

ESSEX PROPERTY TRUST INC
Form 10-Q
May 03, 2016

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

FORM 10-Q

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

For the quarterly period ended March 31, 2016

OR

o 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 001-13106

ESSEX PROPERTY TRUST, INC.
ESSEX PORTFOLIO, L.P.
(Exact name of Registrant as Specified in its Charter)
Maryland (Essex Property Trust, Inc.)
California (Essex Portfolio, L.P.)

77-0369576 (Essex Property Trust, Inc.)
77-0369575 (Essex Portfolio, L.P.)

(State or Other Jurisdiction of Incorporation or Organization) (I.R.S. Employer Identification Number)
1100 Park Place, Suite 200
San Mateo, California 94403
(Address of Principal Executive Offices including Zip Code)

(650) 655-7800
(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 reports), and (2) has been subject to such filing requirements for the past 90 days.

Essex Property Trust, Inc. Yes No Essex Portfolio, L.P. 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).

Essex Property Trust, Inc. Yes No Essex Portfolio, L.P. 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 the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

i

Essex Property Trust, Inc.:

Large accelerated filer Accelerated filer Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Essex Portfolio, L.P.:

Large accelerated filer Accelerated filer Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Essex Property Trust, Inc. Yes No Essex Portfolio, L.P. Yes No

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 65,430,092 shares of Common Stock (\$0.0001 par value) of Essex Property Trust, Inc. were outstanding as of April 28, 2016.

EXPLANATORY NOTE

This report combines the reports on Form 10-Q for the three month period ended March 31, 2016 of Essex Property Trust, Inc. and Essex Portfolio, L.P. Unless stated otherwise or the context otherwise requires, references to “Essex” mean Essex Property Trust, Inc., a Maryland corporation that operates as a self-administered and self-managed real estate investment trust (“REIT”), and references to “EPLP” mean Essex Portfolio, L.P. (the “Operating Partnership”). References to the “Company,” “we,” “us” or “our” mean collectively Essex, EPLP and those entities/subsidiaries owned or controlled by Essex and/or EPLP. References to the “Operating Partnership” mean collectively EPLP and those entities/subsidiaries owned or controlled by EPLP.

Essex is the general partner of EPLP and as the sole general partner of EPLP, Essex has exclusive control of EPLP's day-to-day management.

The Company is structured as an umbrella partnership REIT (“UPREIT”) and Essex contributes all net proceeds from its various equity offerings to the Operating Partnership. In return for those contributions, Essex receives a number of OP Units (see definition below) in the Operating Partnership equal to the number of shares of common stock it has issued in the equity offering. Contributions of properties to the Company can be structured as tax-deferred transactions through the issuance of OP Units in the Operating Partnership, which is one of the reasons why the Company is structured in the manner outlined above. Based on the terms of EPLP's partnership agreement, OP Units can be exchanged with Essex common stock on a one-for-one basis. The Company maintains a one-for-one relationship between the OP Units of the Operating Partnership issued to Essex and shares of common stock.

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

- enhances investors' understanding of the Company and the Operating Partnership 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 streamlined and readable presentation since a substantial portion of the disclosure applies to both the Company and the Operating Partnership; and
- creates time and cost efficiencies through the preparation of one combined report instead of two separate reports.

Management operates the Company and the Operating Partnership as one business. The management of Essex consists of the same members as the management of EPLP.

All of the Company's property ownership, development and related business operations are conducted through the Operating Partnership and Essex has no material assets, other than its investment in EPLP. Essex's primary function is acting as the general partner of EPLP. As general partner with control of the Operating Partnership, the Company consolidates the Operating Partnership for financial reporting purposes. Therefore, the assets and liabilities of the Company and the Operating Partnership are the same on their respective financial statements. Essex also issues equity from time to time and guarantees certain debt of EPLP, as disclosed in this report. The Operating Partnership holds substantially all of the assets of the Company, including the Company's ownership interests in its joint ventures. The Operating Partnership 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 the Company, which are contributed to the capital of the Operating Partnership in exchange for additional limited partnership interests in the Operating Partnership (“OP Units”) (on a one-for-one share of common stock per OP Unit basis), the Operating Partnership generates all remaining capital required by the Company's business. These sources include the Operating Partnership's working capital, net cash provided by operating activities, borrowings under its revolving credit facilities, the issuance of secured and unsecured debt and equity securities and proceeds received from disposition of certain properties and joint ventures.

The Company believes it is important to understand the few differences between Essex and EPLP in the context of how Essex and EPLP operate as a consolidated company. Stockholders' equity, partners' capital and noncontrolling interest are the main areas of difference between the consolidated financial statements of the Company and those of the Operating Partnership. The limited partners of the Operating Partnership are accounted for as partners' capital in the Operating Partnership's consolidated financial statements and as noncontrolling interest in Essex's consolidated financial statements. The noncontrolling interest in the Operating Partnership's consolidated financial statements include the interest of unaffiliated partners in various consolidated partnerships and joint venture partners. The noncontrolling interest in the Company's consolidated financial statements include (i) the same noncontrolling interest as presented in the Operating Partnership's consolidated financial statements and (ii) limited partner OP Unitholders of the Operating Partnership. The differences between stockholders' equity and partners' capital result from differences in the equity issued at the Company and Operating Partnership levels.

To help investors understand the significant differences between the Company and the Operating Partnership, this report provides separate consolidated financial statements for the Company and the Operating Partnership; a single set of consolidated notes to such financial statements that includes separate discussions of stockholders' equity or partners' capital, and earnings per share/unit, as applicable; and a combined Management's Discussion and Analysis of Financial Condition and Results of Operations.

This report also includes separate Part I, Item 4. Controls and Procedures sections and separate Exhibits 31 and 32 certifications for each of the Company and the Operating Partnership in order to establish that the requisite certifications have been made and that the Company and the Operating Partnership are compliant with Rule 13a-15 or Rule 15d-15 of the Securities Exchange Act of 1934 and 18 U.S.C. §1350.

In order to highlight the differences between the Company and the Operating Partnership, the separate sections in this report for the Company and the Operating Partnership specifically refer to the Company and the Operating Partnership. In the sections that combine disclosure of the Company and the Operating Partnership, this report refers to actions or holdings as being actions or holdings of the Company. Although the Operating Partnership is generally the entity that directly or indirectly enters into contracts and joint ventures and holds assets and debt, reference to the Company is appropriate because the Company is one business and the Company operates that business through the Operating Partnership. The separate discussions of the Company and the Operating Partnership in this report should be read in conjunction with each other to understand the results of the Company on a consolidated basis and how management operates the Company.

The information furnished in the accompanying unaudited condensed consolidated balance sheets, statements of income and comprehensive income, equity, capital, and cash flows of the Company and the Operating Partnership reflect all adjustments which are, in the opinion of management, necessary for a fair presentation of the aforementioned condensed consolidated financial statements for the interim periods and are normal and recurring in nature, except as otherwise noted.

The accompanying unaudited condensed consolidated financial statements should be read in conjunction with the notes to such unaudited condensed consolidated financial statements and Management's Discussion and Analysis of Financial Condition and Results of Operations herein. Additionally, these unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements included in the Company's annual report on Form 10-K for the year ended December 31, 2015.

ESSEX PROPERTY TRUST, INC.
 ESSEX PORTFOLIO, L.P.
 FORM 10-Q
 INDEX

PART I. FINANCIAL INFORMATION	Page No.
Item 1. Condensed Consolidated Financial Statements of Essex Property Trust, Inc. (Unaudited)	
<u>Condensed Consolidated Balance Sheets as of March 31, 2016 and December 31, 2015</u>	<u>2</u>
<u>Condensed Consolidated Statements of Income and Comprehensive Income for the three months ended March 31, 2016 and 2015</u>	<u>3</u>
<u>Condensed Consolidated Statement of Equity for the three months ended March 31, 2016</u>	<u>4</u>
<u>Condensed Consolidated Statements of Cash Flows for the three months ended March 31, 2016 and 2015</u>	<u>5</u>
Condensed Consolidated Financial Statements of Essex Portfolio L.P. (Unaudited)	
<u>Condensed Consolidated Balance Sheets as of March 31, 2016 and December 31, 2015</u>	<u>7</u>
<u>Condensed Consolidated Statements of Income and Comprehensive Income for the three months ended March 31, 2016 and 2015</u>	<u>8</u>
<u>Condensed Consolidated Statement of Capital for the three months ended March 31, 2016</u>	<u>9</u>
<u>Condensed Consolidated Statements of Cash Flows for the three months ended March 31, 2016 and 2015</u>	<u>10</u>
<u>Notes to Condensed Consolidated Financial Statements</u>	<u>12</u>
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>25</u>
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risks</u>	<u>32</u>
Item 4. <u>Controls and Procedures</u>	<u>33</u>
PART II. OTHER INFORMATION	
Item 1. <u>Legal Proceedings</u>	<u>34</u>
Item 1A. <u>Risk Factors</u>	<u>34</u>
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>34</u>
Item 5. <u>Other Information</u>	<u>34</u>

Item 6. Exhibits 35

Signatures 36

1

Part I – Financial Information

Item 1. Condensed Financial Statements

ESSEX PROPERTY TRUST, INC. AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

(Unaudited)

(In thousands, except share amounts)

	March 31, 2016	December 31, 2015
ASSETS		
Real estate:		
Rental properties:		
Land and land improvements	\$2,573,923	\$2,522,842
Buildings and improvements	10,052,754	9,808,627
	12,626,677	12,331,469
Less accumulated depreciation	(2,051,802)	(1,949,892)
	10,574,875	10,381,577
Real estate under development	145,711	242,326
Co-investments	1,069,684	1,036,047
Real estate held for sale, net	—	26,879
	11,790,270	11,686,829
Cash and cash equivalents-unrestricted	48,164	29,683
Cash and cash equivalents-restricted	32,319	93,372
Marketable securities	138,597	137,485
Notes and other receivables	18,198	19,285
Prepaid expenses and other assets	39,936	38,437
Total assets	\$12,067,484	\$12,005,091
LIABILITIES AND EQUITY		
Unsecured debt, net	\$2,936,463	\$3,088,680
Mortgage notes payable, net	2,252,057	2,215,077
Lines of credit, net	164,282	11,707
Accounts payable and accrued liabilities	170,444	131,415
Construction payable	36,822	40,953
Dividends payable	111,409	100,266
Other liabilities	34,814	34,518
Cumulative redeemable 7.125% Series H preferred stock at liquidation value	73,750	—
Total liabilities	5,780,041	5,622,616
Commitments and contingencies		
Redeemable noncontrolling interest	46,203	45,452
Equity:		
Common stock; \$0.0001 par value, 656,020,000 shares authorized; 65,426,726 and 65,379,359 shares issued and outstanding, respectively	6	6
Cumulative redeemable 7.125% Series H preferred stock at liquidation value	—	73,750
Additional paid-in capital	7,010,181	7,003,317
Distributions in excess of accumulated earnings	(824,046)	(797,329)
Accumulated other comprehensive loss, net	(44,149)	(42,011)
Total stockholders' equity	6,141,992	6,237,733
Noncontrolling interest	99,248	99,290
Total equity	6,241,240	6,337,023

Total liabilities and equity	\$ 12,067,484	\$ 12,005,091
------------------------------	---------------	---------------

See accompanying notes to the unaudited condensed consolidated financial statements.

2

ESSEX PROPERTY TRUST, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Income and Comprehensive Income
(Unaudited)
(In thousands, except share and per share amounts)

	Three Months Ended March 31,	
	2016	2015
Revenues:		
Rental and other property	\$312,178	\$280,229
Management and other fees from affiliates	2,024	2,644
	314,202	282,873
Expenses:		
Property operating, excluding real estate taxes	60,071	55,618
Real estate taxes	34,419	31,553
Depreciation and amortization	109,707	106,907
General and administrative	9,182	10,545
Merger and integration expenses	—	2,388
Acquisition and investment related costs	828	547
	214,207	207,558
Earnings from operations	99,995	75,315
Interest expense	(52,466)	(47,546)
Total return swap income	3,123	—
Interest and other income	5,208	4,199
Equity income in co-investments	15,068	4,311
Gain on sale of real estate and land	20,258	7,112
Deferred tax expense on gain on sale of real estate and land	(4,279)	—
Gain on remeasurement of co-investment	—	21,362
Net income	86,907	64,753
Net income attributable to noncontrolling interest	(5,071)	(4,076)
Net income attributable to controlling interest	81,836	60,677
Dividends to preferred stockholders	(1,314)	(1,314)
Excess of redemption value of preferred stock over the carrying value	(2,541)	—
Net income available to common stockholders	\$77,981	\$59,363
Comprehensive income	\$84,696	\$65,352
Comprehensive income attributable to noncontrolling interest	(4,998)	(4,091)
Comprehensive income attributable to controlling interest	\$79,698	\$61,261
Per share data:		
Basic:		
Net income available to common stockholders	\$1.19	\$0.92
Weighted average number of shares outstanding during the period	65,405,654	64,185,455
Diluted:		
Net income available to common stockholders	\$1.19	\$0.92
Weighted average number of shares outstanding during the period	65,557,639	64,394,680
Dividend per common share	\$1.60	\$1.44

See accompanying notes to the unaudited condensed consolidated financial statements.

ESSEX PROPERTY TRUST, INC. AND SUBSIDIARIES

Condensed Consolidated Statement of Equity for the three months ended March 31, 2016

(Unaudited)

(Dollars and shares in thousands)

	Series H Preferred stock		Common stock		Additional paid-in capital	Distributions in excess of accumulated earnings	Accumulated other comprehensive loss, net	Noncontrolling Interest	Total
	Shares	Amount	Shares	Amount					
Balances at December 31, 2015	2,950	\$73,750	65,379	\$ 6	\$7,003,317	\$(797,329)	\$(42,011)	\$ 99,290	\$6,337,023
Net income	—	—	—	—	—	81,836	—	5,071	86,907
Change in fair value of derivatives and amortization of swap settlements	—	—	—	—	—	—	(2,445)	(83)	(2,528)
Change in fair value of marketable securities	—	—	—	—	—	—	307	10	317
Issuance of common stock under:									
Stock option and restricted stock plans, net	—	—	41	—	5,232	—	—	—	5,232
Sale of common stock, net	—	—	—	—	(134)	—	—	—	(134)
Equity based compensation costs	—	—	—	—	895	—	—	595	1,490
Reclassification of Series H preferred stock	(2,950)	(73,750)	—	—	2,541	(2,541)	—	—	(73,750)
Changes in the redemption value of redeemable noncontrolling interest	—	—	—	—	(841)	—	—	90	(751)
Distributions to noncontrolling interest	—	—	—	—	—	—	—	(5,465)	(5,465)
Redemptions of noncontrolling interest	—	—	7	—	(829)	—	—	(260)	(1,089)
Common and preferred stock dividends	—	—	—	—	—	(106,012)	—	—	(106,012)
Balances at March 31, 2016	—	\$—	65,427	\$ 6	\$7,010,181	\$(824,046)	\$(44,149)	\$ 99,248	\$6,241,240

See accompanying notes to the unaudited condensed consolidated financial statements.

ESSEX PROPERTY TRUST, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows

(Unaudited)

(In thousands)

	Three Months Ended March 31, 2016	2015
Cash flows from operating activities:		
Net income	\$ 86,907	\$ 64,753
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	109,707	106,907
Amortization of discount on marketable securities and other investments	(3,756)	(2,856)
Amortization of (premium) discount and debt financing costs, net	(3,795)	(6,530)
Gain on sale of marketable securities	(740)	—
Company's share of gain on the sales of co-investments	(7,435)	—
Income from early redemption of preferred equity investments	—	(469)
Earnings from co-investments	(7,633)	(3,842)
Operating distributions from co-investments	9,753	6,055
Gain on the sale of real estate and land	(20,258)	(7,112)
Equity-based compensation	1,490	1,370
Gain on remeasurement of co-investments	—	(21,362)
Changes in operating assets and liabilities:		
Prepaid expenses, receivables and other assets	846	3,548
Accounts payable and accrued liabilities	35,200	21,741
Other liabilities	324	346
Net cash provided by operating activities	200,610	162,549

Edgar Filing: ESSEX PROPERTY TRUST INC - Form 10-Q

Cash flows from investing activities:			
Additions to real estate:			
Acquisitions of real estate and acquisition related capital expenditures	(110,309)	)	(199,190)
Redevelopment	(24,151)	)	(19,140)
Development acquisitions of and additions to real estate under development	(22,656)	)	(90,925)
Capital expenditures on rental properties	(5,688)	)	(16,196)
Acquisition of membership interest in co-investments	—	)	(41,513)
Proceeds from insurance for property losses	435	)	4,589
Proceeds from dispositions of real estate	48,008	)	74,485
Contributions to co-investments	(50,591)	)	(48,650)
Changes in restricted cash and refundable deposits	59,346	)	45,145
Purchases of marketable securities	(1,344)	)	(7,250)
Sales and maturities of marketable securities	5,045	)	717
Non-operating distributions from co-investments	21,146	)	11,072
Net cash used in investing activities	(80,759)	)	(286,856)
Cash flows from financing activities:			
Borrowings under debt agreements	305,895	)	756,562
Repayment of debt	(309,903)	)	(536,830)
Additions to deferred charges	(1,037)	)	(4,456)
Net proceeds from issuance of common stock	(134)	)	174,592
Net proceeds from stock options exercised	5,232	)	15,613
Distributions to noncontrolling interest	(4,858)	)	(3,574)

Edgar Filing: ESSEX PROPERTY TRUST INC - Form 10-Q

Redemption of noncontrolling interest	(1,089	)	(2,154)
Common and preferred stock dividends paid	(95,476	)	(83,663)
Net cash (used in) provided by financing activities	(101,370	)	316,090	
Cash acquired in consolidation of co-investment	—		1,807	
Net increase in cash and cash equivalents	18,481		193,590	
Cash and cash equivalents at beginning of period	29,683		25,610	

5

	Three Months Ended March 31,	
	2016	2015
Cash and cash equivalents at end of period	\$48,164	\$219,200
Supplemental disclosure of cash flow information:		
Cash paid for interest, net of \$3.1 million and \$4.3 million capitalized in 2016 and 2015, respectively	\$48,109	\$50,343
Supplemental disclosure of noncash investing and financing activities:		
Transfers between real estate under development to rental properties, net	\$107,643	\$162,345
Transfer from real estate under development to co-investments	\$2,338	\$1,562
Reclassifications to redeemable noncontrolling interest from additional paid in capital and noncontrolling interest	\$751	\$1,660
Debt assumed in connection with acquisition	\$48,832	\$114,435

See accompanying notes to the unaudited condensed consolidated financial statements.

ESSEX PORTFOLIO, L.P. AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

(Unaudited)

(In thousands, except unit amounts)

	March 31, 2016	December 31, 2015
ASSETS		
Real estate:		
Rental properties:		
Land and land improvements	\$2,573,923	\$2,522,842
Buildings and improvements	10,052,754	9,808,627
	12,626,677	12,331,469
Less accumulated depreciation	(2,051,802)	(1,949,892)
	10,574,875	10,381,577
Real estate under development	145,711	242,326
Co-investments	1,069,684	1,036,047
Real estate held for sale, net	—	26,879
	11,790,270	11,686,829
Cash and cash equivalents-unrestricted	48,164	29,683
Cash and cash equivalents-restricted	32,319	93,372
Marketable securities	138,597	137,485