American Assets Trust, Inc.
Form 10-Q
August 12, 2011

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended June 30, 2011

or

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from ______ to ______

Commission file number: 001-35030

AMERICAN ASSETS TRUST, INC.

(Exact Name of Registrant as Specified in its charter)

Maryland	**27-3338708**
(State of Organization)	**(IRS Employer Identification No.)**
11455 El Camino Real, Suite 200, San Diego, California	**92130**
(Address of Principal Executive Offices)	**(Zip Code)**

(858) 350-2600

(Registrant s Telephone Number, Including Area Code)

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. x Yes ¨ No

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). x Yes ¨ No

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer ¨	Accelerated Filer ¨
Non-Accelerated Filer x (Do not check if a smaller reporting company)	Smaller reporting company ¨

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

The number of Registrant s common shares outstanding on August 12, 2011 was 39,283,796.

AMERICAN ASSETS TRUST, INC.

QUARTERLY REPORT ON FORM 10-Q

FOR THE QUARTER ENDED JUNE 30, 2011

American Assets Trust, Inc.

Consolidated Balance Sheets

(In Thousands, Except Share Data)

	June 30, 2011 (unaudited)	December 31, 2010 (audited)
Assets		
Real estate, at cost		
Operating real estate	$ 1,633,287	$ 1,156,091
Construction in progress	1,144	925
Held for development	8,756	8,081
	1,643,187	1,165,097
Accumulated depreciation	(240,603)	(221,997)
Net real estate	1,402,584	943,100
Cash and cash equivalents	92,535	41,953
Restricted cash	8,077	4,729
Marketable securities	31,445	
Accounts receivable, net	4,944	1,573
Deferred rent receivables, net	21,665	20,051
Notes receivable from affiliate		21,769
Investment in real estate joint ventures		39,816
Prepaid expenses and other assets	69,915	44,366
Purchase deposits	91,600	
Total assets	$ 1,722,765	$ 1,117,357
Liabilities and equity		
Liabilities:		
Secured notes payable	$ 944,279	$ 851,547
Unsecured notes payable		38,013
Notes payable to affiliates		5,266
Accounts payable and accrued expenses	20,007	11,644
Security deposits payable	4,302	2,648
Other liabilities and deferred credits	56,922	39,058
Distributions in excess of earnings on real estate joint ventures		14,060
Total liabilities	1,025,510	962,236
Commitments and contingencies (Note 11)		
Equity:		
Owners equity		121,874
American Assets Trust, Inc. stockholders equity		
Common stock $0.01 par value, 490,000,000 authorized, 39,281,839 outstanding at June 30, 2011	393	
Additional paid-in capital	652,220	
Accumulated deficit	(15,168)	
Total American Assets Trust, Inc. stockholders equity	637,445	
Noncontrolling interests		
Owners in consolidated real estate entities		33,247

Unitholders in the Operating Partnership	59,810	
	59,810	33,247
Total equity	697,255	155,121
Total liabilities and equity	$ 1,722,765	$ 1,117,357

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

American Assets Trust, Inc.

Consolidated Statements of Operations

(Unaudited)

(In Thousands, Except Shares and Per Share Data)

	Three Months Ended June 30, 2011	Three Months Ended June 30, 2010	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
Revenue:				
Rental income	$ 49,794	$ 28,414	$ 95,913	$ 56,509
Other property income	2,485	873	4,402	1,710
Total revenue	52,279	29,287	100,315	58,219
Expenses:				
Rental expenses	14,572	4,870	27,039	9,864
Real estate taxes	5,617	2,992	9,666	5,948
General and administrative	3,825	1,821	7,064	3,408
Depreciation and amortization	14,277	7,509	26,767	14,739
Total operating expenses	38,291	17,192	70,536	33,959
Operating income	13,988	12,095	29,779	24,260
Interest expense	(14,063)	(10,624)	(27,142)	(21,278)
Early extinguishment of debt			(25,867)	
Loan transfer and consent fees			(9,019)	
Gain on acquisition		4,297	46,371	4,297
Other income (expense), net	530	71	(71)	(916)
Net income	455	5,839	14,051	6,363
Net income attributable to restricted shares	(132)		(218)	
Net loss attributable to Predecessor s noncontrolling interests in consolidated real estate entities		469	2,458	899
Net income attributable to Predecessor s controlled owners equity		(6,308)	(16,995)	(7,262)
Net (income) loss attributable to unitholders in the Operating Partnership	(104)		225	
Net income (loss) attributable to American Assets Trust, Inc. stockholders	$ 219	$	$ (479)	$
Net income (loss) attributable to common stockholders per share basic	$ 0.01		$ (0.01)	
Net income (loss) attributable to common stockholders per share diluted	$ 0.01		$ (0.01)	
Weighted average shares of common stock outstanding basic	38,655,084		34,810,932	
Weighted average shares of common stock outstanding diluted	57,051,173		34,810,932	
Dividends declared per common share	$ 0.21		$ 0.38	

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

American Assets Trust, Inc.

Consolidated Statements of Equity

(Unaudited)

(In Thousands, Except Share Data)

	American Assets Trust, Inc. Stockholders Equity Common Shares					Noncontrolling Interests - Unitholders in the Operating Partnership	Predecessor s Noncontrolling Interests - Owners in Consolidated Entities	
	Shares	Amount	Additional Paid-in Capital	Accumulated Deficit	Predecessor s Controlled Owners Equity			Total
Balance at December 31, 2010		$	$	$	$ 121,874	$	$ 33,247	$ 155,121
Net income (loss)				(261)	16,995	(225)	(2,458)	14,051
Distributions					(33,435)		(6,525)	(39,960)
Proceeds from sale of common stock, net	31,625,000	316	587,695					588,011
Cash paid to non-accredited investors							(6,075)	(6,075)
Issuance of restricted stock	628,706	6	(6)					
Forfeiture of restricted stock	(1,951)							
Issuance of common shares and units for acquisition of properties	262,486	3	6,081			27,770		33,854
Proceeds from private placement						5,410		5,410
Notes receivable from affiliate settled in common units						(21,797)		(21,797)
Notes payable to affiliates settled in common units						828		828
Dividends declared and paid				(14,907)		(6,991)		(21,898)
Stock-based compensation			1,190					1,190
Distribution of investment in joint venture not acquired					(9,084)		(2,396)	(11,480)
Exchange of owners equity for common stock and units	6,767,598	68	57,260		(96,350)	54,815	(15,793)	
Balance at June 30, 2011	39,281,839	$ 393	$ 652,220	$ (15,168)	$	$ 59,810	$	$ 697,255

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

American Assets Trust, Inc.

Consolidated Statements of Cash Flows

(Unaudited)

(In Thousands)

	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
OPERATING ACTIVITIES		
Net income	$ 14,051	$ 6,363
Adjustments to reconcile net income to net cash provided by operating activities:		
Deferred rent revenue and amortization of lease intangibles	(731)	361
Depreciation and amortization	26,767	14,739
Amortization of debt issuance costs and debt fair value adjustments	1,895	317
Early extinguishment of debt	25,867	
Loan transfer and consent fees	9,019	
Gain on acquisition of controlling interests	(46,371)	(4,297)
Stock-based compensation expense	1,190	
Loss from real estate joint ventures	188	2,890
Distribution of earnings from real estate joint ventures		3,354
Other, net	935	254
Changes in operating assets and liabilities		
Change in restricted cash	(211)	(47)
Change in accounts receivable	(1,510)	944
Change in prepaid expenses and other assets	112	653
Change in accounts payable and accrued expenses	(1,467)	(488)
Change in security deposits and other liabilities	(1,027)	(35)
Net cash provided by operating activities	28,707	25,008
INVESTING ACTIVITIES		
Acquisition of real estate, net of cash acquired	(128,877)	(19,718)
Deposit on property acquisition	(91,600)	
Capital expenditures	(2,814)	(2,351)
Change in restricted cash	(1,359)	16
Cash acquired from acquisition of controlling interests in real estate joint ventures	15,222	
Leasing commissions	(871)	(776)
Purchase of marketable securities	(33,103)	
Maturity of marketable securities	1,710	
Distribution of capital from real estate joint ventures		10,607
Issuance of notes receivable to affiliate		(800)
Net cash used in investing activities	(241,692)	(13,022)
FINANCING ACTIVITIES		
Issuance of secured notes payable	84,500	7,500
Repayment of secured notes payable	(262,003)	(9,053)
Defeasance costs on repayment of secured notes payable	(24,345)	
Loan transfer and consent fees paid	(8,350)	
Issuance of unsecured notes payable		23,000
Repayment of unsecured notes payable	(38,013)	(2,382)
Repayment of notes payable to affiliates	(19,279)	(1,171)

Debt issuance costs	(2,961)	(365)
Proceeds from issuance of common stock, net	596,541	
Proceeds from private placement of common units	5,410	
Dividends paid to common stock and unitholders	(21,898)	
Payments to nonaccredited investors	(6,075)	
Distributions to Predecessor s controlling and non-controlling interests	(39,960)	(22,112)
Net cash provided by (used in) financing activities	263,567	(4,583)
Net increase in cash and cash equivalents	50,582	7,403
Cash and cash equivalents, beginning of period	41,953	24,189
Cash and cash equivalents, end of period	$ 92,535	$ 31,592

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

American Assets Trust, Inc.

Notes to Consolidated Financial Statements

June 30, 2011

(Unaudited)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Business and Organization

American Assets Trust, Inc. (which may be referred to in these financial statements as the Company, we, us, or our) is a Maryland corporation formed on July 16, 2010 that did not have any operating activity until the consummation of our initial public offering (the Offering) and the related acquisition of certain assets of our Predecessor (as defined below) on January 19, 2011. The Company is the sole general partner of American Assets Trust, L.P., a Maryland limited partnership formed on July 16, 2010 (the Operating Partnership). The Company s operations are carried on through our Operating Partnership and its subsidiaries, including our taxable REIT subsidiary. Since the formation of our Operating Partnership, the Company has controlled our Operating Partnership as its general partner and has consolidated its assets, liabilities and results of operations.

In connection with the Offering, on January 19, 2011 the following transactions were completed:

- We issued a total of 31,625,000 shares of our common stock at $20.50 per share.

- We acquired, through a series of merger and contribution transactions (the Formation Transactions, as more fully described below), certain assets of our Predecessor and certain other entities. In exchange for such assets, the prior investors in such assets that were accredited investors were issued a total of 7,030,084 shares of our common stock and 18,145,039 common units of limited partnership interests in our Operating Partnership (common units), with an aggregate value of approximately $516.1 million, and non-accredited prior investors were paid a total of approximately $6.1 million in cash from the net proceeds of the Offering.

- We entered into a $250.0 million revolving credit facility (the credit facility) with an accordion feature to increase availability to $400.0 million under specified circumstances.

- We repaid $342.0 million of indebtedness (including $24.3 million of defeasance costs) and paid $10.8 million, net of $0.7 million prepaid by our Predecessor, for loan transfer and consent fees and credit facility origination fees from the net proceeds of the Offering.

The net proceeds from the Offering were approximately $594.6 million, net of $1.9 million of offering costs prepaid by our Predecessor, including the underwriters overallotment option which was exercised in full (after deducting the underwriting discount and commissions and expenses of the Offering and Formation Transactions). We contributed the net proceeds of the Offering to our Operating Partnership in exchange for common units.

Our Predecessor is not a legal entity but rather a combination of entities whose assets included entities owned and/or controlled by Ernest S. Rady and his affiliates, including the Ernest Rady Trust U/D/T March 13, 1983 (the Rady Trust), which in turn owned (1) controlling interests in entities owning 17 properties and the property management business of American Assets, Inc. (AAI) (the controlled entities), and (2) noncontrolling interests in entities owning four properties (the noncontrolled entities) (the assets described at (1) and (2) are the Acquired Assets, and do not include our Predecessor s noncontrolling 25% ownership interest in Novato FF Venture, LLC, the entity that owns the Fireman s Fund Headquarters in Novato, California). The Formation Transactions included the acquisition by our Operating Partnership of the (a) Acquired Assets, (b) the entities that own Waikiki Beach Walk (a mixed-used property consisting of a retail portion and a hotel portion) (the Waikiki Beach Walk entities) and (c) the entities that own Solana Beach Towne Centre and Solana Beach Corporate Centre (the Solana Beach Centre entities) (including our Predecessor s ownership interest in these entities).

The Formation Transactions enabled us to (1) consolidate the ownership of our property portfolio under our Operating Partnership, (2) succeed to the property management business of AAI, (3) facilitate the Offering, and (4) qualify as a real estate investment trust (a REIT) for U.S. federal income tax purposes commencing with the taxable year ending December 31, 2011. As a result of the Formation Transactions, we are a vertically integrated and self-administered REIT with approximately 110 employees providing substantial in-house expertise in asset management, property management, property development, leasing, tenant improvement construction, acquisitions, repositioning, redevelopment and financing.

American Assets Trust, Inc.

Notes to Consolidated Financial Statements (Continued)

June 30, 2011

(Unaudited)

We determined that our Predecessor was the acquirer for accounting purposes, and therefore the contribution or acquisition by merger of interests in the controlled entities was considered a transaction between entities under common control since our Executive Chairman, Ernest S. Rady or his affiliates, including the Rady Trust, owned the controlling interest in each of the entities comprising our Predecessor, which, in turn, owned a controlling interest in each of the controlled entities. As a result, the acquisition of interests in each of the controlled entities was recorded at our historical cost. The contribution or acquisition by merger of interests in certain of the noncontrolled entities, which include the Waikiki Beach Walk entities and the Solana Beach Centre entities (including our Predecessor s ownership interest in these noncontrolled entities), was accounted for as an acquisition under the acquisition method of accounting and recognized at the estimated fair value of acquired assets and assumed liabilities on the date of such contribution or acquisition.

Since these transactions occurred on January 19, 2011, the financial condition and results of operations for the entities acquired by us in connection with the Offering and related Formation Transactions are not included in certain historical financial statements. More specifically, our financial condition as of December 31, 2010 and results of operations for the six months ended June 30, 2010 reflect the financial condition and results of operations for our Predecessor. Our financial condition as of June 30, 2011 and results of operations for the six months ended June 30, 2011 reflect the financial condition and results of operation for our Predecessor together with the entities we acquired at the time of the Offering, namely, the Waikiki Beach Walk entities and the Solana Beach Centre entities, and the First & Main property acquired subsequent to the Offering in March 2011. We have included the results of operations for the acquired entities in our consolidated statements of operations from the date of acquisition.

Prior to the Offering, the Predecessor s combined financial statements included investments in certain real estate joint ventures in which Ernest Rady and his affiliates had significant influence, but not control, over major decisions, including the decision to sell or refinance the properties. These investments, which represent non-controlling 25% to 80% ownership interests, were accounted for using the equity method of accounting. The Predecessor s investments in certain real estate joint ventures for which it had unilateral control, evidenced by the ability to make all major decisions, such as the acquisition, sale or refinancing of the property without approval of the minority party, were combined in these financial statements as they were under the common control of Ernest Rady and his affiliates.

As of June 30, 2011, we owned or had a controlling interest in 21 office, retail, multifamily and mixed-use operating properties, the operations of which we consolidate. A summary of the properties owned by us is as follows:

Retail

Carmel Country Plaza

Carmel Mountain Plaza

South Bay Marketplace

Rancho Carmel Plaza

Lomas Santa Fe Plaza

Solana Beach Towne Centre

Del Monte Center

The Shops at Kalakaua

Waikele Center

Alamo Quarry Market

Office

Torrey Reserve Campus

Solana Beach Corporate Centre

Valencia Corporate Center

160 King Street

The Landmark at One Market

First & Main

Multifamily

Loma Palisades

Imperial Beach Gardens

Mariner s Point

Santa Fe Park RV Resort

American Assets Trust, Inc.

Notes to Consolidated Financial Statements (Continued)

June 30, 2011

(Unaudited)

Mixed-Use

Waikiki Beach Walk Retail and Hotel

Basis of Presentation

Our consolidated financial statements include the accounts of the Company, our Operating Partnership and our subsidiaries. The equity interests of other investors in our Operating Partnership are reflected as noncontrolling interests. The combined financial statements of our Predecessor include the accounts of our Predecessor and all entities in which our Predecessor had a controlling interest. When our Predecessor was the general partner or managing member of a limited partnership or limited liability company, as the case may be, our Predecessor was presumed to control the limited partnership or limited liability company unless the limited partners or non-managing members possessed or possess either (1) the substantive ability to dissolve the partnership or otherwise remove our Predecessor as the general partner or managing member without cause (commonly referred to as kick-out rights), or (2) the right to participate in substantive operating and financial decisions of the limited partnership or limited liability company that were expected to be made in the course of their business. The equity interests of other investors were reflected as noncontrolling interests. Our Predecessor accounted for its interests in joint ventures which it did not control using the equity method of accounting.

All significant intercompany transactions and balances are eliminated in consolidation.

The accompanying consolidated financial statements of the Company have been prepared in accordance with the rules applicable to Form 10-Q and include all information and footnotes required for interim financial statement presentation, but do not include all disclosures required under accounting principles generally accepted in the United States (GAAP) for annual financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments, except as otherwise noted) considered necessary for a fair presentation have been included.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that in certain circumstances affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities, and revenues and expenses. These estimates are prepared using management s best judgment, after considering past, current and expected events and economic conditions. Actual results could differ from these estimates.

Consolidated Statements of Cash Flows Supplemental Disclosures

The following table provides supplemental disclosures related to the Consolidated Statements of Cash Flows (in thousands):

	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
Supplemental cash flow information		
Cash paid for interest	$ 25,747	$ 21,165
Supplemental schedule of noncash investing and financing activities		
Accounts payable and accrued liabilities for property under development	$ 828	$ 804
Assumption of debt upon acquisition (Note 2)	$ 268,008	$ 133,000

Assumption of notes to affiliates upon acquisition (Note 2)	$	14,824	$	
Acquisition of working capital deficit, net of cash (Note 2)	$	(3,036)	$	(1,972)
Distribution of investment in joint venture not acquired	$	11,480	$	
Issuance of common shares and units for acquisition of properties	$	33,854	$	
Notes receivable from affiliate settled in common units	$	21,797	$	
Notes payable to affiliates settled in common units	$	828	$	
Reduction to capital for prepaid Offering costs	$	1,974	$	
Transfer taxes accrued at time of Offering	$	6,556	$	

American Assets Trust, Inc.

Notes to Consolidated Financial Statements (Continued)

June 30, 2011

(Unaudited)

Offering Costs

In connection with the Offering, affiliates incurred legal, accounting and related costs, which were assumed or reimbursed by the Company upon the consummation of the Offering and such costs were deducted from the gross proceeds of the Offering.

Revenue Recognition and Accounts Receivable

Our leases with tenants are classified as operating leases. Substantially all such leases contain fixed rent escalations which occur at specified times during the term of the lease. Base rents are recognized on a straight-line basis from when the tenant controls the space through the term of the related lease, net of valuation adjustments, based on management s assessment of credit, collection and other business risks. Percentage rents, which represent additional rents based upon the level of sales achieved by certain tenants, are recognized at the end of the lease year or earlier if we have determined the required sales level is achieved and the percentage rents are collectible. Real estate tax and other cost reimbursements are recognized on an accrual basis over the periods in which the related expenditures are incurred. Other property income includes parking income, general excise tax billed to tenants and fees charged to tenants at our multifamily properties. Other property income is recognized when earned. For a tenant to terminate its lease agreement prior to the end of the agreed term, we may require that they pay a fee to cancel the lease agreement. Lease termination fees for which the tenant has relinquished control of the space are generally recognized on the termination date. When a lease is terminated early but the tenant continues to control the space under a modified lease agreement, the lease termination fee is generally recognized evenly over the remaining term of the modified lease agreement.

We recognize revenue on the hotel portion of our mixed-use property from the rental of hotel rooms and guest services when the rooms are occupied and services have been provided. Food and beverage sales are recognized when the customer has been served or at the time the transaction occurs. Revenue from room rental is included in rental revenue on the statement of operations. Revenue from other sales and services provided is included in other property income on the statement of operations.

We make estimates of the collectibility of our accounts receivable related to minimum rents, straight-line rents, expense reimbursements and other revenue. Accounts receivable and deferred rent receivable are carried net of this allowance for doubtful accounts. We generally do not require collateral or other security from our tenants, other than letters of credit or security deposits. Our determination as to the collectibility of accounts receivable and correspondingly, the adequacy of this allowance, is based primarily upon evaluations of individual receivables, current economic conditions, historical experience and other relevant factors. The allowance for doubtful accounts is increased or decreased through bad debt expense. In some cases, primarily relating to straight-line rents, the collection of these amounts extends beyond one year. Our experience relative to unbilled straight-line rents is that a portion of the amounts otherwise recognizable as revenue is never billed to or collected from tenants due to early lease terminations, lease modifications, bankruptcies and other factors. Accordingly, the extended collection period for straight-line rents along with our evaluation of tenant credit risk may result in the nonrecognition of a portion of straight-line rental income until the collection of such income is reasonably assured. If our evaluation of tenant credit risk changes indicating more straight-line revenue is reasonably collectible than previously estimated and realized, the additional straight-line rental income is recognized as revenue. If our evaluation of tenant credit risk changes indicating a portion of realized straight-line rental income is no longer collectible, a reserve and bad debt expense is recorded. At June 30, 2011 and December 31, 2010, our allowance for doubtful accounts was $2.0 million and $1.0 million, respectively.

We recognize gains on sales of properties upon the closing of the transaction with the purchaser. Gains on properties sold are recognized using the full accrual method when (1) the collectibility of the sales price is reasonably assured, (2) we are not obligated to perform significant activities after the sale, (3) the initial investment from the buyer is sufficient and (4) other profit recognition criteria have been satisfied. Gains on sales of properties may be deferred in whole or in part until the requirements for gain recognition have been met.

We receive various fee income from unconsolidated real estate joint ventures including property management fees, construction management fees, acquisition and disposition fees, leasing fees, asset management fees and financing fees. Fee income is recorded as earned in accordance with the respective fee agreement. Profit from these fees, if any, is eliminated to the extent of our ownership interest in these entities. Subsequent to the Formations Transactions and the acquisition of the outside interests in unconsolidated joint ventures, we no longer earn fee revenue (Note

15).

American Assets Trust, Inc.

Notes to Consolidated Financial Statements (Continued)

June 30, 2011

(Unaudited)

Real Estate

Land, buildings and improvements are recorded at cost. Depreciation is computed using the straight-line method. Estimated useful lives range generally from 30 years to a maximum of 40 years on buildings and major improvements. Minor improvements, furniture and equipment are capitalized and depreciated over useful lives ranging from 3 years to 15 years. Maintenance and repairs that do not improve or extend the useful lives of the related assets are charged to operations as incurred. Tenant improvements are capitalized and depreciated over the life of the related lease or their estimated useful life, whichever is shorter. If a tenant vacates its space prior to the contractual termination of its lease, the undepreciated balance of any tenant improvements are written off if they are replaced or have no future value. For the six months ended June 30, 2011 and 2010, real estate depreciation expense was $19.9 million and $12.6 million, respectively.

Acquisitions of properties are accounted for in accordance with the authoritative accounting guidance on acquisitions and business combinations. Our methodology of allocating the cost of acquisitions to assets acquired and liabilities assumed is based on estimated fair values, replacement cost and appraised values. When we acquire operating real estate properties, the purchase price is allocated to land and buildings, intangibles such as in-place leases, and to current assets and liabilities acquired, if any. Such valuations include a consideration of the non-cancellable terms of the respective leases as well as any applicable renewal periods. The fair values associated with below market renewal options are determined based on a review of several qualitative and quantitative factors on a lease-by-lease basis at acquisition to determine whether it is probable that the tenant would exercise its option to renew the lease agreement. These factors include: (1) the type of tenant in relation to the property it occupies, (2) the quality of the tenant, including the tenant s long term business prospects and (3) whether the fixed rate renewal option was sufficiently lower than the fair rental of the property at the date the option becomes exercisable such that it would appear to be reasonably assured that the tenant would exercise the option to renew. The value allocated to in-place leases is amortized over the related lease term and reflected as depreciation and amortization in the statement of operations. The value of above and below market leases associated with the original noncancelable lease terms are amortized to rental income over the terms of the respective non-cancelable lease periods and are reflected as either an increase (for below market leases) or a decrease (for above market leases) to rental income in the statement of operations. The value of the leases associated with below market lease renewal options that are likely to be exercised are amortized to rental income over the respective renewal periods. If a tenant vacates its space prior to contractual termination of its lease or the lease is not renewed, the unamortized balance of any in-place lease value is written off to rental income and amortization expense. Acquisition-related expenses are expensed in the period incurred.

We capitalize certain costs related to the development and redevelopment of real estate including pre-construction costs, real estate taxes, insurance and construction costs and salaries and related costs of personnel directly involved. Additionally, we capitalize interest costs related to development and significant redevelopment activities. Capitalization of these costs begins when the activities and related expenditures commence and cease when the project is substantially complete and ready for its intended use, at which time the project is placed in service and depreciation commences. Additionally, we make estimates as to the probability of certain development and redevelopment projects being completed. If we determine that the completion of development or redevelopment is no longer probable, we expense all capitalized costs which are not recoverable.

Impairment of Long Lived Assets

We review for impairment on a property by property basis. Impairment is recognized on properties held for use when the expected undiscounted cash flows for a property are less than its carrying amount at which time the property is written-down to fair value. Properties held for sale are recorded at the lower of the carrying amount or the expected sales price less costs to sell. The sale or disposal of a component of an entity is treated as discontinued operations. The operating properties sold by us typically meet the definition of a component of an entity and as such the revenues and expenses associated with sold properties are reclassified to discontinued operations for all periods presented.

Financial Instruments

The estimated fair values of financial instruments are determined using available market information and appropriate valuation methods. Considerable judgment is necessary to interpret market data and develop estimated fair values. The use of different market assumptions or estimation methods may have a material effect on the estimated fair value amounts. Accordingly, estimated fair values are not necessarily indicative of the amounts that could be realized in current market exchanges.

American Assets Trust, Inc.

Notes to Consolidated Financial Statements (Continued)

June 30, 2011

(Unaudited)

Cash and Cash Equivalents

We define cash and cash equivalents as cash on hand, demand deposits with financial institutions and short term liquid investments with an initial maturity of less than three months. Cash balances in individual banks may exceed the federally insured limit of $250,000 by the Federal Deposit Insurance Corporation. No losses have been experienced related to such accounts.

Restricted Cash

Restricted cash consists of amounts held by lenders to provide for future real estate tax expenditures, insurance expenditures and reserves for capital improvements. Activity for accounts related to real estate tax and insurance expenditures is classified as operating activities in the statement of cash flows. Changes in reserves for capital improvements are classified as investing activities in the statement of cash flows.

Marketable Securities

Our portfolio of marketable securities is comprised of debt securities that are classified as trading. Trading securities are presented on our consolidated balance sheets at fair value at the end of each reporting period. Gains and losses resulting from the mark-to-market of these securities are recognized as unrealized gains or losses in income.

Prepaid Expenses and Other Assets

Prepaid expenses and other assets consist primarily of lease costs, lease incentives, acquired in-place leases, acquired above market leases and debt issuance costs. Capitalized lease costs are direct costs incurred which were essential to originate a lease and would not have been incurred had the leasing transaction not taken place and include third party commissions and internal salaries and personnel costs related to obtaining a lease. Capitalized lease costs are amortized over the life of the related lease and included in depreciation and amortization expense on the statement of operations. If a tenant vacates its space prior to the contractual termination of its lease, the unamortized balance of any lease costs are written off. We view these lease costs as part of the up-front initial investment we made in order to generate a long-term cash inflow. Therefore, we classify cash outflows for lease costs as an investing activity in our consolidated statements of cash flows.

Costs related to the issuance of debt instruments are capitalized and are amortized as interest expense over the estimated life of the related issue using the straight-line method which approximates the effective interest method. If a debt instrument is paid off prior to its original maturity date, the unamortized balance of debt issuance costs are written off to interest expense or, if significant, included in early extinguishment of debt. For the six months ended June 30, 2011, $0.6 million in debt issuance costs were written off and included in early extinguishment of debt.

Purchase deposit

Purchase deposit relates to the acquisition of the Lloyd District Portfolio. Such acquisition was completed on July 1, 2011 (Note 17).

Variable Interest Entities

Certain entities that do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties or in which equity investors do not have the characteristics of a controlling financial interest qualify as variable interest entities (VIE). VIEs are required to be consolidated by their primary beneficiary. The primary beneficiary of a VIE is the party that has a controlling interest in the VIE. Identifying the party with the controlling interest requires a focus on which entity has the power to direct the activities of the VIE that most significantly impact the VIE s economic performance and (1) the obligation to absorb the expected losses of the VIE or (2) the right to receive the benefits from the VIE. We have evaluated our investments in certain joint ventures and determined that these joint ventures do not meet the requirements of a VIE and, therefore, consolidation of these ventures is not required. These investments are accounted for using the equity method. Our investment balances in our real estate joint ventures are presented separately in our consolidated balance sheets.

Investments in Real Estate Joint Ventures

We analyze our investments in real estate joint ventures under applicable guidance to determine if the venture is considered a VIE and would require consolidation. To the extent that the ventures do not qualify as VIEs, we further assess the venture to determine whether a general partner, or the general partners as a group, controls a limited partnership or similar entity when the limited partners have certain rights in order to determine whether consolidation is required.

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We consolidate those ventures that are considered to be VIEs where we are the primary beneficiary. For non-VIEs, the Predecessor combined those ventures that Ernest Rady controlled through majority ownership interests or where the Predecessor was the managing member and the partner did not have substantive participating rights. Control is further demonstrated by the ability of the general partner to manage day-to-day operations, refinance debt and sell the assets of the venture without the consent of the limited partner and inability of the limited partner to replace the general partner. We use the equity method of accounting for those ventures where we do not have control over operating and financial policies. Under the equity method of accounting, the investment in each venture is included on our balance sheet; however, the assets and liabilities of the ventures for which we use the equity method are not included in the balance sheet. The investment is adjusted for contributions, distributions and our proportionate share of the net earnings or losses of each respective venture.

We assess whether there has been impairment in the value of our investments in real estate joint ventures periodically. An impairment charge is recorded when events or changes in circumstances indicate that a decline in the fair value below the carrying value has occurred and such decline is other-than-temporary. The ultimate realization of the investments in unconsolidated real estate joint ventures is dependent on a number of factors, including the performance of the investments and market conditions.

Notes Receivable from Affiliate

Certain entities made loans to affiliates in order to attain a higher return on excess cash balances, and these loans were classified as notes receivable from affiliates at December 31, 2010. The notes bore interest at LIBOR and were to be repaid upon demand. The notes were settled as part of the Formation Transactions.

Notes Payable to Affiliates

Owners of certain entities made loans to the entities, and these loans were classified as notes payable to affiliates at December 31, 2010. The notes bore interest at 10% and matured in 2013. The notes were repaid using proceeds from the Offering or were settled as part of the Formation Transactions.

Stock-Based Compensation

We grant stock-based compensation awards to our employees and directors typically in the form of restricted shares of common stock, options to purchase common stock and/or shares of common stock. We measure stock-based compensation expense based on the fair value of the award on the grant date and recognize the expense ratably over the vesting period.

Deferred Compensation

Our Operating Partnership has adopted the American Assets Trust Executive Deferral Plan V (EDP V) and the American Assets Trust Executive Deferral Plan VI (EDP VI). These plans were adopted by our Operating Partnership as successor plans to those deferred compensation plans maintained by AAI in which certain employees of AAI, who were transferred to us in connection with the Offering (the Transferred Participants), participated prior to the Offering. EDP V and EDP VI contain substantially the same terms and conditions as these predecessor plans. AAI transferred to our Operating Partnership the Transferred Participants account balances under the predecessor plans. These transferred account balances represent amounts deferred by the Transferred Participants prior to the Offering while they were employed by AAI.

At the time eligible participants defer compensation, we record compensation cost and a corresponding deferred compensation plan liability, which is included in other liabilities and deferred credits on our consolidated balance sheets. This liability is adjusted to fair value at the end of each accounting period based on the performance of the benchmark funds selected by each participant, and the impact of adjusting the liability to fair value is recorded as an increase or decrease to compensation cost.

Income Taxes

Prior to the Offering, we were comprised primarily of limited partnerships and limited liability companies. Under applicable federal and state income tax rules, the allocated share of net income or loss from the limited partnerships and limited liability companies was reportable in the income tax returns of the respective partners and members.

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(Unaudited)

Subsequent to the Offering, we intend to elect to be taxed as a REIT under the Internal Revenue Code of 1986, as amended (the Code) commencing with the taxable year ending December 31, 2011. To qualify as a REIT, we are required to distribute at least 90% of our REIT taxable income to our stockholders and meet the various other requirements imposed by the Code relating to such matters as operating results, asset holdings, distribution levels and diversity of stock ownership. Provided we qualify for taxation as a REIT, we are generally not subject to corporate level income tax on the earnings distributed currently to our stockholders that we derive from our REIT qualifying activities. If we fail to qualify as a REIT in any taxable year, and are unable to avail ourselves of certain savings provisions set forth in the Code, all of our taxable income would be subject to federal income tax at regular corporate rates, including any applicable alternative minimum tax.

We, together with one of our subsidiaries, will elect to treat such subsidiary as a taxable REIT subsidiary (a TRS) for federal income tax purposes. Certain activities that we undertake must be conducted by a TRS, such as non-customary services for our tenants, and holding assets that we cannot hold directly. A TRS is subject to federal and state income taxes.

Segment Information

Segment information is prepared on the same basis that our management reviews information for operational decision-making purposes. We operate in four business segments: (1) the acquisition, redevelopment, ownership and management of retail real estate, (2) the acquisition, redevelopment, ownership and management of office real estate, (3) the acquisition, redevelopment, ownership and management of multifamily real estate and (4) the acquisition, redevelopment, ownership and management of mixed-use real estate. The products for our retail segment primarily include rental of retail space and other tenant services, including tenant reimbursements, parking and storage space rental. The products for our office segment primarily include rental of office space and other tenant services, including tenant reimbursements, parking and storage space rental. The products for our multifamily segment include rental of apartments and other tenant services. The products of our mixed-use segment include rental of retail space and other tenant services, including tenant reimbursements, parking and storage space rental and operation of a 369-room all-suite hotel.

Reclassifications

Certain items in the consolidated financial statements for prior periods have been reclassified to conform to current classifications.

Recent Accounting Pronouncements

In December 2010, the Financial Accounting Standards Board (FASB) issued ASU No. 2010-29, *Disclosure of Supplementary Pro Forma Information for Business Combinations* (ASU 2010-29), which amended ASC Topic 805, *Business Combinations* (ASC 805). The objective of this guidance is to eliminate diversity in the interpretation of pro forma revenue and earnings disclosures requirements for business combinations. The guidance specifies that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination(s) that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. The guidance also expands the supplemental pro forma disclosures under ASC 805 to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination(s) included in the reported pro forma revenue and earnings. ASU 2010-29 is effective for business combinations for which the acquisition date occurs following the first annual reporting period which commences after December 15, 2010. The guidance is required in interim and annual reporting periods. Our adoption of this guidance effective January 1, 2011 did not have a material effect on our consolidated financial statements.

In May 2011, the FASB issued ASU No. 2011-04, *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs* (ASU 2011-04), which amended ASC Topic 820, *Fair Value Measurement.* ASU 2011-04 clarifies the application of certain existing fair value measurement guidance and expands the disclosures for fair value measurements that are estimated using significant unobservable (Level 3) inputs. ASU 2011-04 is effective for annual and interim reporting periods beginning on or after December 15, 2011. The new guidance is to be adopted prospectively and early adoption is not permitted. We do not believe that adoption of ASU 2011-04 will have a significant impact on our financial position, results of operations or cash flows.

In June 2011, the FASB issued ASU No. 2011-05, *Presentation of Comprehensive Income* (ASU 2011-05), which amended ASC Topic 220, *Comprehensive Income.* ASU 2011-05 eliminates the option to present components of other comprehensive income as part of the statement of changes in equity and requires that all non owner changes in equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. ASU 2011-05 requires retrospective application and will be effective for interim and annual reporting periods beginning after December 15, 2011. We do not believe the adoption of ASU 2011-05 will have significant impact on our disclosures of comprehensive income.

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NOTE 2. REAL ESTATE

As noted above, as part of the Formation Transactions, we acquired the controlling interests in the Waikiki Beach Walk entities and the Solana Beach Centre entities for Operating Partnership units and common shares with a value of approximately $33.9 million. The contribution or acquisition by merger of interests in these entities was accounted for as an acquisition under the acquisition method of accounting and recognized at the estimated fair value of acquired assets and assumed liabilities on the date of such contribution or acquisition. Prior to acquisition, our Predecessor had an 80% noncontrolling interest in the Waikiki Beach Walk entities and a 50% noncontrolling interest in the Solana Beach Centre entities. Upon acquisition, we remeasured the assets and liabilities at fair value and recorded gains of $4.8 million and $41.6 million on the Waikiki Beach Walk entities and the Solana Beach Centre entities, respectively, which are classified as gain on acquisition in the accompanying statement of operations. These gains were calculated based on the difference between the fair value of our Predecessor s ownership interests of $31.3 million and $26.0 million compared to the Predecessor s historical cost interests of $26.5 million and $(15.6) million in the Waikiki Beach Walk entities and Solana Beach Centre entities, respectively.

The fair values assigned to identifiable intangible assets acquired were based on estimates and assumptions determined by management. Using information available at the time the acquisition closed, we allocated the total consideration to tangible assets and liabilities and identified intangible assets and liabilities.

The allocation of the consideration paid for the acquired assets and liabilities was as follows (in thousands):

	Solana Beach Towne Centre	Solana Beach Corporate Centre	Waikiki Beach Walk Retail and Hotel	Total
Land	$ 40,980	$ 14,896	$ 76,635	$ 132,511
Building	35,605	42,094	122,985	200,684
Land improvements	1,750	974	2,276	5,000
Tenant improvements	1,487	1,919	1,801	5,207
Furniture and fixtures			7,910	7,910
Total real estate	79,822	59,883	211,607	351,312
Cash and cash equivalents	957	718	13,547	15,222
Restricted cash	282	200	1,297	1,779
Accounts receivable, net	67		2,168	2,235
Lease intangibles	6,995	5,536	15,997	28,528
Prepaid expenses and other assets	22	45	266	333
Total assets	$ 88,145	$ 66,382	$ 244,882	$ 399,409
Secured notes payable	$ 39,738	$ 49,252	$ 198,618	$ 287,608
Fair market favorable debt value		(600)	(19,000)	(19,600)
Notes payable to affiliates			14,824	14,824
Accounts payable and accrued expenses	924	542	6,520	7,986
Security deposits payable	238	320	861	1,419
Lease intangibles	11,390	125	3,530	15,045
Other liabilities and deferred credits	192	331	442	965

Total liabilities	$ 52,482	$ 49,970	$ 205,795	$ 308,247

We have included the results of operations for each of these acquired entities in our consolidated statements of operations from January 19, 2011, the date of acquisition. For the period January 19, 2011 through June 30, 2011, the acquired entities contributed $26.6 million to total revenue, $22.2 million to operating expenses, $4.4 million to operating income and $(4.3) million to net income.

On March 11, 2011, we acquired an approximately 364,000 square foot, 16-story, LEED Platinum certified office building located at 100 SW Main Street, in Portland, Oregon (First & Main). The purchase price for First & Main was approximately $128.9

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(Unaudited)

million, excluding closing costs of approximately $0.1 million, which are included in other income (expense), net on the statement of operations. The purchase was funded using cash on hand and structured to accommodate a possible tax deferred exchange pursuant to the provisions of Section 1031 of the Code and applicable state revenue and taxation code sections.

The fair values assigned to identifiable intangible assets acquired were based on estimates and assumptions determined by management. Using information available at the time the acquisition closed, we allocated the total consideration to tangible assets and liabilities and identified intangible assets and liabilities. We may adjust the preliminary purchase price allocation after obtaining more information about asset valuations and liabilities assumed. The allocation of the purchase price of the acquired First & Main assets and liabilities was as follows (in thousands):

Land	$ 14,697
Building	102,597
Land improvements	151
Tenant improvements	6,991
Total real estate	124,436
Accounts receivable, net	153
Lease intangibles	9,578
Prepaid expenses and other assets	296
Total assets	$ 134,463
Accounts payable and accrued expenses	$ 387
Below market lease intangible	5,199
Total liabilities	$ 5,586

We have included the results of operations for First & Main in our consolidated statements of operations from March 11, 2011, the date of acquisition. For the period March 11, 2011 through June 30, 2011, First & Main contributed $3.4 million to total revenue, $2.5 million to operating expenses, $0.9 million to operating income and $0.6 million to net income.

Pro Forma Financial Information

The unaudited financial information in the table below summarizes the combined results of operations of the Solana Beach Centre entities, the Waikiki Beach Walk entities and First & Main with the historical results of operations of the Company/Predecessor on a pro forma basis, as though the entities had been acquired on January 1, 2010. The pro forma financial information for the six months ended June 30, 2010, also includes the pro forma results of operations for The Landmark at One Market, which was acquired by the Predecessor on June 30, 2010, as though the entity had been acquired on January 1, 2010. The pro forma financial information is presented for informational purposes only and is not indicative of the results of operations that would have been achieved if the acquisitions had taken place on January 1, 2010. The pro forma financial information includes adjustments to depreciation expense for acquired property and equipment, adjustments to amortization charges for acquired intangible assets and liabilities, adjustments to straight-line rent revenue and the removal of the gain on acquisition of the controlling interests of the Solana Beach Centre entities and Waikiki Beach Walk entities for the six months ended June 30, 2011 and The Landmark at One Market for the six months ended June 30, 2010.

The following table summarizes the unaudited pro forma financial information (in thousands):

	Six Months Ended June 30, 2011	2010
Total revenue	$ 104,398	$ 96,303
Total operating expenses	73,536	63,127
Operating income	30,862	33,176
Net loss	$ (31,823)[(1)]	$ (433)

(1) The net loss for the six months ended June 30, 2011 includes one-time expenses for the early extinguishment of debt and loan transfer and consent fees but excludes the gain on acquisition of the controlling interests in the Solana Beach Centre entities and the Waikiki Beach Walk entities.

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NOTE 3. INVESTMENTS IN REAL ESTATE JOINT VENTURES

As of December 31, 2010, our Predecessor had four joint venture arrangements with unrelated third parties. We owned from 25% to 80% of each of these ventures. For two of these ventures, we were the general partner or managing member; however, the outside owners were either a co-general partner or had substantive participating rights, and we could not make significant decisions without the outside owners approval. Accordingly, we accounted for these investments under the equity method. We acted as the manager of the three properties owned by these two ventures and received fees in accordance with service contracts (Note 15).

For the joint venture that owned a mixed-use property in Honolulu, Hawaii, we had an effective 80% limited ownership interest in the property; however, the outside owner was the managing member and managed the day-to-day business of the property. In addition, we did not have kick-out rights relating to the outside owner s managing membership interest. Accordingly, we accounted for these investments under the equity method of accounting.

The properties owned by these unconsolidated joint ventures at December 31, 2010 were as follows:

Property	Type	Location
Solana Beach Towne Centre	Retail	Solana Beach, CA
Solana Beach Corporate Centre	Office	Solana Beach, CA
Fireman s Fund Headquarters	Office	Novato, CA
Waikiki Beach Walk	Mixed Use	Honolulu, HI

As noted above, as part of the Formation Transactions, we acquired the unrelated third party s interest in Solana Beach Towne Centre, Solana Beach Corporate Centre and Waikiki Beach Walk. We consolidated the operations of these properties subsequent to the Formation Transactions. The Predecessor s ownership interest in Fireman s Fund Headquarters was not acquired, and rather the ownership interests in this entity were distributed to its owners as part of the Formation Transactions. In addition, we no longer receive fee income from these ventures.

The Waikiki Beach Walk property has a 47.7% investment in WBW CHP LLC, an entity that was formed to construct a chilled water plant to provide air conditioning to the property and other adjacent facilities. The operating expenses of WBW CHP LLC are recovered through reimbursements from its members. Annual contributions are made to fund maintenance reserves. Upon acquisition of the Waikiki Beach Walk property, the investment in WBW CHP LLC was recorded at its fair value of $0.

NOTE 4. ACQUIRED IN-PLACE LEASES AND ABOVE/BELOW MARKET LEASES

The following summarizes our acquired lease intangibles, which are included in prepaid expenses and other assets and other liabilities and deferred credits, as of June 30, 2011 and December 31, 2010 (in thousands):

	June 30, 2011	December 31, 2010
In-place leases	$ 59,339	$ 41,108
Accumulated amortization	(32,658)	(30,901)
Above market leases	41,368	33,557
Accumulated amortization	(23,762)	(21,433)
Acquired lease intangible assets, net	$ 44,287	$ 22,331

Below market leases	$ 73,526	$ 54,576
Accumulated accretion	(23,198)	(21,546)
Acquired lease intangible liabilities, net	$ 50,328	$ 33,030

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(Unaudited)

NOTE 5. MARKETABLE SECURITIES

Our portfolio of marketable securities is comprised of debt securities that are classified as trading securities. At June 30, 2011, our marketable securities consisted of investments in mortgage-backed securities issued by the Government National Mortgage Association (GNMA securities). We report our trading securities at fair value, based on quoted market prices (Level 1 of the fair value hierarchy see Note 6). Gains and losses resulting from the mark-to-market of these securities are recognized as unrealized gains or losses in income. For the six months ended June 30, 2011, we recorded $0.1 million in unrealized gains in our statement of operations, which are included in other income (expense). Unrealized gains were $0.1 million as of June 30, 2011.

NOTE 6. FAIR VALUE OF FINANCIAL INSTRUMENTS

A fair value measurement is based on the assumptions that market participants would use in pricing an asset or liability. The hierarchy for inputs used in measuring fair value is as follows:

1. Level 1 Inputs quoted prices in active markets for identical assets or liabilities

2. Level 2 Inputs observable inputs other than quoted prices in active markets for identical assets and liabilities

3. Level 3 Inputs unobservable inputs

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, for disclosure purposes, the level within which the fair value measurement is categorized is based on the lowest level input that is significant to the fair value measurement.

Except as disclosed below, the carrying amount of our financial instruments approximates their fair value. The fair value of our secured notes payable and unsecured notes payable is sensitive to fluctuations in interest rates. Discounted cash flow analysis (Level 2) is generally used to estimate the fair value of our mortgages and notes payable, using rates ranging from 3.7% to 8.5%. Considerable judgment is necessary to estimate the fair value of financial instruments. The estimates of fair value presented herein are not necessarily indicative of the amounts that could be realized upon disposition of the financial instruments. A summary of the carrying amount and fair value of our notes payable is as follows (in thousands):

	June 30, 2011		December 31, 2010	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Secured notes payable	$ 944,279	$ 974,511	$ 851,547	$ 871,016
Unsecured notes payable			$ 38,013	$ 38,023

Due to their related party nature, notes to affiliates outstanding at December 31, 2010 cannot be measured at fair value.

NOTE 7. PREPAID EXPENSES AND OTHER ASSETS

Prepaid expenses and other assets consist of the following:

	June 30, 2011	December 31, 2010
	(In thousands)	
Leasing commissions, net of accumulated amortization of $15,316 and $13,750, respectively	$ 16,380	$ 11,335
Acquired above market leases, net	17,606	12,124
Acquired in-place leases, net	26,681	10,207
Lease incentives, net of accumulated amortization of $1,665 and $1,480, respectively	2,035	2,220
Other intangible assets, net of accumulated amortization of $2,806 and $1,325, respectively	2,116	364
Debt issuance costs, net of accumulated amortization of $1,896 and $2,469, respectively	4,004	2,233
Prepaid expenses, deposits, and other	1,093	5,883
Total prepaid expenses and other assets	$ 69,915	$ 44,366

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Lease incentives are amortized over the term of the related lease and included as a reduction of rental income in the statement of operations. Prepaid expenses and deposits included $5.3 million in costs related to the Offering at December 31, 2010, which were recorded as a reduction of capital at the time of the Offering.

NOTE 8. OTHER LIABILITIES AND DEFERRED CREDITS

Other liabilities and deferred credits consist of the following:

	June 30, 2011	December 31, 2010
	(In thousands)	
Acquired below market leases, net	$ 50,328	$ 33,030
Prepaid rent and deferred revenue	4,447	5,257
Straight-line rent liability	870	722
Deferred rent expense and lease intangible	714	
Deferred compensation	493	
Other liabilities	70	49
Total other liabilities and deferred credits	$ 56,922	$ 39,058

Straight-line rent liability relates to leases which have rental payments that decrease over time or one-time upfront payments for which the rental revenue is deferred and recognized on a straight-line basis.

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(Unaudited)

NOTE 9. DEBT

The following is a summary of our total debt outstanding as of June 30, 2011 and December 31, 2010 (in thousands):

Description of Debt	Principal Balance as of June 30, 2011	Principal Balance as of December 31, 2010	Stated Interest Rate as of June 30, 2011	Stated Maturity Date
Secured Notes Payable				
Valencia Corporate Center (1)(2)(3)	$	$ 7,223	N/A	February 1, 2011
Valencia Corporate Center (1)(4)		15,639	N/A	October 1, 2012
160 King Street (1)(2)(5)(10)		8,564	N/A	November 1, 2012
Carmel Country Plaza (1)(4)		10,145	N/A	January 2, 2013
Santa Fe Park RV Resort (1)(4)		1,856	N/A	January 2, 2013
Lomas Santa Fe Plaza (1)(4)		19,599	N/A	May 1, 2013
Torrey Reserve South Court (1)(4)		12,892	N/A	May 1, 2013
Carmel Mountain Plaza (1)(4)		62,907	N/A	June 1, 2013
Alamo Quarry Market (4)(6)	97,026	98,011	5.670%	January 8, 2014
160 King Street (7)	32,182	32,931	5.680%	May 1, 2014
Waikele Center (5)	140,700	140,700	5.145%	November 1, 2014
The Shops at Kalakaua (5)	19,000	19,000	5.449%	May 1, 2015
The Landmark at One Market (5)(6)	133,000	133,000	5.605%	July 5, 2015
Del Monte Center (5)	82,300	82,300	4.926%	July 8, 2015
Rancho Carmel Plaza (1)(4)		8,049	N/A	January 1, 2016
First & Main (5)	84,500		3.965%	July 1, 2016
Imperial Beach Gardens (5)	20,000	20,000	6.163%	September 1, 2016
Mariner s Point (5)	7,700	7,700	6.092%	September 1, 2016
Torrey Reserve ICW Plaza (1)(5)		43,000	N/A	February 1, 2017
South Bay Marketplace (5)	23,000	23,000	5.477%	February 10, 2017
Waikiki Beach Walk Retail (5)	130,310		5.390%	July 1, 2017
Solana Beach Corporate Centre III-IV (11)	37,330		6.390%	August 1, 2017
Loma Palisades (5)	73,744	73,744	6.090%	July 1, 2018
Torrey Reserve North Court (4)	22,046	22,165	7.220%	June 1, 2019
Torrey Reserve Torrey Daycare (1)(8)		1,660	N/A	June 1, 2019
Torrey Reserve VCI, VCII, VCIII (4)	7,421	7,462	6.355%	June 1, 2020
Solana Beach Corporate Centre I-II (4)	11,860		5.910%	June 1, 2020
Solana Beach Towne Centre (4)	39,533		5.910%	June 1, 2020
	961,652	851,547		

Unamortized fair value adjustment	(17,373)			
	944,279	851,547		
Unsecured Notes Payable				
Waikele Center Notes (1)(2)(5)		5,813	N/A	February 15, 2011
Landmark Note (1)(2)(5)		19,000	N/A	July 1, 2013
Carmel Mountain Note (1)(2)(5)		13,200	N/A	August 1, 2013
		38,013		
Notes Payable to Affiliates				
Del Monte Center Affiliates (1)(9)		5,266	N/A	March 1, 2013
Total Debt Outstanding	$ 944,279	$ 894,826		

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Notes to Consolidated Financial Statements (Continued)

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(1) Note was voluntarily repaid in full as part of the Formation Transactions.
(2) Loan was fully or partially guaranteed by owners or affiliates.
(3) Interest rate has floor of 4.50%
(4) Principal payments based on a 30-year amortization schedule.
(5) Interest only.
(6) Maturity Date is the earlier of the loan maturity date under the loan agreement, or the Anticipated Repayment Date as specifically defined in the loan agreement, which is the date after which substantial economic penalties apply if the loan has not been paid off.
(7) Principal payments based on a 20-year amortization schedule.
(8) Principal payments based on a 25-year amortization schedule. The interest rate will be reset to the greater of 6.50% or LIBOR plus 4.00% on June 1, 2014.
(9) Principal payments based on a 5-year amortization schedule.
(10) Secured by the owners equity interests in the entity.
(11) Loan is interest only through August 2012. Beginning in September 2012, principal payments are based on a 30-year amortization schedule.

We used a portion of net proceeds received from the Offering to repay in full certain outstanding indebtedness, including applicable prepayment costs, exit fees and defeasance costs. The defeasance costs of $24.3 million are included in early extinguishment of debt, along with $0.6 million of unamortized deferred loan fees and $0.9 million of unamortized debt fair value adjustments that were written off related to loans repaid at the time of the Offering. Additionally, we paid $9.0 million in loan transfer and consent fees to lenders, which were expensed as incurred, in order for the lenders to consent to the transfer of the existing loans at certain properties to the Operating Partnership as part of the Formation Transactions.

On June 1, 2011, we, through a subsidiary, entered into a five-year non-recourse mortgage loan with PNC Bank, National Association with an original principal amount of $84.5 million. The loan is secured by a first-priority deed of trust on the First & Main property and an assignment of all leases, rents and security deposits relating to the First & Main property. The loan has a maturity date of July 1, 2016, bears interest at a fixed rate per annum of 3.965% and is interest only.

Certain loans require us to comply with various financial covenants, including the maintenance of minimum debt coverage ratios. As of June 30, 2011, we were in compliance with all loan covenants.

Revolving Credit Facility

On January 19, 2011, in connection with the Offering, we entered into a credit facility pursuant to which a group of lenders provided commitments for a revolving credit facility allowing borrowings of up to $250.0 million. The credit facility has an initial term of three years, and we have the option to extend the term for one additional year if we meet specified requirements. The credit facility has an accordion feature that may allow us to increase the availability thereunder by up to $150.0 million, subject to meeting specified requirements and obtaining additional commitments from lenders. No amounts have been borrowed on the credit facility to date. The credit facility bears interest at the rate of either LIBOR or a base rate, in each case plus a margin that will vary depending on our leverage ratio. The amount available for us to borrow under the credit facility is subject to the net operating income of our properties that form the borrowing base of the facility and a minimum implied debt yield of such properties.

The credit facility includes a number of customary financial covenants, including:

- a maximum leverage ratio (defined as total indebtedness net of certain unrestricted cash and cash equivalents to total asset value) of 65% on or prior to December 31, 2011 and 60% thereafter,

- a minimum fixed charge coverage ratio (defined as consolidated earnings before interest, taxes, depreciation and amortization to consolidated fixed charges) of 1.50x, a maximum secured leverage ratio (defined as total secured indebtedness to secured total asset value) of 57.5% on or prior to December 31, 2012 and 50% thereafter,

a minimum tangible net worth equal to at least 75% of our tangible net worth at January 19, 2011, plus 85% of the net proceeds of any additional equity issuances (other than additional equity issuances in connection with any dividend reinvestment program), and

a $35.0 million limit on the maximum principal amount of recourse indebtedness we may have outstanding at any time, other than under the credit facility.

The credit facility provides that our annual distributions may not exceed the greater of (1) 95.0% of our funds from operations (FFO) or (2) the amount required for us to (a) qualify and maintain our REIT status and (b) avoid the payment of federal or state income or excise tax. If certain events of default exist or would result from a distribution, we may be precluded from making distributions other than those necessary to qualify and maintain our status as a REIT.

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Notes to Consolidated Financial Statements (Continued)

June 30, 2011

(Unaudited)

We and certain of our subsidiaries guarantee the obligations under the credit facility, and certain of our subsidiaries pledged specified equity interests in our subsidiaries as collateral for our obligations under the credit facility.

On March 7, 2011, the credit facility was amended to allow us or our Operating Partnership to purchase GNMA securities with maturities of up to 30 years.

NOTE 10. EQUITY

Noncontrolling Interests

Noncontrolling interests in our Operating Partnership are interests in the Operating Partnership that are not owned by us. Noncontrolling interests consisted of 18,396,089 common units (the noncontrolling common units), and represented approximately 32% of the ownership interests in our Operating Partnership at June 30, 2011. Common units and shares of our common stock have essentially the same economic characteristics in that common units and shares of our common stock share equally in the total net income or loss distributions of our Operating Partnership. Investors who own common units have the right to cause our Operating Partnership to redeem any or all of their common units for cash equal to the then-current market value of one share of our common stock, or, at our election, shares of our common stock on a one-for-one basis.

On February 14, 2011, we completed a private placement transaction of 251,050 common units for approximately $5.4 million.

Dividends

During the second quarter of 2011, we declared and paid dividends on our shares of common stock and noncontrolling common units of $0.21 per share and per unit for the second quarter. During the first quarter of 2011, we declared and paid dividends on our shares of common stock and noncontrolling common units of $0.17 per share and per unit for the period from and including January 19, 2011 to March 31, 2011.

Taxability of Dividends

Earnings and profits, which determine the taxability of distributions to stockholders and holders of common units, may differ from income reported for financial reporting purposes due to the differences for federal income tax purposes in the treatment of loss on extinguishment of debt, revenue recognition and compensation expense and in the basis of depreciable assets and estimated useful lives used to compute depreciation.

Stock-Based Compensation

Concurrently with the closing of the Offering, we made grants of restricted shares of our common stock to certain executive officers pursuant to the terms of their employment agreements. These awards were made pursuant to our 2011 Equity Incentive Award Plan (the 2011 Plan). At such time, we granted to such executive officers a total of 198,000 shares that are subject to timing-based vesting and 297,000 shares that are subject to performance-based vesting, with fair market values of $4.1 million for the timing-based vesting awards and $3.9 million for the performance-based vesting awards. Those awards subject to time-based vesting will vest, subject to the recipient s continued employment, in two substantially equal installments on each of the third and fourth anniversaries of the date of grant. The vesting of those restricted stock awards subject to performance-based vesting is based on the achievement of absolute and relative total shareholder return hurdles over a three-year performance period, commencing on January 19, 2011. Following the completion of the three-year performance period, our compensation committee will determine the number of shares to which the executive officer is entitled based on our performance relative to the performance hurdles set forth in the restricted stock award agreement he entered into in connection with his initial award grant. These shares will then vest in two substantially equal installments, with the first installment vesting on the third anniversary of the date of grant and the second installment vesting on the fourth anniversary of the date of grant, subject to the executive officer s continued employment on those dates.

Concurrently with the closing of the Offering, we also granted each of our non-employee directors 1,951 restricted shares of our common stock pursuant to the 2011 Plan, other than one who was granted 1,952 restricted shares. These awards of restricted stock will vest ratably as to one-third of the shares granted on each of the first three anniversaries of the date of grant, subject to the director s continued service on our board of directors, and had an aggregate fair value of $0.2 million on the date of the grants. On June 29, 2011, one of our directors notified us of his resignation as a director of the Company and, as a result, immediately forfeited the 1,951 restricted shares of our common stock previously granted to him, none of which had vested.

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Notes to Consolidated Financial Statements (Continued)

June 30, 2011

(Unaudited)

On March 16, 2011 we granted a total of 123,950 restricted shares of our common stock to certain other employees pursuant to the 2011 Plan with a fair value of $1.6 million. These shares are subject to performance-based vesting, with the terms described above related to performance-based vesting.

For the performance-based stock awards, the fair value of the awards was estimated using a Monte Carlo Simulation model. The volatilities of the returns on the stock price of the Company and the group REITs were estimated based on a three year look-back period. The expected growth rate of the stock prices over the derived service period of the employee is determined with consideration of the risk free rate as of the grant date. For the restricted stock grants that are time-vesting, we estimate the stock compensation expense based on the fair value of the stock at the grant date.

None of the restricted shares were vested at June 30, 2011. We recognize noncash compensation expense ratably over the vesting period, and accordingly, we recognized $1.2 million in noncash compensation expense for the six months ended June 30, 2011, which is included in general and administrative expense on the statement of operations. Unrecognized compensation expense was $8.5 million.

Earnings Per Share

We have calculated earnings per share (EPS) under the two-class method. The two-class method is an earnings allocation methodology whereby EPS for each class of common stock and participating security is calculated according to dividends declared and participation rights in undistributed earnings. For the three and six months ended June 30, 2011, we had a weighted average of approximately 628,663 and 527,812 unvested shares outstanding, respectively, which are considered participating securities. Therefore, we have allocated our earnings for basic and diluted EPS between common shares and unvested shares.

Diluted EPS is calculated by dividing the net income applicable to common stockholders for the period by the weighted average number of common and dilutive instruments outstanding during the period using the treasury stock method. Since we were in a net loss position for the six months ended June 30, 2011, all potentially dilutive instruments are anti-dilutive and have been excluded from our computation of weighted average dilutive shares outstanding. For the three and six months ended June 30, 2011, diluted shares exclude incentive restricted stock as these awards are considered contingently issuable. Additionally, the unvested restricted stock awards subject to time vesting are anti-dilutive for all periods presented and accordingly, have been excluded from the weighted average common shares used to compute diluted EPS.

The computation of basic and diluted EPS is presented below (dollars in thousands, except share and per share amounts):

	Three Months Ended June 30, 2011	Six Months Ended June 30, 2011
Numerator		
Net income (loss) attributable to American Assets Trust Inc. common stockholders basic	$ 219	$ (479)
Plus: Net income attributable to unitholders in the Operating Partnership	104	(1)
Net income (loss) attributable to common stockholders diluted	$ 323	$ (479)
Denominator		
Weighted average common shares outstanding basic	38,655,084	34,810,932
Effect of dilutive securities conversion of Operating Partnership units	18,396,089	(1)

Weighted average common shares outstanding diluted	57,051,173	34,810,932
Earnings per common share basic	$	