

WELLS REAL ESTATE INVESTMENT TRUST II INC

Form 424B3

May 16, 2007

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WELLS REAL ESTATE INVESTMENT TRUST II, INC.

SUPPLEMENT NO. 2 DATED MAY 16, 2007

TO THE PROSPECTUS DATED APRIL 24, 2007

This document supplements, and should be read in conjunction with, our prospectus dated April 24, 2007 relating to our offering of 475,000,000 shares of common stock, as supplemented by supplement no. 1 dated May 3, 2007. Capitalized terms used in this supplement have the same meanings as set forth in the prospectus. The purpose of this supplement is to disclose:

the status of our public offerings;

information regarding our indebtedness;

Management's Discussion and Analysis of Financial Condition and Results of Operations similar to that filed in our Quarterly Report on Form 10-Q for the three months ended March 31, 2007, filed on May 10, 2007; and

our unaudited financial statements as of and for the three months ended March 31, 2007.

Status of Our Public Offerings

We commenced our initial public offering of 785 million shares of common stock on December 1, 2003, which consisted of a 600 million-share primary offering and a 185 million-share offering under our dividend reinvestment plan. We stopped making offers under the primary offering on November 26, 2005. We raised gross offering proceeds of approximately \$2.0 billion from the sale of approximately 197.1 million shares in our initial public offering, including shares sold under the dividend reinvestment plan after the primary offering terminated.

On November 10, 2005, we commenced this offering of 300.6 million shares of common stock. Of these shares, we are offering 300 million shares in a primary offering and 0.6 million shares under our dividend reinvestment plan. On April 14, 2006, we amended the registration statements for this offering and our initial public offering in order to offer in a combined prospectus the 300.6 million shares registered under the follow-on offering and 174.4 million unsold shares related to the dividend reinvestment plan and registered under the initial public offering. As of May 11, 2007, we had received gross offering proceeds of approximately \$1.2 billion from the sale of approximately 126.0 million shares in this follow-on offering, including dividend reinvestment plan shares sold under the combined prospectus.

As of May 11, 2007, we had received aggregate gross offering proceeds of approximately \$3.2 billion from the sale of approximately 323.1 million shares in our public offerings. After incurring approximately \$64.4 million in acquisition fees, approximately \$300.3 million in selling commissions and dealer-manager fees, approximately \$45.0 million in other organization and offering expenses, and funding common stock redemptions of approximately \$71.7 million pursuant to the share redemption program, as of May 11, 2007, we had raised aggregate net offering proceeds available for investment in properties of approximately \$2.7 billion, substantially all of which had been invested in real estate properties.

Indebtedness

As of May 11, 2007, our leverage ratio, that is, the ratio of total debt to total purchase price of real estate assets plus cash and cash equivalents, was approximately 19%. As of May 11, 2007, total indebtedness was approximately \$633.4 million, which consisted of fixed-rate mortgages on

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certain properties of approximately \$585.7 million and a variable rate mortgage on a property of approximately \$47.7 million. We currently have no amount outstanding under our \$400.0 million line of credit with Wachovia Bank, N.A. (the Wachovia Line of Credit). Based on the value of our borrowing-base properties, we had approximately \$374.7 million in remaining capacity under the Wachovia Line of Credit, of which approximately \$2.0 million was pledged in the form of letters of credit for future tenant improvements and leasing costs.

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

The following discussion and analysis should be read in conjunction with the accompanying consolidated financial statements and notes thereto contained in this supplement no. 2, as well as our consolidated financial statements and notes thereto and Management's Discussion and Analysis of Financial Condition and Results of Operations for the year ended December 31, 2006 included in the prospectus. This discussion contains forward-looking statements, which can be identified with the use of forward-looking terminology such as *may*, *will*, *intend* or similar words. Actual results may differ from those described in forward-looking statements. For a discussion of the factors that could cause actual results to differ from those anticipated, see *Risk Factors* in the prospectus.

We commenced our initial public offering on December 1, 2003 and have received investor proceeds under this offering and our initial public offering of common stock and invested in real estate assets through March 31, 2007. Thus, our results of operations for the three months ended March 31, 2007 and 2006 reflect growing operational revenues and expenses and general and administrative expenses. Operational revenues and expenses have increased due to real property acquisitions. General and administrative expenses have increased commensurate with our overall growth, however, as a percent of total revenues, have remained stable at approximately 4% for the three months ended March 31, 2007 and 2006.

Liquidity and Capital Resources

Overview

From January 2004 through March 2007, we raised significant funds through the sale of our common stock in this offering and in our initial public offering. We primarily used the proceeds from these sales of common stock, net of offering costs and other expenses, to acquire real properties and fund certain capital improvements identified at the time of acquisition. We anticipate receiving proceeds from the sale of our common stock in this offering in the future, and investing such proceeds in future acquisitions of real properties. We also anticipate receiving proceeds from the sale of our common stock under our dividend reinvestment plan in the future, and using a significant portion of such proceeds to fund redemptions of our common stock under our share redemption program. We expect that our primary source of future operating cash flows will be cash generated from the operations of the properties currently in our portfolio and those to be acquired in the future. The amount of future dividends to be paid to our stockholders will be largely dependent upon the amount of cash generated from our operating activities, how quickly we are able to invest investor proceeds in quality income-producing assets, our expectations of future cash flows, and our determination of near-term cash needs for capital improvements, tenant re-leasing, redemptions of our common stock, and debt repayments.

The competition to acquire high-quality commercial office properties remains high. Timing differences arise between acquiring properties and raising capital and between making operating payments and collecting operating receipts. Accordingly, we may periodically be required to borrow funds on a short-term basis to meet our dividend payment schedule. Our primary focus, however, is to continue to maintain the quality of our portfolio. Thus, in this intensely competitive environment, we may opt to lower the dividend rather than compromise that quality or accumulate significant borrowings to meet a dividend level higher than operating cash flow would support. We continue to carefully monitor our cash flows and market conditions and their impact on our earnings and future dividend projections.

Short-term Liquidity and Capital Resources

During the three months ended March 31, 2007, we generated net cash flows from operating activities of approximately \$37.1 million, which is primarily comprised of receipts for rental income, tenant reimbursements, hotel income, and interest and other income, partially offset by payments for operating costs, interest expense, asset and property management fees, and general and administrative expenses. From net cash flows from operating activities and cash on hand, we paid dividends to stockholders of approximately \$43.1 million during the three months ended March 31, 2007. We generated net cash flows from financing activities of approximately \$86.3 million during the three months ended March 31, 2007, primarily as a result of raising proceeds from the sale of common stock under this offering, net of commissions, dealer-manager fees, and other offering costs, of approximately \$225.5 million, reduced by net debt repayments of approximately \$85.3 million. Such net cash flows from financing activities and cash on hand were used primarily to invest approximately \$117.0 million in real estate and pay acquisition fees of approximately \$7.9 million. We expect to utilize the residual cash balance of approximately \$43.6 million as of March 31, 2007 to satisfy current liabilities, pay future dividends, fund future acquisitions of real properties, or reduce indebtedness.

We intend to continue to generate capital from the sale of common stock in this offering and from third-party borrowings, and to use such capital primarily to fund future acquisitions of real estate. We expect that we will use a significant portion of the proceeds from sales under our dividend reinvestment plan to fund redemptions under the share redemption program. As of May 11, 2007, we had a remaining borrowing capacity of approximately \$374.7 million under

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the Wachovia Line of Credit. Accordingly, we believe that we have adequate capacity to continue to expand our portfolio and meet our future operating cash flow needs. We expect to use substantially all of our future operating cash flow, after payments for certain capital expenditures, to pay dividends to stockholders.

On March 2, 2007, our board of directors declared a daily dividend for stockholders of record from March 16, 2007 through June 15, 2007 in an amount equal to an annualized dividend of \$0.60 per share, which is consistent with the rate of dividends declared for the first quarter of 2007 and each quarter of 2006 on a per-share basis. Such dividend will be paid in June 2007.

Long-term Liquidity and Capital Resources

We expect that our primary sources of capital over the long term will include proceeds from the sale of our common stock, proceeds from secured or unsecured borrowings from third-party lenders, and net cash flows from operations. This offering, which we commenced in November 2005, was extended until the earlier of the sale of all 300.0 million shares or December 1, 2008. Thereafter, our board of directors may commence a second follow-on offering. We may continue to offer the 175.0 million dividend reinvestment plan shares beyond these dates until we have sold all of these shares through the reinvestment of dividends. We expect that our primary uses of capital will be for property acquisitions, either directly or through investments in joint ventures, tenant improvements, offering-related costs, operating expenses, including interest expense on any outstanding indebtedness, and dividends.

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

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

Contractual Commitments and Contingencies

Our contractual obligations as of March 31, 2007 will become payable in the following periods (in thousands):

Contractual Obligations	Total	2007	2008-2009	2010-2011	Thereafter
Outstanding debt obligations ⁽¹⁾	\$ 690,212	\$ 17,612	\$ 155,625	\$ 71,646	\$ 445,329
Capital lease obligations ⁽²⁾	78,000				78,000
Operating lease obligations	3,105	45	120	120	2,820
Total	\$ 771,317	\$ 17,657	\$ 155,745	\$ 71,766	\$ 526,149

(1) Amounts include principal payments only. We made interest payments of \$10.0 million during the three months ended March 31, 2007 and expect to pay interest in future periods on outstanding debt obligations based on the rates and terms disclosed in Note 4 to our consolidated financial statements for the year ended December 31, 2006 included in the prospectus and in Note 4 to our accompanying consolidated financial statements in this supplement.

(2) Amount includes principal payments only. We made interest payments of \$1.2 million during the three months ended March 31, 2007 and expect to pay interest in future periods based on the terms disclosed in Note 4 to our Consolidated Financial Statements for the year ended December 31, 2006 included in the prospectus.

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Results of Operations

Overview

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

We commenced our initial public offering on December 1, 2003. Following the receipt and acceptance of subscriptions for the minimum offering of \$2,500,000 on January 22, 2004, we acquired 18 properties during the year ended December 31, 2004, 21 properties during the year ended December 31, 2005, and 10 properties during the year ended December 31, 2006. During the three months ended March 31, 2007, we acquired two properties, bringing our total portfolio to 51 properties as of March 31, 2007. Accordingly, the results of operations presented for the three months ended March 31, 2007 and 2006, respectively, are not directly comparable.

Comparison of the three months ended March 31, 2006 versus the three months ended March 31, 2007

Rental income and tenant reimbursements increased from approximately \$56.3 million and \$12.9 million, respectively, for the three months ended March 31, 2006 to approximately \$73.6 million and \$20.3 million, respectively, for the three months ended March 31, 2007, primarily as a result of the growth in the portfolio during 2006 and the first three months of 2007. Rental income and tenant reimbursements are expected to continue to increase in future periods, as compared to historical periods, as a result of owning the assets acquired during 2006 and the first three months of 2007 for an entire period and future acquisitions of real estate assets.

Property operating costs and asset and property management fees increased from approximately \$21.5 million and \$5.9 million, respectively, for the three months ended March 31, 2006 to approximately \$30.6 million and \$7.6 million, respectively, for the three months ended March 31, 2007, primarily as a result of the growth in the portfolio during 2006 and the first three months of 2007. Property operating costs and asset and property management fees are expected to continue to increase in future periods, as compared to historical periods, due to owning the assets acquired during 2006 and the first three months of 2007 for an entire period and future acquisitions of additional real estate assets.

Depreciation of real estate increased from approximately \$10.7 million for the three months ended March 31, 2006 to approximately \$14.2 million for the three months ended March 31, 2007, primarily as a result of the growth in the portfolio during 2006 and the first three months of 2007. Depreciation is expected to continue to increase in future periods, as compared to historical periods, due to owning the assets acquired during 2006 and the first three months of 2007 for an entire period and future acquisitions of additional real estate assets.

Amortization increased from approximately \$19.5 million for the three months ended March 31, 2006 to approximately \$30.9 million for the three months ended March 31, 2007 due to the growth in the portfolio during 2006 and recognizing write-offs of unamortized lease-specific assets related to a termination of the right to lease space at 5 Houston Center of approximately \$5.2 million in the first quarter of 2007. Exclusive of the aforementioned write-off of \$5.2 million, amortization is expected to increase in future periods, as compared to historical periods, due to owning the assets acquired during 2006 and the first three months for an entire period and future acquisitions of additional real estate assets.

General and administrative expenses increased from approximately \$2.9 million for the three months ended March 31, 2006 to approximately \$3.5 million for the three months ended March 31, 2007 due to the increase in the size of our portfolio of real estate assets during 2006 and the first three months of 2007. General and administrative expenses, as a percent of total revenues, remained stable at approximately 4.0% for the three months ended March 31, 2007 and 2006.

Interest expense increased from approximately \$11.2 million for the three months ended March 31, 2006 to approximately \$11.7 million for the three months ended March 31, 2007, primarily due to new mortgage notes as well as an increase in the interest rate under our line of credit, which offset the decrease in the average balance outstanding under the line of credit. Future levels of interest expense will vary primarily based on the amounts of future borrowings and the costs of borrowings. Future borrowings will be used primarily to fund future acquisitions of real estate or interests therein. Accordingly, the amounts of future borrowings and future interest expense will largely depend on the level of additional proceeds we raise in this offering and any future offerings, the opportunities to acquire real estate assets consistent with our investment objectives, and the timing of such future acquisitions.

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We recognized a loss on early extinguishment of debt of approximately \$1.1 million during the three months ended March 31, 2006 in connection with prepaying the University Circle Buildings mortgage note in January 2006. The loss resulted from a prepayment penalty of approximately \$5.7 million and a write-off of approximately \$0.6 million in deferred financing costs, partially offset by a write-off of the unamortized fair value adjustment to debt of approximately \$5.2 million.

Interest and other income decreased from approximately \$1.8 million for the three months ended March 31, 2006 to approximately \$1.6 million for the three months ended March 31, 2007, primarily as a result of holding lower average cash balances during the three months ended March 31, 2007, as compared to the three months ended March 31, 2006, due to timing differences in raising capital in this offering and in our initial public offering and closing on property acquisitions between periods.

Net loss and net loss per share increased from approximately \$0.9 million and \$0.00, respectively, for the three months ended March 31, 2006 to approximately \$2.6 million and \$0.01, respectively, for the three months ended March 31, 2007, primarily as a result of the termination at 5 Houston Center described above, partially offset by additional income from the growth of our portfolio. We expect future real estate acquisitions to increase net income in future periods and expect future net income per share to fluctuate primarily based on the level of proceeds raised in this offering and any future offerings and the rate at which we are able to invest such proceeds in income-generating real estate assets.

Funds From Operations

Funds from operations (FFO) is a non-GAAP financial measure and should not be viewed as an alternative to net income as a measurement of our operating performance. We believe that FFO is a beneficial indicator of the performance of equity real estate investment trusts (REITs). Specifically, FFO calculations exclude factors such as depreciation and amortization of real estate assets and gains or losses from sales of operating real estate assets. As such factors can vary among owners of identical assets in similar conditions based on historical cost accounting and useful-life estimates, FFO may provide a valuable comparison of operating performance between periods and with other REITs. Management believes that accounting for real estate assets in accordance with U.S. generally accepted accounting principles (GAAP) implicitly assumes that the value of real estate assets diminishes predictably over time. Since real estate values have historically risen or fallen with market conditions, many industry investors and analysts have considered the presentation of operating results for real estate companies that use historical cost accounting to be insufficient by themselves. As a result, we believe that the use of FFO, together with the required GAAP presentation, provides a more complete understanding of our performance relative to our competitors and a more informed and appropriate basis on which to make decisions involving operating, financing, and investing activities. We calculate FFO in accordance with the current National Association of Real Estate Investment Trust (NAREIT) definition. However, other REITs may not define FFO in accordance with the NAREIT definition, or may interpret the current NAREIT definition differently than we do.

As presented below, FFO is adjusted to exclude the impact of certain noncash items, such as depreciation, amortization, and gains on the sale of real estate assets. Reconciliations of net loss to FFO are presented below (in thousands):

	For the Three Months Ended	
	March 31,	
	2007	2006
Net loss	\$ (2,610)	\$ (881)
Add:		
Depreciation of real assets	14,194	10,678
Amortization of lease-related costs	30,905	19,470
FFO	\$ 42,489	\$ 29,267
Weighted-average common shares outstanding	291,017	206,104

Set forth below is additional information related to certain cash and noncash items included in or excluded from net loss above, which may be helpful in assessing our operating results. In addition, cash flows generated from FFO may be used to fund all or a portion of certain capitalizable items that are excluded from FFO, such as capitalized interest, tenant improvements, building improvements, and deferred lease costs. Please see the accompanying consolidated statements of cash flows for detail of our operating, investing, and financing cash activities.

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Noncash Items Included in Net Loss:

Straight-line rental revenue of approximately \$5.0 million and \$5.8 million was recognized for the three months ended March 31, 2007 and 2006, respectively;

Amortization of above-market/below-market in-place leases and lease incentives was recognized as net decreases to rental income of approximately \$4.6 million and \$2.9 million for the three months ended March 31, 2007 and 2006, respectively;

Amortization of deferred financing costs, discounts on notes payable, and interest accrued into the basis of notes payable of approximately \$1.3 million and \$0.5 million was recognized as interest expense for the three months ended March 31, 2007 and 2006, respectively;

Approximately \$1.1 million was recognized as a loss on early extinguishment of debt for the three months ended March 31, 2006 in connection with prepayment of the University Circle Buildings mortgage note during January 2006; and

Cash Item Excluded from Net Loss:

Master lease proceeds relating to previous acquisitions of approximately \$0.2 million and \$0.2 million were collected during the three months ended March 31, 2007 and 2006, respectively. Master lease proceeds are recorded as an adjustment to the basis of real estate assets during the period acquired and, accordingly, are not included in net loss or FFO. We consider master lease proceeds when determining cash available for dividends to our stockholders.

Election as a REIT

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

Wells TRS II, LLC (Wells TRS) is our wholly owned subsidiary. Wells TRS is organized as a Delaware limited liability company and includes the operations of, among other things, a full-service hotel. We have elected to treat Wells TRS as a taxable REIT subsidiary. We may perform additional, non-customary services for tenants of buildings that we own through Wells TRS, including any real estate or non-real estate related services; however, any earnings related to such services are subject to federal and state income taxes. In addition, for us to continue to qualify as a REIT, our investments in taxable REIT subsidiaries cannot exceed 20% of the value of our total assets. Deferred tax assets and liabilities are established for temporary differences between the financial reporting basis and the tax basis of assets and liabilities at the enacted rates expected to be in effect when the temporary differences reverse.

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

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

Application of Critical Accounting Policies

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

Investment in Real Estate Assets

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

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

Allocation of Purchase Price of Acquired Assets

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

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

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

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

consolidated balance sheets and are amortized to expense over the remaining terms of the respective leases.

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

Valuation of Real Estate Assets

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

Projections of expected future operating cash flows require that we estimate future market rental income amounts subsequent to the expiration of current lease agreements, property operating expenses, the number of months it takes to re-lease the property, and the number of years the property is held for investment, among other factors. The subjectivity of assumptions used in the future cash flow analysis, including discount rates, could result in an incorrect assessment of the property's fair value and could result in the misstatement of the carrying value of our real estate and related intangible assets and net income.

Related-Parties

Transactions and Agreements

We have entered into agreements with our advisor, Wells Capital, Inc. (*Wells Capital*), and its affiliates, whereby we pay certain fees and reimbursements to Wells Capital or its affiliates, for acquisition fees, commissions, dealer-manager fees, asset and property management fees, construction fees, reimbursement of organizational and offering costs, and reimbursement of operating costs. See Note 7 to our accompanying consolidated financial statements included herein for a discussion of the various related-party transactions, agreements, and fees.

Our Relationship with Wells REIT and the Impact of Its Internalization Transaction on Us

Wells Real Estate Investment Trust, Inc. (*Wells REIT*) is a separate REIT from us that also was sponsored by Wells Real Estate Funds, Inc. (*WREF*), our sponsor and the sole stockholder of Wells Capital, Wells Investment Securities, Inc. (*WIS*), and Wells Management Company, Inc. (*Wells Management*). Prior to April 16, 2007, we and Wells REIT shared a common advisor, Wells Capital, and a common property manager, Wells Management. We also shared with Wells REIT all of the same executive officers and many of the same directors, except that we had separate presidents from February 2, 2007, which is the date that Wells REIT entered into the merger agreement relating to the internalization transaction described below.

On April 16, 2007, Wells REIT acquired entities affiliated with WREF. Wells REIT entered into the merger in order to internalize advisory, asset management, property management, and other services previously provided to Wells REIT by WREF and its affiliates. As a result of the internalization transaction, 81 employees of WREF and its affiliates became employees of Wells REIT. A majority of those employees did not previously provide significant services to us. Following the internalization transaction, WREF and its affiliates have 351 employees. WREF and its affiliates are seeking successors to some of the personnel who had provided services to us and became employees of Wells REIT in the internalization transaction.

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Some of the personnel acquired by Wells REIT in the internalization had primary responsibility for the management of six of our properties. To ensure continuity of property management services, we amended our existing Master Property Management, Leasing, and Construction Agreement with Wells Management to eliminate the provision of property management services for those six properties effective upon consummation of the Wells REIT internalization transaction. We also entered into a property management agreement with a subsidiary of Wells REIT to provide property management services to us for the six properties. Wells Management and unaffiliated third parties, however, will continue to provide leasing services for the six properties. The terms of our agreement with Wells REIT for property management services are substantially similar to the terms under which we engage Wells Management for property management services.

In connection with the Wells REIT internalization transaction, all three of our officers resigned from their officer positions with Wells REIT, four of our board members resigned from their positions as board members of Wells REIT, and two Wells REIT directors resigned from our board. On May 9, 2007, Leo F. Wells, III resigned as chairman of the board of directors of Wells REIT. As a result, we and Wells REIT share no common officers and no common directors.

On April 18, 2007, E. Nelson Mills became one of our independent directors. He is also an independent director of Institutional REIT, Inc. and Wells Timberland REIT, Inc. Since December 2004, Mr. Mills has served as the chief operations officer and chief financial officer of Williams Realty Advisors, LLC, where he is responsible for investment and financial strategy and is in charge of the design, formation, and operation of a series of real estate investment funds. From April 2004 to December 2004, Mr. Mills was a financial consultant to Timbervest, LLC, an investment manager specializing in timberland investments. From September 2000 to April 2004, Mr. Mills served as chief financial officer of Lend Lease Real Estate Investments (US), Inc., an investment manager specializing in the acquisition and management of commercial real estate, and from August 1998 to August 2000 served as a senior vice president of Lend Lease with responsibility for tax planning and administration and the supervision of various merger and acquisition activities. Prior to joining Lend Lease, Mr. Mills was a tax partner with KPMG LLP from January 1987 to August 1998. Mr. Mills received a Bachelor of Science degree in Business Administration from the University of Tennessee and a Master's of Business Administration degree from the University of Georgia. Mr. Mills is also a Certified Public Accountant.

Legal Action Against Related-Parties

On March 12, 2007, a stockholder of Wells REIT filed a purported class action and derivative complaint, *Washtenaw County Employees Retirement System v. Wells Real Estate Investment Trust, Inc., et al.* in the United States District Court for the District of Maryland against, among others, Wells REIT, our advisor, certain affiliates of WREF, and certain of our officers and directors who formerly served as officers and directors of Wells REIT prior to the closing of the internalization transaction on April 16, 2007. The complaint alleges violations of the federal proxy rules and breaches of fiduciary duty arising from the Wells REIT internalization transaction and the related proxy statement filed with the Securities and Exchange Commission on February 26, 2007, as amended. The complaint seeks, among other things, unspecified monetary damages. On April 9, 2007, the District Court denied the plaintiff's motion for an order enjoining the internalization transaction. On April 17, 2007, the Court granted the defendants' motion to transfer venue to the Northern District of Georgia, and the case was docketed in the Northern District of Georgia on April 24, 2007. Our advisor and officers and directors who are named in the complaint intend to vigorously defend this action. Any financial loss incurred by Wells Capital or its affiliates could hinder their ability to successfully manage our operations and our portfolio of investments.

Commitments and Contingencies

We are subject to certain commitments and contingencies with regard to certain transactions. Refer to Note 5 of our accompanying consolidated financial statements in this supplement for further explanation. Examples of such commitments and contingencies include:

Commitments under existing lease agreements; and

Litigation.

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(in thousands, except share and per-share amounts)

	(Unaudited)	
	March 31,	December 31,
	2007	2006
Assets:		
Real estate assets, at cost:		
Land	\$ 384,308	\$ 370,971
Buildings and improvements, less accumulated depreciation of \$93,198 and \$79,175 as of March 31, 2007 and December 31, 2006, respectively	1,973,865	1,922,523
Intangible lease assets, less accumulated amortization of \$123,519 and \$106,147 as of March 31, 2007 and December 31, 2006, respectively	463,285	458,917
Construction in progress	873	420
Total real estate assets	2,822,331	2,752,831
Cash and cash equivalents	43,624	46,100
Tenant receivables, net of allowance for doubtful accounts of \$1,605 and \$1,548 as of March 31, 2007 and December 31, 2006, respectively	60,148	53,372
Prepaid expenses and other assets	36,099	35,554
Deferred financing costs, less accumulated amortization of \$1,834 and \$1,535 as of March 31, 2007 and December 31, 2006, respectively	2,861	3,184
Deferred lease costs, less accumulated amortization of \$62,638 and \$52,906 as of March 31, 2007 and December 31, 2006, respectively	314,243	319,184
Investment in bonds	78,000	78,000
Total assets	\$ 3,357,306	\$ 3,288,225
Liabilities:		
Line of credit and notes payable	\$ 690,212	\$ 774,523
Accounts payable, accrued expenses, and accrued capital expenditures	35,780	41,817
Due to affiliates	3,662	13,977
Dividends payable	7,924	7,317
Deferred income	12,309	9,138
Intangible lease liabilities, less accumulated amortization of \$12,777 and \$10,638 as of March 31, 2007 and December 31, 2006, respectively	89,895	92,343
Obligations under capital leases	78,000	78,000
Total liabilities	917,782	1,017,115
Commitments and Contingencies		
Minority Interest	3,094	3,090
Redeemable Common Stock	12,563	
Stockholders Equity:		
Common stock, \$0.01 par value; 900,000,000 shares authorized; 304,020,721 and 280,119,233 shares issued and outstanding as of March 31, 2007 and December 31, 2006, respectively	3,040	2,801
Additional paid-in capital	2,706,767	2,491,817

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Cumulative distributions in excess of earnings	(272,257)	(225,549)
Redeemable common stock	(12,563)	
Other comprehensive loss	(1,120)	(1,049)
Total stockholders' equity	2,423,867	2,268,020
Total liabilities, minority interest, redeemable common stock, and stockholders' equity	\$ 3,357,306	\$ 3,288,225

See accompanying notes.

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WELLS REAL ESTATE INVESTMENT TRUST II, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per-share amounts)

	(Unaudited)	
	Three Months Ended March 31,	
	2007	2006
Revenues:		
Rental income	\$ 73,577	\$ 56,285
Tenant reimbursements	20,291	12,914
Hotel income	4,554	4,369
	98,422	73,568
Expenses:		
Property operating costs	30,638	21,500
Hotel operating costs	4,027	3,787
Asset and property management fees:		
Related-party	6,222	4,708
Other	1,411	1,147
Depreciation	14,194	10,678
Amortization	30,905	19,470
General and administrative	3,491	2,918
	90,888	64,208
Real estate operating income		