

BOSTON PROPERTIES INC
Form 10-Q
August 07, 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 1934

For the Quarterly Period Ended June 30, 2018

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: 1-13087 (Boston Properties, Inc.)

Commission File Number: 0-50209 (Boston Properties Limited Partnership)

BOSTON PROPERTIES, INC.
BOSTON PROPERTIES LIMITED PARTNERSHIP
(Exact name of Registrants as specified in its charter)

Boston Properties, Inc.	Delaware (State or other jurisdiction of incorporation or organization)	04-2473675 (I.R.S. Employer Identification Number)
Boston Properties Limited Partnership	Delaware (State or other jurisdiction of incorporation or organization)	04-3372948 (I.R.S. Employer Identification Number)

Prudential Center, 800 Boylston Street, Suite 1900, Boston, Massachusetts 02199-8103
(Address of principal executive offices) (Zip Code)
(617) 236-3300
(Registrants' 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.

Boston Properties, Inc.: Yes No Boston Properties Limited Partnership: Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, 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).

Boston Properties, Inc.: Yes No Boston Properties Limited Partnership: Yes No

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

Boston Properties, Inc.:

Large accelerated filer
growth company

Accelerated filer

Non-accelerated filer

Smaller reporting company

Emerging

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Boston Properties Limited Partnership:

Large accelerated filer Accelerated filer Non-accelerated filer

x 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.

Boston Properties, Inc. Boston Properties Limited Partnership

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Boston Properties, Inc.: Yes No x Boston Properties Limited Partnership: Yes No x

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

Boston Properties, Inc. Common Stock, par value \$0.01 per share 154,419,806

(Registrant) (Class) (Outstanding on August 2, 2018)

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EXPLANATORY NOTE

This report combines the quarterly reports on Form 10-Q for the period ended June 30, 2018 of Boston Properties, Inc. and Boston Properties Limited Partnership. Unless stated otherwise or the context otherwise requires, references to “BXP” mean Boston Properties, Inc., a Delaware corporation and real estate investment trust (“REIT”), and references to “BPLP” and the “Operating Partnership” mean Boston Properties Limited Partnership, a Delaware limited partnership. BPLP is the entity through which BXP conducts substantially all of its business and owns, either directly or through subsidiaries, substantially all of its assets. BXP is the sole general partner and also a limited partner of BPLP. As the sole general partner of BPLP, BXP has exclusive control of BPLP’s day-to-day management. Therefore, unless stated otherwise or the context requires, references to the “Company,” “we,” “us” and “our” mean collectively BXP, BPLP and those entities/subsidiaries consolidated by BXP.

As of June 30, 2018, BXP owned an approximate 89.7% ownership interest in BPLP. The remaining approximate 10.3% interest is owned by limited partners. The other limited partners of BPLP are (1) persons who contributed their direct or indirect interests in properties to BPLP in exchange for common units or preferred units of limited partnership interest in BPLP and/or (2) recipients of long term incentive plan units of BPLP pursuant to BXP’s Stock Option and Incentive Plans. Under the limited partnership agreement of BPLP, unitholders may present their common units of BPLP for redemption at any time (subject to restrictions agreed upon at the time of issuance of the units that may restrict such right for a period of time, generally one year from issuance). Upon presentation of a common unit for redemption, BPLP must redeem the unit for cash equal to the then value of a share of BXP’s common stock. In lieu of a cash redemption by BPLP, however, BXP may elect to acquire any common units so tendered by issuing shares of BXP common stock in exchange for the common units. If BXP so elects, its common stock will be exchanged for common units on a one-for-one basis. This one-for-one exchange ratio is subject to specified adjustments to prevent dilution. BXP generally expects that it will elect to issue its common stock in connection with each such presentation for redemption rather than having BPLP pay cash. With each such exchange or redemption, BXP’s percentage ownership in BPLP will increase. In addition, whenever BXP issues shares of its common stock other than to acquire common units of BPLP, BXP must contribute any net proceeds it receives to BPLP and BPLP must issue to BXP an equivalent number of common units of BPLP. This structure is commonly referred to as an umbrella partnership REIT, or UPREIT.

The Company believes that combining the quarterly reports on Form 10-Q of BXP and BPLP into this single report provides the following benefits:

- enhances investors’ understanding of BXP and BPLP by enabling investors to view the business as a whole in the same manner as management views and operates the business;
- eliminates duplicative disclosure and provides a more concise and readable presentation because a substantial portion of the disclosure applies to both BXP and BPLP; and
- creates time and cost efficiencies through the preparation of one combined report instead of two separate reports.

The Company believes it is important to understand the few differences between BXP and BPLP in the context of how BXP and BPLP operate as a consolidated company. The financial results of BPLP are consolidated into the financial statements of BXP. BXP does not have any other significant assets, liabilities or operations, other than its investment in BPLP, nor does it have employees of its own. BPLP, not BXP, generally executes all significant business relationships other than transactions involving the securities of BXP. BPLP holds substantially all of the assets of BXP, including ownership interests in joint ventures. BPLP conducts the operations of the business and is structured as a partnership with no publicly traded equity. Except for the net proceeds from equity offerings by BXP, which are contributed to the capital of BPLP in exchange for common or preferred units of partnership in BPLP, as applicable, BPLP generates all remaining capital required by the Company’s business. These sources include working capital, net cash provided by operating activities, borrowings under its credit facilities, the issuance of secured and unsecured debt and equity securities and proceeds received from the disposition of certain properties and interests in joint ventures. Shareholders’ equity, partners’ capital and noncontrolling interests are the main areas of difference between the consolidated financial statements of BXP and BPLP. The limited partners of BPLP are accounted for as partners’ capital in BPLP’s financial statements and as noncontrolling interests in BXP’s financial statements. The noncontrolling interests in BPLP’s financial statements include the interests of unaffiliated partners in various consolidated

partnerships. The noncontrolling interests in BXP's financial statements include the same

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noncontrolling interests at BPLP's level and limited partners of BPLP. The differences between shareholders' equity and partners' capital result from differences in the equity issued at BXP and BPLP levels.

In addition, the consolidated financial statements of BXP and BPLP differ in total real estate assets resulting from previously applied acquisition accounting by BXP for the issuance of common stock in connection with non-sponsor redemptions of common units of BPLP. This accounting resulted in a step-up of the real estate assets at BXP. This resulted in a difference between the net real estate of BXP as compared to BPLP of approximately \$311.9 million, or 1.9% at June 30, 2018 and a corresponding difference in depreciation expense and gains on sales of real estate upon the sale of certain properties having an allocation of the real estate step-up. The acquisition accounting was nullified on a prospective basis beginning in 2009 as a result of the Company's adoption of a new accounting standard requiring any future redemptions to be accounted for solely as an equity transaction.

To help investors better understand the key differences between BXP and BPLP, certain information for BXP and BPLP in this report has been separated, as set forth below:

Item 1. Financial Statements (unaudited), which includes the following specific disclosures for BXP and BPLP:

- Note 3. Real Estate;
- Note 7. Noncontrolling Interests;
- Note 8. Stockholders' Equity / Partners' Capital;
- Note 9. Earnings Per Share / Common Unit; and
- Note 11. Segment Information

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations includes information specific to each entity, where applicable; and

Item 2. Liquidity and Capital Resources includes separate reconciliations of amounts to each entity's financial statements, where applicable.

This report also includes separate Part I - Item 4. Controls and Procedures and Part II - Item 2. Unregistered Sales of Equity Securities and Use of Proceeds sections for each of BXP and BPLP, as well as separate Exhibits 12, 31 and 32 calculation of ratios of earnings to fixed charges and certifications for each of BXP and BPLP.

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BOSTON PROPERTIES, INC. AND BOSTON PROPERTIES LIMITED PARTNERSHIP
 FORM 10-Q
 for the quarter ended June 30, 2018
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PART I. FINANCIAL INFORMATION

ITEM 1—Financial Statements.

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BOSTON PROPERTIES, INC.
CONSOLIDATED BALANCE SHEETS
(Unaudited)

	June 30, 2018	December 31, 2017
	(in thousands, except for share and par value amounts)	
ASSETS		
Real estate, at cost (amounts related to variable interest entities (“VIEs”) of \$7,358,363 and \$7,172,718 at June 30, 2018 and December 31, 2017, respectively)	\$21,526,520	\$21,096,642
Less: accumulated depreciation (amounts related to VIEs of \$(910,381) and \$(854,172) at June 30, 2018 and December 31, 2017, respectively)	(4,745,590)	(4,589,634)
Total real estate	16,780,930	16,507,008
Cash and cash equivalents (amounts related to VIEs of \$277,252 and \$304,955 at June 30, 2018 and December 31, 2017, respectively)	472,555	434,767
Cash held in escrows (amounts related to VIEs of \$6,099 and \$6,135 at June 30, 2018 and December 31, 2017, respectively)	254,505	70,602
Investments in securities	30,063	29,161
Tenant and other receivables (amounts related to VIEs of \$17,130 and \$27,057 at June 30, 2018 and December 31, 2017, respectively)	63,660	92,186
Accrued rental income (amounts related to VIEs of \$268,120 and \$242,589 at June 30, 2018 and December 31, 2017, respectively)	912,652	861,575
Deferred charges, net (amounts related to VIEs of \$264,973 and \$281,678 at June 30, 2018 and December 31, 2017, respectively)	678,319	679,038
Prepaid expenses and other assets (amounts related to VIEs of \$34,853 and \$33,666 at June 30, 2018 and December 31, 2017, respectively)	85,972	77,971
Investments in unconsolidated joint ventures	682,507	619,925
Total assets	\$19,961,163	\$19,372,233
LIABILITIES AND EQUITY		
Liabilities:		
Mortgage notes payable, net (amounts related to VIEs of \$2,934,336 and \$2,939,183 at June 30, 2018 and December 31, 2017, respectively)	\$2,972,052	\$2,979,281
Unsecured senior notes, net	7,251,578	7,247,330
Unsecured line of credit	—	45,000
Unsecured term loan, net	498,248	—
Accounts payable and accrued expenses (amounts related to VIEs of \$80,098 and \$106,683 at June 30, 2018 and December 31, 2017, respectively)	327,067	331,500
Dividends and distributions payable	139,263	139,040
Accrued interest payable (amounts related to VIEs of \$6,669 and \$6,907 at June 30, 2018 and December 31, 2017, respectively)	96,844	83,646
Other liabilities (amounts related to VIEs of \$183,114 and \$164,806 at June 30, 2018 and December 31, 2017, respectively)	462,869	443,980
Total liabilities	11,747,921	11,269,777
Commitments and contingencies	—	—
Equity:		
Stockholders’ equity attributable to Boston Properties, Inc.:		
Excess stock, \$0.01 par value, 150,000,000 shares authorized, none issued or outstanding	—	—

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Preferred stock, \$0.01 par value, 50,000,000 shares authorized; 5.25% Series B cumulative redeemable preferred stock, \$0.01 par value, liquidation preference \$2,500 per share, 92,000 shares authorized, 80,000 shares issued and outstanding at June 30, 2018 and December 31, 2017	200,000	200,000
Common stock, \$0.01 par value, 250,000,000 shares authorized, 154,490,429 and 154,404,186 issued and 154,411,529 and 154,325,286 outstanding at June 30, 2018 and December 31, 2017, respectively	1,544	1,543
Additional paid-in capital	6,391,460	6,377,908
Dividends in excess of earnings	(649,747) (712,343)
Treasury common stock at cost, 78,900 shares at June 30, 2018 and December 31, 2017	(2,722) (2,722)
Accumulated other comprehensive loss	(47,695) (50,429)
Total stockholders' equity attributable to Boston Properties, Inc.	5,892,840	5,813,957
Noncontrolling interests:		
Common units of Boston Properties Limited Partnership	621,221	604,739
Property partnerships	1,699,181	1,683,760
Total equity	8,213,242	8,102,456
Total liabilities and equity	\$ 19,961,163	\$ 19,372,233

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

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BOSTON PROPERTIES, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2018	2017	2018	2017
	(in thousands, except for per share amounts)			
Revenue				
Rental				
Base rent	\$516,439	\$520,542	\$1,035,946	\$1,024,104
Recoveries from tenants	95,259	89,163	190,377	178,327
Parking and other	26,904	26,462	53,038	52,072
Total rental revenue	638,602	636,167	1,279,361	1,254,503
Hotel revenue	14,607	13,375	23,709	20,795
Development and management services	9,305	7,365	17,710	13,837
Direct reimbursements of payroll and related costs from management services contracts	1,970	—	4,855	—
Total revenue	664,484	656,907	1,325,635	1,289,135
Expenses				
Operating				
Rental	237,790	230,454	478,119	458,741
Hotel	8,741	8,404	16,814	15,495
General and administrative	28,468	27,141	64,362	58,527
Payroll and related costs from management services contracts	1,970	—	4,855	—
Transaction costs	474	299	495	333
Depreciation and amortization	156,417	151,919	322,214	311,124
Total expenses	433,860	418,217	886,859	844,220
Operating income	230,624	238,690	438,776	444,915
Other income (expense)				
Income from unconsolidated joint ventures	769	3,108	1,230	6,192
Interest and other income	2,579	1,504	4,227	2,118
Gains from investments in securities	505	730	379	1,772
Gains from early extinguishments of debt	—	14,354	—	14,354
Interest expense	(92,204)	(95,143)	(182,424)	(190,677)
Income before gains on sales of real estate	142,273	163,243	262,188	278,674
Gains on sales of real estate	18,292	3,767	114,689	3,900
Net income	160,565	167,010	376,877	282,574
Net income attributable to noncontrolling interests				
Noncontrolling interests in property partnerships	(14,400)	(15,203)	(31,634)	(19,627)
Noncontrolling interest—common units of Boston Properties Limited Partnership	(14,859)	(15,473)	(35,311)	(26,933)
Net income attributable to Boston Properties, Inc.	131,306	136,334	309,932	236,014
Preferred dividends	(2,625)	(2,625)	(5,250)	(5,250)
Net income attributable to Boston Properties, Inc. common shareholders	\$128,681	\$133,709	\$304,682	\$230,764
Basic earnings per common share attributable to Boston Properties, Inc. common shareholders:				
Net income	\$0.83	\$0.87	\$1.97	\$1.50
Weighted average number of common shares outstanding	154,415	154,177	154,400	154,019

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Diluted earnings per common share attributable to Boston
Properties, Inc. common shareholders:

Net income	\$0.83	\$0.87	\$1.97	\$1.50
Weighted average number of common and common equivalent shares outstanding	154,571	154,331	154,638	154,273
Dividends per common share	\$0.80	\$0.75	\$1.60	\$1.50

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

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BOSTON PROPERTIES, INC.
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
 (Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2018	2017	2018	2017
	(in thousands)			
Net income	\$160,565	\$167,010	\$376,877	\$282,574
Other comprehensive income (loss):				
Effective portion of interest rate contracts	—	(6,313)	—	(6,133)
Amortization of interest rate contracts (1)	1,666	1,397	3,332	2,703
Other comprehensive income (loss)	1,666	(4,916)	3,332	(3,430)
Comprehensive income	162,231	162,094	380,209	279,144
Net income attributable to noncontrolling interests	(29,259)	(30,676)	(66,945)	(46,560)
Other comprehensive (income) loss attributable to noncontrolling interests	(299)	2,738	(598)	2,520
Comprehensive income attributable to Boston Properties, Inc.	\$132,673	\$134,156	\$312,666	\$235,104

(1) Amounts reclassified from comprehensive income primarily to interest expense within the Boston Properties, Inc.'s Consolidated Statements of Operations.

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

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BOSTON PROPERTIES, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(Unaudited and in thousands)

	Common Stock		Preferred Stock	Additional Paid-in Capital	Dividends in Excess of Earnings	Treasury Stock, at cost	Accumulated Other Comprehensive Loss	Noncontrolling Interests	Total
	Shares	Amount							
Equity, December 31, 2017	154,325	\$1,543	\$200,000	\$6,377,908	\$(712,343)	\$(2,722)	\$(50,429)	\$2,288,499	\$8,102,456
Cumulative effect of a change in accounting principle	—	—	—	—	4,933	—	—	563	5,496
Redemption of operating partnership units to common stock	35	1	—	1,195	—	—	—	(1,196)	—
Allocated net income for the year	—	—	—	—	309,932	—	—	66,945	376,877
Dividends/distributions declared	—	—	—	—	(252,269)	—	—	(28,708)	(280,977)
Shares issued pursuant to stock purchase plan	3	—	—	429	—	—	—	—	429
Net activity from stock option and incentive plan	49	—	—	600	—	—	—	21,530	22,130
Contributions from noncontrolling interests in property partnerships	—	—	—	—	—	—	—	27,532	27,532
Distributions to noncontrolling interests in property partnerships	—	—	—	—	—	—	—	(44,033)	(44,033)
Amortization of interest rate contracts	—	—	—	—	—	—	2,734	598	3,332
Reallocation of noncontrolling interest	—	—	—	11,328	—	—	—	(11,328)	—
Equity, June 30, 2018	154,412	\$1,544	\$200,000	\$6,391,460	\$(649,747)	\$(2,722)	\$(47,695)	\$2,320,402	\$8,213,242
Equity, December 31, 2016	153,790	\$1,538	\$200,000	\$6,333,424	\$(693,694)	\$(2,722)	\$(52,251)	\$2,145,629	\$7,931,924
Redemption of operating partnership units to common stock	481	5	—	16,417	—	—	—	(16,422)	—
Allocated net income for the year	—	—	—	—	236,014	—	—	46,560	282,574
Dividends/distributions declared	—	—	—	—	(236,368)	—	—	(26,977)	(263,345)
Shares issued pursuant to stock purchase plan	3	—	—	373	—	—	—	—	373

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Net activity from stock option and incentive plan	34	—	—	1,980	—	—	—	19,188	21,168
Cumulative effect of a change in accounting principle	—	—	—	—	(272)	—	(1,763) (2,035
Contributions from noncontrolling interests in property partnerships	—	—	—	—	—	—	—	133,072	133,072
Distributions to noncontrolling interests in property partnerships	—	—	—	—	—	—	—	(26,949) (26,949
Effective portion of interest rate contracts	—	—	—	—	—	—	(3,301) (2,832) (6,133
Amortization of interest rate contracts	—	—	—	—	—	—	2,391	312	2,703
Reallocation of noncontrolling interest	—	—	—	10,840	—	—	—	(10,840) —
Equity, June 30, 2017	154,308	\$1,543	\$200,000	\$6,363,034	\$(694,320)	\$(2,722)	\$(53,161)	\$2,258,978	\$8,073,352

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

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BOSTON PROPERTIES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	For the six months ended June 30,	
	2018	2017
	(in thousands)	
Cash flows from operating activities:		
Net income	\$376,877	\$282,574
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	322,214	311,124
Non-cash compensation expense	23,243	19,237
Income from unconsolidated joint ventures	(1,230)	(6,192)
Distributions of net cash flow from operations of unconsolidated joint ventures	1,663	2,905
Gains from investments in securities	(379)	(1,772)
Gains from early extinguishments of debt	—	(14,354)
Non-cash portion of interest expense	10,607	(11,979)
Gains on sales of real estate	(114,689)	(3,900)
Change in assets and liabilities:		
Tenant and other receivables, net	33,012	2,033
Accrued rental income, net	(45,759)	(19,348)
Prepaid expenses and other assets	(4,641)	36,223
Accounts payable and accrued expenses	(9,899)	(2,608)
Accrued interest payable	12,999	(158,761)
Other liabilities	11,571	(33,121)
Tenant leasing costs	(54,743)	(37,252)
Total adjustments	183,969	82,235
Net cash provided by operating activities	560,846	364,809
Cash flows from investing activities:		
Acquisition of real estate	—	(15,953)
Construction in progress	(380,565)	(297,747)
Building and other capital improvements	(96,730)	(100,808)
Tenant improvements	(83,982)	(107,533)
Proceeds from sales of real estate	141,249	17,049
Capital contributions to unconsolidated joint ventures	(65,250)	(41,491)
Investments in securities, net	(523)	(1,195)
Net cash used in investing activities	(485,801)	(547,678)

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BOSTON PROPERTIES, INC.
 CONSOLIDATED STATEMENTS OF CASH FLOWS
 (Unaudited)

For the six
 months ended
 June 30,
 2018 2017
 (in thousands)

Cash flows from financing activities:

Proceeds from mortgage notes payable	—	2,300,000
Repayments of mortgage notes payable	Ø9,192	Ø1,308,708
Borrowings on unsecured line of credit	345,000	Ø30,000
Repayments of unsecured line of credit	Ø390,000	