depreciation and Amortization as of December 31, 2008 and 2007, which can be found on pages 75 and 77, respectively.

3. The exhibits listed on the Exhibit Index either are filed with this Annual Report on Form 10-K or have been filed previously with the SEC and are incorporated by reference to those prior filings.

(b) The exhibits required by Item 601 of Regulation S-K, including each management contract or compensatory plan or arrangement required to be filed as an exhibit to this form are listed under Item 15(a)(3).



SIGNATURES

Pursuant to the requirements of the Section 13 or 15(d) 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.

MISSION WEST PROPERTIES, INC.

Date: March 13, 2009

By: /s/ Carl E. Berg

Carl E. Berg
Chief Executive Officer
(Principal Executive Officer)

Date: March 13, 2009

By: /s/ Wayne N. Pham

Wayne N. Pham
Vice President of Finance and
Controller (Principal Financial
and Accounting Officer)

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Carl E. Berg his true and lawful attorney-in-fact with the power of substitution, to sign any amendments to this Report on Form 10-K and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming all that each of said attorney-in-fact, or his or her substitute, may do or choose to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

| Signature | Title | Date |
| --- | --- | --- |
| /s/ Carl E. Berg<br>-------------------------------<br>Carl E. Berg | Chairman of the Board, Chief Executive Officer and Director | March 1 |
| /s/ William A. Hasler<br>-------------------------------<br>William A. Hasler | Director | March 1 |
| /s/ Lawrence B. Helzel<br>-------------------------------<br>Lawrence B. Helzel | Director | March 1 |
| /s/ Raymond V. Marino<br>-------------------------------<br>Raymond V. Marino | President, Chief Operating Officer and Director | March 1 |
| /s/ Martin S. Roher<br>-------------------------------<br>Martin S. Roher | Director | March 1 |



Exhibits required by Item 601 of Regulation S-K.

EXHIBIT INDEX

| | |
|---|---|
| 3.2.1 | Articles of Amendment and Restatement of Mission West Properties, Inc. (1) |
| 3.2.2 | Amended and Restated Bylaws of Mission West Properties, Inc. as of Decembe |
| 4.1 | Description of Capital Stock (2) |
| 4.1.1 | Specimen Common Stock certificate (2) |
| 10.1.1 | Amended and Restated Agreement of Limited Partnership of Mission West Prop |
| 10.1.2 | Amended and Restated Agreement of Limited Partnership of Mission West Prop |
| 10.1.3 | Amended and Restated Agreement of Limited Partnership of Mission West Prop |
| 10.1.4 | Amended and Restated Agreement of Limited Partnership of Mission West Prop |
| 10.2 | Exchange Rights Agreement between Mission West Properties and the Limited |
| 10.3.1* | 1997 Stock Option Plan (3) |
| 10.3.2* | Form of Incentive Stock Option Agreement (1) |
| 10.3.3* | Form of Non-statutory Stock Option Agreement (1) |
| 10.3.4* | Form of Directors Stock Option Agreement (1) |
| 10.4.1 | Acquisition Agreement, dated as of May 14, 1998, among Mission West Proper and the Berg Group (as defined therein) (1) |
| 10.4.2 | Amendment of Acquisition Agreement, dated as of July 1, 1998 (1) |
| 10.4.3 | Form of Partnership Interest Purchase Demand Note (1) |
| 10.5.1 | Stock Purchase Agreement dated as of May 4, 1998, between Mission West Pro Common Stock in a private placement of 5,800,000 shares and Subscription A |
| 10.5.2 | Stock Purchase Agreement dated as of May 4, 1998 between Mission West Prop Stock in a private placement of 695,058 shares and Subscription Agreement |
| 10.5.3 | Form of Registration Rights Agreement for purchasers, who acquired shares 1998 Stock Purchase Agreements (2c) |
| 10.6 | Pending Projects Acquisition Agreement among Mission West Properties, the Berg Group (2b) |
| 10.7 | Berg Land Holdings Option Agreement between Mission West Properties and ce |
| 10.8 | Berg & Berg Enterprises, Inc. Sublease Agreement (1) |
| 10.9 | Not in use |
| 10.10 | Not in use |
| 10.11 | Not in use |
| 10.12 | Lease Agreement with Apple Computer, Inc. (4a) |
| 10.13 | Not in use |
| 10.14 | Lease Agreement with Amdahl Corporation (4b) |
| 10.15 | Hartford Fixed Rate Term Loan Agreement ((5)) |
| 10.15.1 | Hartford Life Insurance Company Promissory Note ((5)) |
| 10.15.2 | Hartford Life and Annuity Insurance Company Promissory Note ((5)) |
| 10.15.3 | Hartford Life and Accident Insurance Company Promissory Note ((5)) |
| 10.15.4 | Hartford-Mission West Properties, L.P. (Santa Clara) Deed of Trust, S Filing (5) |
| 10.15.5 | Hartford-Mission West Properties, L.P. (Alameda) Deed of Trust, Securit |
| 10.15.6 | Hartford-Mission West Properties, L.P. I Deed of Trust, Security Agreement |
| 10.15.7 | Hartford-Mission West Properties, L.P. II Deed of Trust, Security Agreemen |
| 10.15.8 | Hartford-Mission West Properties, L.P. III Deed of Trust, Security Agreeme |
| 10.15.9 | Hartford Carveout Indemnity Agreement (5) |
| 10.15.10 | Hartford Environmental Indemnity Agreement (5) |
| 10.19 | Waiver Agreement (6) |
| 10.20 | Ownership Limit Exemption Agreement dated December 29, 1998 between Missio Paul McCarthy (7) |
| 10.21 | Lease Agreement with Microsoft Corporation, dated July 25, 1998 (8) |
| 10.21.1 | Lease Agreement with Microsoft Corporation, dated December 23, 2004 (8a) |
| 10.22 | Contribution Agreement (8) |
| 10.23 | Not in use |



| | |
|---|---|
| 10.24 | Not in use |

| | |
|---|---|
| 10.25 | Not in use |
| 10.26 | Supplemental Agreement among Mission West Properties, Inc., Carl E. Berg a |
| 10.27 | Berg Group Revolving Credit - $100,000,000 Secured Promissory Note (10) (T |
| 10.27.1 | Third Amendment to Berg Group $100,000,000 Revolving Line of Credit (11) ( |
| 10.28 | Berg Group Deed of Trust Securing Revolving Promissory Note (12) |
| 10.29 | Not in use |
| 10.30 | Mission West Properties, LP Continuing Guaranty (13) |
| 10.31 | Mission West Properties, LP II Continuing Guaranty (13) |
| 10.32 | Mission West Properties, L.P. Promissory Note to Northwestern Mutual Life |
| 10.32.1 | Mission West Properties, L.P. First Amendment to Promissory Note to Northw Company |
| 10.33 | Mission West Properties, L.P. I Promissory Note to Northwestern Mutual Lif |
| 10.33.1 | Mission West Properties, L.P. I First Amendment to Promissory Note to Nort Company |
| 10.34 | Mission West Properties, L.P. II Promissory Note to Northwestern Mutual Li |
| 10.34.1 | Mission West Properties, L.P. II First Amendment to Promissory Note to Nor Company |
| 10.35 | Mission West Properties, L.P. Deed of Trust and Security Agreement (First |
| 10.36 | Mission West Properties, L.P. Deed of Trust and Security Agreement (Second |
| 10.36.1 | Mission West Properties, L.P. First Amendment to Deed of Trust and Securit |
| 10.37 | Mission West Properties, L.P. I Deed of Trust and Security Agreement (Firs |
| 10.38 | Mission West Properties, L.P. I Deed of Trust and Security Agreement (Seco |
| 10.38.1 | Mission West Properties, L.P. I First Amendment to Deed of Trust and Secur |
| 10.39 | Mission West Properties, L.P. II Deed of Trust and Security Agreement (Fir |
| 10.40 | Mission West Properties, L.P. II Deed of Trust and Security Agreement (Sec |
| 10.40.1 | Mission West Properties, L.P. II First Amendment to Deed of Trust and Secu |
| 10.41 | Mission West Properties, L.P. Absolute Assignment of Leases and Rents (Fir |
| 10.42 | Mission West Properties, L.P. I Absolute Assignment of Leases and Rents (F |
| 10.43 | Mission West Properties, L.P. II Absolute Assignment of Leases and Rents ( |
| 10.44 | Mission West Properties L.P., L.P. I and L.P. II First Amendment to Contri |
| 10.45 | Not in use |
| 10.46* | 2004 Equity Incentive Plan (14) |
| 10.47 | Allianz Loan Secured Installment Note (15) |
| 10.48 | Allianz Loan Deed of Trust, Security Agreement, Fixture Filing with Absolu |
| 10.49 | Allianz Loan Limited Guaranty (15) |
| 10.50* | Form of Non-statutory Stock Option Agreement with Dividend Rights under 20 |
| 10.51 | Allianz Loan II Secured Installment Note (16) |
| 10.52 | Allianz Loan II Deed of Trust, Security Agreement, Fixture Filing with Ab |
| 10.53 | Allianz Loan II Limited Guaranty (16) |
| 10.54 | Allianz Loan II Loan Modification Agreement(16) |
| 10.55 | Allianz Loan II Loan Modification Agreement and Amendment of Deed of Trust |
| 21.1 | Subsidiaries of the Registrant (17) |
| 23.1 | Consent of Independent Registered Public Accounting Firm |
| 24.1 | Powers of Attorney (included on the signature page hereto) |
| 31.1 | Certification of Chief Executive Officer pursuant to Rule 13a-14(a) |
| 31.2 | Certification of Chief Operating Officer pursuant to Rule 13a-14(a) |
| 31.3 | Certification of Chief Financial Officer pursuant to Rule 13a-14(a) |
| 32.1 | Certificate Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |

*Management contract or compensatory plan or arrangement

(1) Incorporated herein by reference to the same-numbered exhibit to the Company's Registration Statement on Form S-4/A filed on July 20, 1998 and declared effective on November 23, 1998 (Commission File No. 333-52835-99).

(1a) Incorporated herein by reference to Exhibit 3.2 to the current report on Form 8-K filed December 20, 2007



(Commission File No. 000-25235).

(2) Incorporated herein by reference to the registration statement on Form 8-A/A filed March 21, 2008 (Commission File No. 001-34000).

(2a) Incorporated herein by reference to the same numbered exhibit to the registration statement on Form 8-A/A filed March 21, 2008 (Commission File No. 001-34000).

(2b) Incorporated herein by reference to the same-numbered exhibit to the Company's Post-effective Amendment No. 1 to Registration Statement on Form S-4 filed on Form S-3 on February 11, 1999 (Commission File No. 333-52835-99).

(2c) Incorporated herein by reference to Exhibit 10.8 to the Company's Post-effective Amendment No. 1 to Registration Statement on Form S-4 filed on Form S-3 on February 11, 1999 (Commission File No. 333-52835-99).

(3) Incorporated herein by reference to Exhibit E to the Company's Schedule 14A Proxy Statement filed with the Securities and Exchange Commission on October 21, 1997 (Commission File No. 001-08383).

(4a) Incorporated herein by reference to Exhibit 10.15 to the Company's Registration Statement on Form S-4/A filed on June 17, 1998 and declared effective on November 23, 1998 (Commission File No. 333-52835).

(4b) Incorporated herein by reference to Exhibit 10.17 to the Company's Registration Statement on Form S-4/A filed on June 17, 1998 and declared effective on November 23, 1998 (Commission File No. 333-52835).

(5) Incorporated herein by reference to the same-numbered exhibit to current report on Form 8-K filed on October 7, 2008 (Commission File No. 001-34000).

(6) Incorporated herein by reference to the same-numbered exhibit to the Registration Statement on Form S-4/A filed on November 16, 1998 and declared effective on November 23, 1998 (Commission File No. 333-52835-99).

(7) Incorporated herein by reference to the same numbered exhibit to the annual report on Form 10-K for 1998 filed on March 31, 1999 (Commission File No. 000-25235).

(8) Incorporated herein by reference to the same-numbered exhibit to current report on Form 8-K filed on May 14, 1999 (Commission File No. 000-25235).

(8a) Incorporated herein by reference to the same-numbered exhibit to the quarterly report on Form 10-Q filed on May 10, 2005 (Commission File No. 000-25235).

(9) Incorporated herein by reference to the same-numbered exhibit to the Registration Statement on Form S-11/A filed on June 15, 1999 (Commission File No. 333-80203).

(10) Incorporated herein by reference to the same-numbered exhibit to the quarterly report on Form 10-Q filed on November 13, 2001 (Commission File No. 000-25235).

(11) Incorporated herein by reference to the same-numbered exhibit to the quarterly report on Form 10-Q filed on August 12, 2003 (Commission File No. 000-25235).

(12) Incorporated herein by reference to the same numbered exhibit to the annual report on Form 10-K for 1999 filed on March 30, 2000 (Commission File No. 000-25235).

(13) Incorporated herein by reference to the same-numbered exhibit to the annual report on Form 10-K for 2002 filed on March 27, 2003 (Commission File No. 000-25235).

(14) Incorporated herein by reference to Appendix II to the Company's Schedule 14A Proxy Statement filed with the Securities and Exchange Commission on October 22, 2004 (Commission File No. 000-25235).

(15) Incorporated herein by reference to the same-numbered exhibit to the quarterly report on Form 10-Q filed on May 10, 2005 (Commission File No. 000-25235).

(16) Incorporated herein by reference to the same-numbered exhibit to the quarterly report on Form 10-Q filed on August 9, 2005 (Commission File No. 000-25235).

(17) Incorporated herein by reference to the same-numbered exhibit to the annual report on Form 10-K for 1998 filed on March 31, 1999 (Commission File No. 000-25235).