

Hudson Pacific Properties, Inc.
Form 10-Q
May 04, 2018
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2018

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF
^o 1934

For the transition period from _____ to _____

Commission File Number: 001-34789 (Hudson Pacific Properties, Inc.)

Commission File Number: 333-202799-01 (Hudson Pacific Properties, L.P.)

Hudson Pacific Properties, Inc.
Hudson Pacific Properties, L.P.
(Exact name of registrant as specified in its charter)

Hudson Pacific Properties, Inc.	Maryland (State or other jurisdiction of incorporation or organization)	27-1430478 (I.R.S. Employer Identification Number)
Hudson Pacific Properties, L.P.	Maryland (State or other jurisdiction of incorporation or organization)	80-0579682 (I.R.S. Employer Identification Number)

11601 Wilshire Blvd., Ninth Floor
Los Angeles, California 90025
(Address of principal executive offices) (Zip Code)
(310) 445-5700
(Registrant's telephone number, including area code)

N/A
(Former name, former address and former fiscal year, if changed since last report)

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.

Hudson Pacific Properties, Inc. Yes No
Hudson Pacific Properties, L.P. 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

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Hudson Pacific Properties, Inc. Yes No Hudson Pacific Properties, L.P.
Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Hudson Pacific Properties, Inc.
Large accelerated filer Accelerated filer Non-accelerated filer
(Do not check if a smaller reporting company)
Smaller reporting company Emerging growth company

Hudson Pacific Properties, L.P.
Large accelerated filer Accelerated filer Non-accelerated filer
(Do not check if a smaller reporting company)
Smaller reporting company Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Hudson Pacific Properties, Inc. Hudson Pacific Properties, L.P.
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Hudson Pacific Properties, Inc. Yes No Hudson Pacific Properties, L.P.
Yes No

The number of shares of common stock of Hudson Pacific Properties, Inc. outstanding at May 1, 2018 was 156,680,066.

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EXPLANATORY NOTE

This report combines the quarterly reports on Form 10-Q for the period ended March 31, 2018 of Hudson Pacific Properties, Inc., a Maryland corporation, and Hudson Pacific Properties, L.P., a Maryland limited partnership. Unless otherwise indicated or unless the context requires otherwise, all references in this report to “we,” “us,” “our,” or “our Company” refer to Hudson Pacific Properties, Inc. together with its consolidated subsidiaries, including Hudson Pacific Properties, L.P. Unless otherwise indicated or unless the context requires otherwise, all references to “our operating partnership” or “the operating partnership” refer to Hudson Pacific Properties, L.P. together with its consolidated subsidiaries.

Hudson Pacific Properties, Inc. is a real estate investment trust, or REIT, and the sole general partner of our operating partnership. As of March 31, 2018, Hudson Pacific Properties, Inc. owned approximately 99.6% of the outstanding common units of partnership interest (including unvested restricted units) in our operating partnership, or common units. The remaining approximately 0.4% of outstanding common units at March 31, 2018 were owned by certain of our executive officers and directors, certain of their affiliates and other outside investors. As the sole general partner of our operating partnership, Hudson Pacific Properties, Inc. has the full, exclusive and complete responsibility for our operating partnership’s day-to-day management and control.

We believe combining the quarterly reports on Form 10-Q of Hudson Pacific Properties, Inc. and the operating partnership into this single report results in the following benefits:

- enhancing investors’ understanding of our Company and our operating partnership by enabling investors to view the business as a whole in the same manner as management views and operates the business;
- eliminating duplicative disclosure and providing a more streamlined and readable presentation because a substantial portion of the disclosures apply to both our Company and our operating partnership; and
- creating time and cost efficiencies through the preparation of one combined report instead of two separate reports.

There are a few differences between our Company and our operating partnership, which are reflected in the disclosures in this report. We believe it is important to understand the differences between our Company and our operating partnership in the context of how we operate as an interrelated, consolidated company. Hudson Pacific Properties, Inc. is a REIT, the only material assets of which are the units of partnership interest in our operating partnership. As a result, Hudson Pacific Properties, Inc. does not conduct business itself, other than acting as the sole general partner of our operating partnership, issuing equity from time to time and guaranteeing certain debt of our operating partnership. Hudson Pacific Properties, Inc. itself does not issue any indebtedness but guarantees some of the debt of our operating partnership. Our operating partnership, which is structured as a partnership with no publicly traded equity, holds substantially all of the assets of our Company and conducts substantially all of our business. Except for net proceeds from equity issuances by Hudson Pacific Properties, Inc., which are generally contributed to our operating partnership in exchange for units of partnership interest in our operating partnership, our operating partnership generates the capital required by our Company’s business through its operations, its incurrence of indebtedness or through the issuance of units of partnership interest in our operating partnership.

Non-controlling interest, stockholders’ equity and partners’ capital are the main areas of difference between the consolidated financial statements of our Company and those of our operating partnership. The common units in our operating partnership are accounted for as partners’ capital in our operating partnership’s consolidated financial statements and, to the extent not held by our Company, as a non-controlling interest in our Company’s consolidated financial statements. The differences between stockholders’ equity, partners’ capital and non-controlling interest result from the differences in the equity issued by our Company and our operating partnership.

To help investors understand the significant differences between our Company and our operating partnership, this report presents the consolidated financial statements and Note 15, earnings per share, separately for our Company and our operating partnership. All other sections of this report, including “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” are presented together for our Company and our operating partnership.

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In order to establish that the Chief Executive Officer and the Chief Financial Officer of each entity have made the requisite certifications and that our Company and our operating partnership are compliant with Rule 13a-15 or Rule 15d-15 of the Securities Exchange Act of 1934, or the Exchange Act and 18 U.S.C. §1350, this report also includes separate Part I, Item 4 “Controls and

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Procedures” sections and separate Exhibit 31 and 32 certifications for each of Hudson Pacific Properties, Inc. and our operating partnership.

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HUDSON PACIFIC PROPERTIES, INC. AND HUDSON PACIFIC PROPERTIES, L.P.
 QUARTERLY REPORT FOR THE THREE MONTHS ENDED MARCH 31, 2018
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PART I—FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS OF HUDSON PACIFIC PROPERTIES, INC.

HUDSON PACIFIC PROPERTIES, INC.

CONSOLIDATED BALANCE SHEETS

(in thousands, except share data)

	March 31, 2018 (unaudited)	December 31, 2017
ASSETS		
Investment in real estate, at cost	\$6,499,393	\$ 6,423,441
Accumulated depreciation and amortization	(574,814)	(533,498)
Investment in real estate, net	5,924,579	5,889,943
Cash and cash equivalents	64,080	78,922
Restricted cash	10,900	22,358
Accounts receivable, net	5,945	4,363
Straight-line rent receivables, net	119,436	109,457
Deferred leasing costs and lease intangible assets, net	241,912	244,554
Prepaid expenses and other assets, net	69,735	61,138
Assets associated with real estate held for sale	11,704	211,335
TOTAL ASSETS	\$6,448,291	\$ 6,622,070
LIABILITIES AND EQUITY		
Notes payable, net	\$2,240,688	\$ 2,421,380
Accounts payable and accrued liabilities	146,588	163,107
Lease intangible liabilities, net	45,651	49,930
Security deposits and prepaid rent	65,692	64,031
Derivative liabilities	—	265
Liabilities associated with real estate held for sale	630	2,216
TOTAL LIABILITIES	2,499,249	2,700,929
6.25% Series A cumulative redeemable preferred units of the operating partnership	10,177	10,177
EQUITY		
Hudson Pacific Properties, Inc. stockholders' equity:		
Common stock, \$0.01 par value, 490,000,000 authorized, 155,626,055 shares and 155,602,508 shares outstanding at March 31, 2018 and December 31, 2017, respectively	1,556	1,556
Additional paid-in capital	3,625,673	3,622,988
Accumulated other comprehensive income	22,936	13,227
Retained earnings	9,500	—
Total Hudson Pacific Properties, Inc. stockholders' equity	3,659,665	3,637,771
Non-controlling interest—members in consolidated entities	263,556	258,602
Non-controlling interest—units in the operating partnership	15,644	14,591
TOTAL EQUITY	3,938,865	3,910,964
TOTAL LIABILITIES AND EQUITY	\$6,448,291	\$ 6,622,070

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

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HUDSON PACIFIC PROPERTIES, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(unaudited, in thousands, except share data)

	Three Months Ended March 31, 2018	2017
REVENUES		
Office		
Rental	\$ 130,082	\$ 133,516
Tenant recoveries	20,904	17,401
Parking and other	5,546	5,899
Total Office revenues	156,532	156,816
Studio		
Rental	10,383	6,685
Tenant recoveries	354	665
Other property-related revenue	6,435	4,042
Other	414	77
Total Studio revenues	17,586	11,469
TOTAL REVENUES	174,118	168,285
OPERATING EXPENSES		
Office operating expenses	53,240	47,954
Studio operating expenses	9,664	7,251
General and administrative	15,564	13,810
Depreciation and amortization	60,553	70,767
TOTAL OPERATING EXPENSES	139,021	139,782
INCOME FROM OPERATIONS	35,097	28,503
OTHER EXPENSE (INCOME)		
Interest expense	20,503	21,930
Interest income	(9)	(30)
Unrealized gain on ineffective portion of derivatives	—	(6)
Transaction-related expenses	118	—
Other income	(404)	(678)
TOTAL OTHER EXPENSES	20,208	21,216
INCOME BEFORE GAINS ON SALE OF REAL ESTATE	14,889	7,287
Gains on sale of real estate	37,674	16,866
NET INCOME	52,563	24,153
	(159)	(159)

Net income attributable to preferred stock and units				
Net income attributable to participating securities	(327)	(240)
Net income attributable to non-controlling interest in consolidated entities	(3,323)	(3,037)
Net income attributable to non-controlling interest in the operating partnership	(177)	(202)
Net income attributable to Hudson Pacific Properties, Inc. common stockholders	\$ 48,577		\$ 20,515	
Basic and diluted per share amounts:				
Net income attributable to common stockholders—basic	\$ 0.31		\$ 0.14	
Net income attributable to common stockholders—diluted	\$ 0.31		\$ 0.14	
Weighted average shares of common stock outstanding—basic	155,626,055		147,950,594	
Weighted average shares of common stock outstanding—diluted	156,714,822		149,950,346	
Dividends declared per share	\$ 0.25		\$ 0.25	

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

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HUDSON PACIFIC PROPERTIES, INC.
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
 (unaudited, in thousands)

	Three Months Ended March 31,	
	2018	2017
Net income	\$52,563	\$24,153
Other comprehensive income: change in fair value of derivatives	9,513	2,864
Comprehensive income	62,076	27,017
Comprehensive income attributable to preferred stock and units	(159)	(159)
Comprehensive income attributable to participating securities	(391)	(240)
Comprehensive income attributable to non-controlling interest in consolidated entities	(3,323)	(3,037)
Comprehensive income attributable to non-controlling interest in the operating partnership	(211)	(230)
Comprehensive income attributable to Hudson Pacific Properties, Inc. common stockholders	\$57,992	\$23,351

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

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HUDSON PACIFIC PROPERTIES, INC.
CONSOLIDATED STATEMENTS OF EQUITY
(unaudited, in thousands, except share data)

	Hudson Pacific Properties, Inc. Stockholders' Equity							
	Shares of Common Stock	Stock Amount	Additional Paid-in Capital	Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive (Loss) Income	Non- controlling Interest— in the Operating Partnership	Non-controlling Interest— Units in Consolidated Entities	Members Total Equity
Balance at January 1, 2017	136,492,235	\$ 1,364	\$ 3,109,394	\$ (16,971)	\$ 9,496	\$ 294,859	\$ 304,608	\$ 3,702,750
Contributions	—	—	—	—	—	—	3,870	3,870
Distributions	—	—	—	—	—	—	(74,836)	(74,836)
Proceeds from sale of common stock, net of underwriters' discount and transaction costs	18,656,575	187	647,195	—	—	—	—	647,382
Issuance of unrestricted stock	917,086	9	(9)	—	—	—	—	—
Shares withheld to satisfy tax withholding	(463,388)	(4)	(16,037)	—	—	—	—	(16,041)
Declared dividend	—	—	(106,269)	(51,619)	—	(656)	—	(158,544)
Amortization of stock-based compensation	—	—	13,249	—	—	2,666	—	15,915
Net income	—	—	—	68,590	—	375	24,960	93,925
Change in fair value of derivatives	—	—	—	—	7,353	45	—	7,398
Redemption of common units in the operating partnership	—	—	(24,535)	—	(3,622)	(282,698)	—	(310,855)
Balance at December 31, 2017	155,602,508	1,556	3,622,988	—	13,227	14,591	258,602	3,910,964
Cumulative adjustment related to adoption of ASU 2017-12	—	—	—	(231)	230	1	—	—
Contributions	—	—	—	—	—	—	2,691	2,691
Distributions	—	—	—	—	—	—	(1,060)	(1,060)
Proceeds from sale of common stock, net of underwriters'	—	—	(173)	—	—	—	—	(173)

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discount and transaction costs								
Issuance of unrestricted stock	43,900	—	—	—	—	—	—	—
Shares withheld to satisfy tax withholding	(20,353)	—	(693)	—	—	—	—	(693)
Declared dividend	—	—	—	(39,173)	—	(178)	—	(39,351)
Amortization of stock-based compensation	—	—	3,551	—	—	1,019	—	4,570
Net income	—	—	—	48,904	—	177	3,323	52,404
Change in fair value of derivatives	—	—	—	—	9,479	34	—	9,513
Balance at March 31, 2018	155,626,055	\$ 1,556	\$ 3,625,673	\$ 9,500	\$ 22,936	\$ 15,644	\$ 263,556	\$ 3,938,865

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

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HUDSON PACIFIC PROPERTIES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited, in thousands)

	Three Months Ended March 31,	
	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$52,563	\$24,153
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	60,553	70,767
Non-cash portion of interest expense	1,658	1,186
Amortization of stock-based compensation	4,338	3,902
Straight-line rents	(9,942)	2,366
Straight-line rent expenses	136	381
Amortization of above- and below-market leases, net	(3,811)	(5,732)
Amortization of above- and below-market ground lease, net	624	637
Amortization of lease incentive costs	303	379
Other non-cash adjustments ⁽¹⁾	256	539
Gains on sale of real estate	(37,674)	(16,866)
Change in operating assets and liabilities:		
Accounts receivable	(1,782)	4,650
Deferred leasing costs and lease intangibles	(6,614)	(6,635)
Prepaid expenses and other assets	3,313	(1,072)
Accounts payable and accrued liabilities	(33)	12,378
Security deposits and prepaid rent	559	(5,313)
Net cash provided by operating activities	64,447	85,720
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to investment property	(103,512)	(76,225)
Proceeds from sale of real estate	237,004	81,707
Contributions to unconsolidated entity	—	(1,071)
Deposits for property acquisitions	—	(56,323)
Net cash provided by (used in) investing activities	133,492	(51,912)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from notes payable	130,000	—
Payments of notes payable	(308,529)	(300,642)
Proceeds from issuance of common stock, net	(173)	647,675
Payment for redemption of common units in the operating partnership	—	(310,855)
Distributions paid to common stock and unitholders	(39,351)	(39,919)
Distributions paid to preferred unitholders	(159)	(159)
Contributions from non-controlling member in consolidated entities	2,691	103
Distributions to non-controlling member in consolidated entities	(1,060)	(310)
Payments to satisfy tax withholding	(693)	(4,203)
Payments of loan costs	(6,965)	—
Net cash used in financing activities	(224,239)	(8,310)
Net increase in cash and cash equivalents and restricted cash	(26,300)	25,498
Cash and cash equivalents and restricted cash—beginning of period	101,280	108,192
Cash and cash equivalents and restricted cash—end of period	\$74,980	\$133,690

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:

Cash paid for interest, net of capitalized interest	\$12,915	\$16,172
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NON-CASH INVESTING ACTIVITIES:

Accounts payable and accrued liabilities for real estate investments	\$20,462	\$3,501
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(1) Represents bad debt expense/recovery and unrealized loss/gain on ineffective portion of derivative instruments.

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

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ITEM 1. FINANCIAL STATEMENTS OF HUDSON PACIFIC PROPERTIES, L.P.

HUDSON PACIFIC PROPERTIES, L.P.
CONSOLIDATED BALANCE SHEETS
(in thousands, except unit data)

	March 31, 2018 (unaudited)	December 31, 2017
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Investment in real estate, at cost	\$6,499,393	\$ 6,423,441
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Straight-line rent receivables, net	119,436	109,457
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Prepaid expenses and other assets, net	69,735	61,138
Assets associated with real estate held for sale	11,704	211,335
TOTAL ASSETS	\$6,448,291	\$ 6,622,070
LIABILITIES		
Notes payable, net	\$2,240,688	\$ 2,421,380
Accounts payable and accrued liabilities	146,588	163,107
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Derivative liabilities	—	265
Liabilities associated with real estate held for sale	630	2,216
TOTAL LIABILITIES	2,499,249	2,700,929
6.25% Series A cumulative redeemable preferred units of the operating partnership	10,177	10,177
CAPITAL		
Hudson Pacific Properties, L.P. partners' capital:		
Common units, 156,195,100 and 156,171,553 issued and outstanding at March 31, 2018 and December 31, 2017, respectively.	3,652,289	3,639,086
Accumulated other comprehensive income	23,020	13,276
Total Hudson Pacific Properties, L.P. partners' capital	3,675,309	3,652,362
Non-controlling interest—members in consolidated entities	263,556	258,602
TOTAL CAPITAL	3,938,865	3,910,964
TOTAL LIABILITIES AND CAPITAL	\$6,448,291	\$