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HCP, INC.

Form 10-Q

May 02, 2019

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0000765880 hcp:BrookdaleMember hcp:SalesRevenuesMember 2019-01-01 2019-03-31 0000765880  
hcp:BrookdaleMember hcp:ManagementAndAccountingServicesMember  
hcp:SeniorHousingOperatingPortfolioMember 2019-03-31 0000765880 hcp:BrookdaleMember  
hcp:ManagementAndAccountingServicesMember hcp:SeniorHousingOperatingPortfolioMember 2019-01-01  
2019-03-31 0000765880 hcp:BrookdaleMember srt:MaximumMember  
hcp:ManagementAndAccountingServicesMember hcp:SeniorHousingOperatingPortfolioMember 2019-01-01  
2019-03-31 0000765880 hcp:BrookdaleMember srt:MaximumMember 2019-01-01 2019-03-31 0000765880  
hcp:BrookdaleMember us-gaap:AssetsTotalMember hcp:SeniorHousingOperatingPortfolioMember 2019-01-01  
2019-03-31 0000765880 hcp:BrookdaleMember srt:MinimumMember 2019-01-01 2019-03-31 0000765880  
hcp:BrookdaleMember srt:MinimumMember hcp:ManagementAndAccountingServicesMember  
hcp:SeniorHousingOperatingPortfolioMember 2019-01-01 2019-03-31 0000765880  
us-gaap:FairValueInputsLevel2Member us-gaap:EstimateOfFairValueFairValueDisclosureMember 2019-03-31  
0000765880 us-gaap:CarryingReportedAmountFairValueDisclosureMember 2019-03-31 0000765880  
us-gaap:FairValueInputsLevel2Member us-gaap:EstimateOfFairValueFairValueDisclosureMember 2018-12-31  
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2019-03-31 0000765880 us-gaap:InterestRateSwapMember us-gaap:CashFlowHedgingMember 2019-03-31

0000765880 srt:MaximumMember us-gaap:InterestRateSwapMember 2019-01-01 2019-03-31 0000765880  
hcp:CreditFacilityAnd2015TermLoanMember us-gaap:NetInvestmentHedgingMember 2019-03-31 xbrli:pure  
hcp:property hcp:facility xbrli:shares iso4217:USD xbrli:shares hcp:joint\_venture hcp:renewal\_option iso4217:USD  
iso4217:GBP hcp:derivative hcp:renewal hcp:tenant hcp:loan

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# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

## FORM 10-Q

(Mark One)

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

**For the quarterly period ended March 31, 2019**

**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 001-08895**

### **HCP, Inc.**

(Exact name of registrant as specified in its charter)

**Maryland 33-0091377**

(State or other jurisdiction of (I.R.S. Employer incorporation or organization) Identification No.)

**1920 Main Street, Suite 1200**

**Irvine, CA 92614**

(Address of principal executive offices)

**(949) 407-0700**

(Registrant's telephone number, including area code)

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

Securities registered pursuant to Section 12(b) of the Act:

|                                |                   |   |
|--------------------------------|-------------------|---|
| Title of each class            | Trading symbol(s) | Name of each exchange on which registered |
| Common stock, \$1.00 par value | HCP               | New York Stock Exchange                   |

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. YES NO

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or such shorter period that the registrant was required to submit such files). 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 definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer Accelerated Filer

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Non-accelerated Filer    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.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act) YES    NO

At April 30, 2019, there were 477,983,011 shares of the registrant's \$1.00 par value common stock outstanding.

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**HCP, INC.**

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(In thousands, except share and per share data)

(Unaudited)

|  | <b>March 31,<br/>2019</b> | <b>December 31,<br/>2018</b> |
|--|---------------------------|------------------------------|
| <b>ASSETS</b>  |                           |                              |
| Real estate:   |                           |                              |
| Buildings and improvements   | \$ 11,220,557             | \$ 10,877,248                |
| Development costs and construction in progress   | 605,165                   | 537,643                      |
| Land   | 1,717,259                 | 1,637,506                    |
| Accumulated depreciation and amortization  | (2,915,798 )              | (2,842,947 )                 |
| Net real estate  | 10,627,183                | 10,209,450                   |
| Net investment in direct financing leases  | 363,395                   | 713,818                      |
| Loans receivable, net  | 86,139                    | 62,998                       |
| Investments in and advances to unconsolidated joint ventures   | 531,966                   | 540,088                      |
| Accounts receivable, net of allowance of \$5,175 and \$5,127, respectively   | 48,555                    | 48,171                       |
| Cash and cash equivalents  | 120,117                   | 110,790                      |
| Restricted cash  | 26,535                    | 29,056                       |
| Intangible assets, net   | 275,565                   | 305,079                      |
| Assets held for sale, net  | 10,842                    | 108,086                      |
| Right-of-use asset, net  | 165,748                   | —                            |
| Other assets, net  | 643,456                   | 591,017                      |
| Total assets   | \$ 12,899,501             | \$ 12,718,553                |
| <b>LIABILITIES AND EQUITY</b>  |                           |                              |
| Bank line of credit  | \$ 276,500                | \$ 80,103                    |
| Senior unsecured notes   | 5,260,622                 | 5,258,550                    |
| Mortgage debt  | 137,525                   | 138,470                      |
| Other debt   | 89,223                    | 90,785                       |
| Intangible liabilities, net  | 49,488                    | 54,663                       |
| Liabilities of assets held for sale, net   | 132                       | 1,125                        |
| Lease liability  | 152,837                   | —                            |
| Accounts payable and accrued liabilities   | 352,642                   | 391,583                      |
| Deferred revenue   | 181,467                   | 190,683                      |
| Total liabilities  | 6,500,436                 | 6,205,962                    |
| Commitments and contingencies  |                           |                              |
| Common stock, \$1.00 par value: 750,000,000 shares authorized; 477,928,816 and 477,496,499 shares issued and outstanding, respectively | 477,929                   | 477,496                      |
| Additional paid-in capital   | 8,405,258                 | 8,398,847                    |
| Cumulative dividends in excess of earnings   | (3,042,422 )              | (2,927,196 )                 |
| Accumulated other comprehensive income (loss)  | (3,883 )                  | (4,708 )                     |
| Total stockholders' equity   | 5,836,882                 | 5,944,439                    |
| Joint venture partners   | 389,369                   | 391,401                      |
| Non-managing member unitholders  | 172,814                   | 176,751                      |
| Total noncontrolling interests   | 562,183                   | 568,152                      |
| Total equity   | 6,399,065                 | 6,512,591                    |
| Total liabilities and equity   | \$ 12,899,501             | \$ 12,718,553                |

See accompanying Notes to the Unaudited Consolidated Financial Statements.



Table of Contents**HCP, Inc.****CONSOLIDATED STATEMENTS OF OPERATIONS**

(In thousands, except per share data)

(Unaudited)

|  | <b>Three Months Ended<br/>March 31,</b> |                  |
|--|---|------------------|
|  | <b>2019</b>                             | <b>2018</b>      |
| <b>Revenues:</b>   |   |                  |
| Rental and related revenues  | \$ 294,222                              | \$ 316,752       |
| Resident fees and services   | 126,695                                 | 142,814          |
| Income from direct financing leases  | 13,524                                  | 13,266           |
| Interest income  | 1,713                                   | 6,365            |
| Total revenues   | 436,154                                 | 479,197          |
| <b>Costs and expenses:</b>   |   |                  |
| Interest expense   | 49,327                                  | 75,102           |
| Depreciation and amortization  | 131,951                                 | 143,250          |
| Operating  | 168,927                                 | 172,552          |
| General and administrative   | 21,355                                  | 29,175           |
| Transaction costs  | 4,518                                   | 2,195            |
| Impairments (recoveries), net  | 8,858                                   | —                |
| Total costs and expenses   | 384,936                                 | 422,274          |
| <b>Other income (expense):</b>   |   |                  |
| Gain (loss) on sales of real estate, net   | 8,044                                   | 20,815           |
| Other income (expense), net  | 3,133                                   | (40,407 )        |
| Total other income (expense), net  | 11,177                                  | (19,592 )        |
| <b>Income (loss) before income taxes and equity income (loss) from unconsolidated joint ventures</b> | <b>62,395</b>                           | <b>37,331</b>    |
| Income tax benefit (expense)   | 3,458                                   | 5,336            |
| Equity income (loss) from unconsolidated joint ventures  | (863 )                                  | 570              |
| <b>Net income (loss)</b>   | <b>64,990</b>                           | <b>43,237</b>    |
| Noncontrolling interests' share in earnings  | (3,520 )                                | (3,005 )         |
| <b>Net income (loss) attributable to HCP, Inc.</b>   | <b>61,470</b>                           | <b>40,232</b>    |
| Participating securities' share in earnings  | (441 )                                  | (391 )           |
| <b>Net income (loss) applicable to common shares</b>   | <b>\$ 61,029</b>                        | <b>\$ 39,841</b> |
| <b>Earnings per common share:</b>  |   |                  |
| Basic  | \$ 0.13                                 | \$ 0.08          |
| Diluted  | \$ 0.13                                 | \$ 0.08          |
| <b>Weighted average shares outstanding:</b>  |   |                  |
| Basic  | 477,766                                 | 469,557          |
| Diluted  | 479,131                                 | 469,695          |

See accompanying Notes to the Unaudited Consolidated Financial Statements.

Table of Contents**HCP, Inc.****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**

(In thousands)

(Unaudited)

|  | <b>Three Months<br/>Ended March 31,</b> |             |
|--|---|-------------|
|  | <b>2019</b>                             | <b>2018</b> |
| Net income (loss)  | \$ 64,990                               | \$ 43,237   |
| Other comprehensive income (loss):   |   |             |
| Net unrealized gains (losses) on derivatives                               | 94                                      | (5,164 )    |
| Change in Supplemental Executive Retirement Plan obligation and other      | 69                                      | 104         |
| Foreign currency translation adjustment                                    | 662                                     | 7,652       |
| Reclassification adjustment realized in net income (loss)                  | —                                       | 125         |
| Total other comprehensive income (loss)                                    | 825                                     | 2,717       |
| Total comprehensive income (loss)  | 65,815                                  | 45,954      |
| Total comprehensive income (loss) attributable to noncontrolling interests | (3,520 )                                | (3,005 )    |
| Total comprehensive income (loss) attributable to HCP, Inc.                | \$ 62,295                               | \$ 42,949   |

See accompanying Notes to the Unaudited Consolidated Financial Statements.

Table of Contents**HCP, Inc.****CONSOLIDATED STATEMENTS OF EQUITY**

(In thousands, except per share data)

(Unaudited)

|  | Common Stock |           | Additional  | Cumulative    | Accumulated   | Total         | Total          | Total       |
|--|--------------|-----------|-------------|---------------|---------------|---------------|----------------|-------------|
|  | Shares       | Amount    | Paid-In     | Dividends     | Other         | Stockholders' | Noncontrolling | Equity      |
|  |              |           | Capital     | In Excess     | Comprehensive | Equity        | Interests      |             |
|  |              |           |             | Of Earnings   | Income (Loss) |               |                |             |
| <b>December 31, 2018</b>                             | 477,496      | \$477,496 | \$8,398,847 | \$(2,927,196) | \$ (4,708 )   | \$5,944,439   | \$568,152      | \$6,512,591 |
| Impact of adoption of ASU No. 2016-02 <sup>(1)</sup> | —            | —         | —           | 590           | —             | 590           | —              | 590         |
| <b>January 1, 2019</b>                               | 477,496      | 477,496   | 8,398,847   | (2,926,606)   | (4,708)       | 5,945,029     | 568,152        | 6,513,181   |
| Net income (loss)                                    | —            | —         | —           | 61,470        | —             | 61,470        | 3,520          | 64,990      |
| Other comprehensive income (loss)                    | —            | —         | —           | —             | 825           | 825           | —              | 825         |
| Issuance of common stock, net                        | 342          | 342       | 1,190       | —             | —             | 1,532         | —              | 1,532       |
| Conversion of DownREIT units to common stock         | 184          | 184       | 3,890       | —             | —             | 4,074         | (4,074)        | —           |
| Repurchase of common stock                           | (95)         | (95)      | (2,824)     | —             | —             | (2,919)       | —              | (2,919)     |
| Exercise of stock options                            | 2            | 2         | 44          | —             | —             | 46            | —              | 46          |
| Amortization of deferred compensation                | —            | —         | 4,111       | —             | —             | 4,111         | —              | 4,111       |
| Common dividends (\$0.37 per share)                  | —            | —         | —           | (177,286)     | —             | (177,286)     | —              | (177,286)   |
| Distributions to noncontrolling interests            | —            | —         | —           | —             | —             | —             | (5,415)        | (5,415)     |
| <b>March 31, 2019</b>                                | 477,929      | \$477,929 | \$8,405,258 | \$(3,042,422) | \$ (3,883 )   | \$5,836,882   | \$562,183      | \$6,399,065 |
|  | Common Stock |           | Additional  | Cumulative    | Accumulated   | Total         | Total          | Total       |
|  | Shares       | Amount    | Paid-In     | Dividends     | Other         | Stockholders' | Noncontrolling | Equity      |
|  |              |           | Capital     | In Excess     | Comprehensive | Equity        | Interests      |             |
|  |              |           |             | Of Earnings   | Income (Loss) |               |                |             |
| <b>December 31, 2017</b>                             | 469,436      | \$469,436 | \$8,226,113 | \$(3,370,520) | \$ (24,024 )  | \$5,301,005   | \$293,933      | \$5,594,938 |
| Impact of adoption of ASU No. 2017-05 <sup>(2)</sup> | —            | —         | —           | 79,144        | —             | 79,144        | —              | 79,144      |
| <b>January 1, 2018</b>                               | 469,436      | 469,436   | 8,226,113   | \$(3,291,376) | (24,024)      | 5,380,149     | 293,933        | 5,674,082   |
| Net income (loss)                                    | —            | —         | —           | 40,232        | —             | 40,232        | 3,005          | 43,237      |
| Other comprehensive income (loss)                    | —            | —         | —           | —             | 2,717         | 2,717         | —              | 2,717       |
| Issuance of common stock, net                        | 382          | 382       | 2,392       | —             | —             | 2,774         | —              | 2,774       |
| Repurchase of common stock                           | (93)         | (93)      | (2,051)     | —             | —             | (2,144)       | —              | (2,144)     |
| Amortization of deferred compensation                | —            | —         | 5,919       | —             | —             | 5,919         | —              | 5,919       |
| Common dividends (\$0.37 per share)                  | —            | —         | —           | (174,149)     | —             | (174,149)     | —              | (174,149)   |
| Distributions to noncontrolling interests            | —            | —         | —           | —             | —             | —             | (5,077)        | (5,077)     |
| Issuances of noncontrolling interests                | —            | —         | —           | —             | —             | —             | 995            | 995         |
| Purchase of noncontrolling interests                 | —            | —         | (49,207)    | —             | —             | (49,207)      | (18,224)       | (67,431)    |
| <b>March 31, 2018</b>                                | 469,725      | \$469,725 | \$8,183,166 | \$(3,425,293) | \$ (21,307 )  | \$5,206,291   | \$274,632      | \$5,480,923 |

(1) On January 1, 2019, the Company adopted a series of Accounting Standards Updates ("ASUs") related to accounting for leases, and recognized the cumulative-effect of adoption to beginning retained earnings. Refer to Note 2 for a detailed impact of adoption.

(2) On January 1, 2018, the Company adopted ASU No. 2017-05, *Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets* ("ASU 2017-05"), and recognized the cumulative-effect of adoption to beginning retained earnings. Refer to Note 2 for a detailed impact of adoption.

See accompanying Notes to the Unaudited Consolidated Financial Statements.

Table of Contents**HCP, Inc.****CONSOLIDATED STATEMENTS OF CASH FLOWS**

(In thousands)

(Unaudited)

|  | <b>Three Months Ended</b> |             |
|--|---------------------------|-------------|
|  | <b>March 31,</b>          |             |
|  | <b>2019</b>               | <b>2018</b> |
| <b>Cash flows from operating activities:</b>   |                           |             |
| Net income (loss)  | \$ 64,990                 | \$ 43,237   |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: |                           |             |
| Depreciation and amortization of real estate, in-place lease and other intangibles       | 131,951                   | 143,250     |
| Amortization of deferred compensation  | 4,111                     | 5,919       |
| Amortization of deferred financing costs   | 2,699                     | 3,336       |
| Straight-line rents  | (5,091 )                  | (10,686 )   |
| Equity loss (income) from unconsolidated joint ventures                                  | 863                       | (570 )      |
| Distributions of earnings from unconsolidated joint ventures                             | 5,232                     | 5,336       |
| Deferred income tax expense (benefit)  | (3,800 )                  | (2,394 )    |
| Impairments (recoveries), net  | 8,858                     | (3,298 )    |
| Loss (gain) on sales of real estate, net   | (8,044 )                  | (20,815 )   |
| Loss (gain) on consolidation, net  | —                         | 41,017      |
| Other non-cash items   | 560                       | (2,401 )    |
| Decrease (increase) in accounts receivable and other assets, net                         | (11,114 )                 | (18,082 )   |
| Increase (decrease) in accounts payable, accrued liabilities and deferred revenue        | (32,633 )                 | 12,315      |
| Net cash provided by (used in) operating activities                                      | 158,582                   | 196,164     |
| <b>Cash flows from investing activities:</b>   |                           |             |
| Acquisitions of real estate  | (106,298 )                | (22,121 )   |
| Development and redevelopment of real estate   | (136,654 )                | (113,648 )  |
| Leasing costs, tenant improvements, and recurring capital expenditures                   | (19,220 )                 | (19,246 )   |
| Proceeds from sales of real estate, net  | 122,678                   | 30,392      |
| Contributions to unconsolidated joint ventures   | (3,870 )                  | (3,688 )    |
| Distributions in excess of earnings from unconsolidated joint ventures                   | 5,497                     | 7,257       |
| Proceeds from sales/principal repayments on debt investments and direct financing leases | 481                       | 132,429     |
| Investments in loans receivable, direct financing leases and other                       | (22,891 )                 | (647 )      |
| Net cash provided by (used in) investing activities                                      | (160,277 )                | 10,728      |
| <b>Cash flows from financing activities:</b>   |                           |             |
| Borrowings under bank line of credit   | 320,000                   | 240,000     |
| Repayments under bank line of credit   | (125,000 )                | (170,000 )  |
| Repayments and repurchase of debt, excluding bank line of credit                         | (2,437 )                  | (1,172 )    |
| Issuance of common stock and exercise of options   | 1,578                     | 2,774       |
| Repurchase of common stock   | (2,919 )                  | (2,144 )    |
| Dividends paid on common stock   | (177,286 )                | (174,149 )  |
| Issuance of noncontrolling interests   | —                         | 995         |
| Distributions to and purchase of noncontrolling interests                                | (5,415 )                  | (67,542 )   |
| Net cash provided by (used in) financing activities                                      | 8,521                     | (171,238 )  |
| Effect of foreign exchanges on cash, cash equivalents and restricted cash                | (20 )                     | 111         |
| Net increase (decrease) in cash, cash equivalents and restricted cash                    | 6,806                     | 35,765      |
| Cash, cash equivalents and restricted cash, beginning of period                          | 139,846                   | 82,203      |
| Cash, cash equivalents and restricted cash, end of period                                | \$ 146,652                | \$ 117,968  |

See accompanying Notes to the Unaudited Consolidated Financial Statements.



Table of Contents**HCP, Inc.****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited)

**NOTE 1. Business**

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*Overview*

HCP, Inc., a Standard & Poor's 500 company, is a Maryland corporation that is organized to qualify as a real estate investment trust ("REIT") which, together with its consolidated entities (collectively, "HCP" or the "Company"), invests primarily in real estate serving the healthcare industry in the United States ("U.S."). The Company acquires, develops, leases, owns and manages healthcare real estate. The Company's diverse portfolio is comprised of investments in the following reportable healthcare segments: (i) senior housing triple-net; (ii) senior housing operating portfolio ("SHOP"); (iii) life science and (iv) medical office.

**NOTE 2. Summary of Significant Accounting Policies**

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**Basis of Presentation**

The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information. Management is required to make estimates and assumptions in the preparation of financial statements in conformity with GAAP. These estimates and assumptions affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from management's estimates.

The consolidated financial statements include the accounts of HCP, Inc., its wholly-owned subsidiaries, joint ventures ("JVs") and variable interest entities ("VIEs") that it controls through voting rights or other means. Intercompany transactions and balances have been eliminated upon consolidation. All adjustments (consisting of normal recurring adjustments) necessary to present fairly the Company's financial position, results of operations and cash flows have been included. Operating results for the three months ended March 31, 2019 are not necessarily indicative of the results that may be expected for the year ending December 31, 2019. The accompanying unaudited interim financial information should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2018 included in the Company's Annual Report on Form 10-K filed with the U.S. Securities and Exchange Commission ("SEC").

**Recent Accounting Pronouncements***Adopted*

*Revenue Recognition.* Between May 2014 and February 2017, the Financial Accounting Standards Board ("FASB") issued four Accounting Standards Updates ("ASUs") changing the requirements for recognizing and reporting revenue (together, herein referred to as the "Revenue ASUs"): (i) ASU No. 2014-09, *Revenue from Contracts with Customers* ("ASU 2014-09"), (ii) ASU No. 2016-08, *Principal versus Agent Considerations (Reporting Revenue Gross versus Net)* ("ASU 2016-08"), (iii) ASU No. 2016-12, *Narrow-Scope Improvements and Practical Expedients* ("ASU 2016-12"), and (iv) ASU No. 2017-05, *Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets* ("ASU 2017-05"). ASU 2014-09 provides guidance for revenue recognition to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2016-08 is intended to improve the operability and understandability of the implementation guidance on principal versus agent considerations. ASU 2016-12 provides practical expedients and improvements on the previously narrow scope of ASU 2014-09. ASU 2017-05 clarifies the scope of the FASB's guidance on nonfinancial asset derecognition and aligns the accounting for partial sales of nonfinancial assets and in-substance nonfinancial assets with the guidance in ASU 2014-09. The Company adopted the Revenue ASUs effective January 1, 2018 and utilized a modified retrospective adoption approach, resulting in a cumulative-effect adjustment to equity of \$79 million as of January 1, 2018. Under the Revenue ASUs, the Company also elected to utilize a practical expedient which allows the Company to only reassess contracts that were not



completed as of the adoption date, rather than all historical contracts.

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As the timing and recognition of the majority of the Company's revenue is the same whether accounted for under the Revenue ASUs or lease accounting guidance (see discussion below), the impact of the Revenue ASUs, upon and subsequent to adoption, is generally limited to the following:

Prior to the adoption of the Revenue ASUs, the Company recognized a gain on sale of real estate using the full accrual method when collectibility of the sales price was reasonably assured, the Company was not obligated to perform additional activities that may be considered significant, the initial investment from the buyer was sufficient and other profit recognition criteria had been satisfied. The Company deferred all or a portion of a gain on sale of real estate if the requirements for gain recognition were not met at the time of sale. Subsequent to adopting the Revenue ASUs on January 1, 2018, the Company began recognizing a gain on sale of real estate upon transferring control of the asset to the purchaser, which is generally satisfied at the time of sale. In conjunction with its adoption of the Revenue ASUs, the Company reassessed its historical partial sale of real estate transactions to determine which transactions, if any, were not completed contracts (i.e., the transaction did not qualify for sale treatment under previous guidance). The Company concluded that it had one such material transaction, its partial sale of RIDEA II in the first quarter of 2017 (which was not a completed sale under historical guidance as of the Company's adoption date due to a minor obligation related to the interest sold). In accordance with the Revenue ASUs, the Company recorded its retained 40% equity investment at fair value as of the sale date. As a result, the Company recorded an adjustment to equity as of January 1, 2018 (under the modified retrospective transition approach) representing a step-up in the fair value of its equity investment in RIDEA II of \$107 million (to a carrying value of \$121 million as of January 1, 2018) and a \$30 million impairment charge to decrease the carrying value to the sales price of the investment (see Note 3). The Company completed the sale of its equity investment in June 2018 and no longer holds an economic interest in RIDEA II.

The Company generally expects that the new guidance will result in certain transactions qualifying as sales of real estate at an earlier date than under historical accounting guidance.

The Company, along with its joint venture partners and independent SHOP operators, provide certain ancillary services to SHOP residents that are not contemplated in the lease with each resident (i.e., guest meals, concierge services, pharmacy services, etc.). These services are provided and paid for in addition to the standard services included in each resident lease (i.e., room and board, standard meals, etc.). The Company bills residents for ancillary services one month in arrears and recognizes revenue as the services are provided, as the Company has no continuing performance obligation related to those services. Included within resident fees and services for both the three months ended March 31, 2019 and 2018 is \$10 million of ancillary service revenue.

*Leases.* In February 2016, the FASB issued ASU No. 2016-02, *Leases* ("ASU 2016-02"). ASU 2016-02 (codified under Accounting Standards Codification ("ASC") 842, *Leases*) amends the previous accounting for leases to: (i) require lessees to put most leases on their balance sheets (not required for short-term leases with lease terms of 12 months or less), but continue recognizing expenses on their income statements in a manner similar to requirements under prior accounting guidance, (ii) eliminate real estate specific lease provisions, and (iii) modify the classification criteria and accounting for sales-type leases for lessors. Additionally, ASU 2016-02 provides a practical expedient, which the Company elected, that allows an entity to not reassess the following upon adoption (must be elected as a group): (i) whether an expired or existing contract contains a lease arrangement, (ii) lease classification related to expired or existing lease arrangements, or (iii) whether costs incurred on expired or existing leases qualify as initial direct costs. As a result of adopting ASU 2016-02 on January 1, 2019 using the modified retrospective transition approach, the Company recognized a cumulative-effect adjustment to equity of \$1 million as of January 1, 2019. Under ASU 2016-02, the Company began capitalizing fewer costs related to the drafting and negotiation of its lease agreements. Additionally, the Company began recognizing all of its significant operating leases for which it is the lessee, including corporate office leases, equipment leases, and ground leases, on its consolidated balance sheets as a lease liability and corresponding right-of-use asset. As such, the Company recognized a lease liability of \$153 million and right-of-use asset of \$166 million on January 1, 2019. The aggregate lease liability is calculated as the present value of minimum lease payments, discounted using a rate that approximates the Company's secured incremental borrowing rate, adjusted for the noncancelable term of each lease. The right-of-use asset is calculated as the aggregate lease liability, adjusted for the existing accrued straight-line rent liability balance of \$20 million and net unamortized above/below market

ground lease intangible assets of \$33 million.

Under ASU 2016-02, a practical expedient was offered to lessees to make a policy election, which the Company elected, to not separate lease and nonlease components, but rather account for the combined components as a single lease component under ASC 842. In July 2018, the FASB issued ASU No. 2018-11, *Leases - Targeted Improvements* (“ASU 2018-11”), which provides lessors with a similar option to elect a practical expedient allowing them to not separate lease and nonlease components in a contract for the purpose of revenue recognition and disclosure. This practical expedient is limited to circumstances in which: (i) the timing and pattern of transfer are the same for the nonlease component and the related lease component and (ii) the lease component, if accounted for separately, would be classified as an operating lease. This practical expedient causes an entity to assess whether a contract is predominantly lease or service based and recognize the entire contract under the relevant accounting guidance (i.e.,

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predominantly lease-based would be accounted for under ASU 2016-02 and predominantly service-based would be accounted for under the Revenue ASUs). The Company elected this practical expedient as well and, as a result, beginning January 1, 2019, the Company recognizes revenue from its senior housing triple-net, medical office, and life science segments under ASC 842 and revenue from its SHOP segment under the Revenue ASUs (codified under ASC 606, *Revenue from Contracts with Customers*).

In conjunction with reaching the conclusions above, the Company concluded it was appropriate (under ASC 205, *Presentation of Financial Statements*) to reclassify amounts previously classified as revenue from tenant recoveries (within the senior housing triple-net, life science, and medical office segments) and present them combined with rental and related revenues within the consolidated statements of operations. The Company implemented this change during the fourth quarter of 2018. Included within rental and related revenues for the three months ended March 31, 2018 is \$37 million of tenant recoveries.

In December 2018, the FASB issued ASU No. 2018-20, *Narrow Scope Improvements for Lessors* (“ASU 2018-20”), which requires that a lessor: (i) exclude certain lessor costs paid directly by a lessee to third parties on behalf of the lessor from a lessor's measurement of variable lease revenue and associated expense (i.e., no gross up of revenue and expense for these costs), and (ii) include lessor costs that are paid by the lessor and reimbursed by the lessee in the measurement of variable lease revenue and the associated expense (i.e., gross up revenue and expense for these costs). This is consistent with the Company's historical presentation and did not require a material change on January 1, 2019. *Other.* Effective January 1, 2019, the Company adopted the following ASU, which did not have a material impact to its consolidated financial position, results of operations, cash flows or disclosures upon adoption:

ASU No. 2017-12, *Targeted Improvements to Accounting for Hedging Activities* (“ASU 2017-12”). The amendments in ASU 2017-12 expand and refine hedge accounting for both nonfinancial and financial risk components and align the recognition and presentation of the effects of the hedging instrument and the hedged item in the financial statements. For cash flow and net investment hedges existing at the date of adoption, the Company adopted the amendments in ASU 2017-12 using the modified retrospective approach. For amendments impacting presentation and disclosure, the Company adopted ASU 2017-12 using a prospective approach.

*Not Yet Adopted*

*Credit Losses.* In June 2016, the FASB issued ASU No. 2016-13, *Measurement of Credit Losses on Financial Instruments* (“ASU 2016-13”). ASU 2016-13 is intended to improve financial reporting by requiring timelier recognition of credit losses on loans and other financial instruments held by financial institutions and other organizations. The amendments in ASU 2016-13 eliminate the “probable” initial threshold for recognition of credit losses in current accounting guidance and, instead, reflect an entity's current estimate of all expected credit losses over the life of the financial instrument. Previously, when credit losses were measured under current accounting guidance, an entity generally only considered past events and current conditions in measuring the incurred loss. The amendments in ASU 2016-13 broaden the information that an entity must consider in developing its expected credit loss estimate for assets measured either collectively or individually. The use of forecasted information incorporates more timely information in the estimate of expected credit loss. ASU 2016-13 is effective for fiscal years, and interim periods within, beginning after December 15, 2019. Early adoption is permitted for fiscal years, and interim periods within, beginning after December 15, 2018. A reporting entity is required to apply the amendments in ASU 2016-13 using a modified retrospective approach by recording a cumulative-effect adjustment to equity as of the beginning of the fiscal year of adoption. A prospective transition approach is required for debt securities for which an other-than-temporary impairment had been recognized before the effective date. Upon adoption of ASU 2016-13, the Company is required to reassess its financing receivables, including direct financing leases (“DFLs”) and loans receivable, and expects that application of ASU 2016-13 may result in the Company recognizing credit losses at an earlier date than would otherwise be recognized under current accounting guidance. The Company is evaluating the impact of the adoption of ASU 2016-13 on January 1, 2020 to its consolidated financial position and results of operations.

**Segment Reporting**

The Company's reportable segments, based on how it evaluates its business and allocates resources, are as follows: (i) senior housing triple-net, (ii) SHOP, (iii) life science and (iv) medical office. During the first quarter of 2019, as a result of a change in how operating results are reported to the Company's chief operating decision makers for the

purpose of evaluating performance and allocating resources, two facilities were reclassified from other non-reportable segments to the medical office segment. Accordingly, all prior period segment information has been recast to conform to the current period presentation.

Table of Contents**NOTE 3. Real Estate Transactions**

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**2019 Real Estate Investments***Cambridge Acquisition*

During the three months ended March 31, 2019, the Company acquired a life science facility for \$71 million and development rights at an adjacent undeveloped land parcel for consideration of up to \$27 million. The existing facility and land parcel are located in Cambridge, Massachusetts.

*Discovery Portfolio Acquisition*

In April 2019, the Company acquired a portfolio of nine senior housing properties for \$445 million. The properties are located across Florida, Georgia and Texas and will be operated by Discovery Senior Living, LLC (“Discovery”).

*Oakmont Portfolio Acquisition and Transitions*

On May 1, 2019, the Company acquired three newly-built, senior housing communities for \$113 million. The portfolio will be operated by Oakmont Senior Living LLC (“Oakmont”). Additionally, the Company transitioned four senior housing triple-net properties to RIDEA structures with Oakmont continuing as the operator.

**2018 Real Estate Investments***MSREI MOB JV*

In August 2018, the Company and Morgan Stanley Real Estate Investment (“MSREI”) formed a joint venture (the “MSREI JV”) to own a portfolio of medical office buildings (“MOBs”), which the Company owns 51% of and consolidates. To form the joint venture, MSREI contributed cash of \$298 million and HCP contributed nine wholly-owned MOBs (the “Contributed Assets”). The Contributed Assets are primarily located in Texas and Florida and were valued at approximately \$320 million at the time of contribution. The MSREI JV used substantially all of the cash contributed by MSREI to acquire an additional portfolio of 16 MOBs in Greenville, South Carolina (the “Greenville Portfolio”) for \$285 million. Concurrent with acquiring the additional MOBs, the MSREI JV entered into 10-year leases with the anchor tenants in the Greenville Portfolio.

The Contributed Assets are accounted for at historical depreciated cost by the Company, as the assets continue to be consolidated. The Greenville Portfolio was accounted for as an asset acquisition, which required the Company to record the individual components of the acquisition at their relative fair values. As a result, the Company recorded net real estate of \$276 million and net intangible assets of \$20 million during the three months ended September 30, 2018 related to the Greenville Portfolio. Additionally, during the three months ended September 30, 2018, the Company recognized a noncontrolling interest of \$298 million related to the interest owned by MSREI. Refer to Note 14 for a discussion of the Company’s consolidation of the MSREI JV.

*Life Science JV Interest Purchase*

In November 2018, the Company acquired the outstanding equity interests in three life science joint ventures (which owned four buildings) for \$92 million, bringing the Company’s equity ownership to 100% for all three joint ventures. As the Company began consolidating the assets upon acquisition, it derecognized the existing investment in the joint ventures, marked the real estate to fair value (using a relative fair value allocation), and recognized a gain on consolidation of \$50 million within other income (expense), net.

*Sierra Point Towers Acquisition*

In November 2018, the Company entered into definitive agreements to acquire two life science buildings in South San Francisco, California adjacent to the Company’s The Shore at Sierra Point development, for \$245 million. The Company made a \$15 million nonrefundable deposit upon completing due diligence and expects to close the transaction in the second quarter of 2019.

*Other*

During the three months ended March 31, 2018, the Company acquired development rights on a land parcel in the Boston suburb of Lexington, Massachusetts for \$21 million. The Company commenced a life science development on the land in 2018.

**Development Activities**

As part of the development program with HCA Healthcare, during the first quarter of 2019, the Company signed definitive agreements to develop three additional MOBs, two of which will be on-campus, with an aggregate estimated cost of \$70 million. Construction on these projects is expected to commence in the second quarter of 2019.

Table of Contents**Held for Sale**

At March 31, 2019, two MOBs and one SHOP facility were classified as held for sale, with an aggregate carrying value of \$11 million, primarily comprised of real estate assets of \$10 million, net of accumulated depreciation of \$5 million. At December 31, 2018, nine SHOP facilities and one undeveloped life science land parcel were classified as held for sale, with an aggregate carrying value of \$108 million, primarily comprised of real estate assets of \$101 million, net of accumulated depreciation of \$30 million. Liabilities of assets held for sale was primarily comprised of intangible and other liabilities at both March 31, 2019 and December 31, 2018.

**2019 Dispositions of Real Estate**

During the quarter ended March 31, 2019, the Company sold nine SHOP assets for \$68 million, two senior housing triple-net assets for \$26 million, and one undeveloped life science land parcel for \$35 million, resulting in total gain on sales of \$8 million.

**2018 Dispositions of Real Estate***Shoreline Technology Center*

In November 2018, the Company sold its Shoreline Technology Center life science campus located in Mountain View, California for \$1.0 billion and recognized a gain on sale of \$726 million.

*RIDEA II Sale Transaction*

In January 2017, the Company completed the contribution of its ownership interest in RIDEA II to an unconsolidated joint venture owned by HCP and an investor group led by Columbia Pacific Advisors, LLC (“CPA”) (the “HCP/CPA JV”). Also in January 2017, RIDEA II was recapitalized with \$602 million of debt, of which \$360 million was provided by a third-party and \$242 million was provided by HCP. In return for both transaction elements, the Company received combined proceeds of \$480 million from the HCP/CPA JV and \$242 million in loans receivable and retained an approximately 40% ownership interest in RIDEA II. This transaction resulted in the Company deconsolidating the net assets of RIDEA II and recognizing a net gain on sale of \$99 million. Refer to Note 2 for the impact of adopting the Revenue ASUs on January 1, 2018 to the Company’s partial sale of RIDEA II in the first quarter of 2017.

In June 2018, the Company sold its remaining 40% ownership interest in RIDEA II to an investor group led by CPA for \$91 million. Additionally, CPA refinanced the Company’s \$242 million of loans receivable from RIDEA II, resulting in total proceeds of \$332 million. The Company no longer holds an economic interest in RIDEA II.

*U.K. Portfolio*

In June 2018, the Company entered into a joint venture with an institutional investor (the “U.K. JV”) through which the Company sold a 51% interest in substantially all United Kingdom (“U.K.”) assets previously owned by the Company (the “U.K. Portfolio”) based on a total value of £382 million (\$507 million). The Company retained a 49% noncontrolling interest in the joint venture and received gross proceeds of \$402 million, including proceeds from the refinancing of the Company’s previously held intercompany loans. Upon closing the U.K. JV, the Company deconsolidated the U.K. Portfolio, recognized its retained noncontrolling interest investment at fair value (\$105 million) and recognized a gain on sale of \$11 million, net of \$17 million of cumulative foreign currency translation reclassified from other comprehensive income. The U.K. JV provides numerous mechanisms by which the joint venture partner can acquire the Company’s remaining interest in the U.K. JV. The fair value of the Company’s retained noncontrolling interest investment is based on Level 2 measurements within the fair value hierarchy.

Additionally, in August 2018, the Company sold its remaining £11 million U.K. development loan at par.

*Other*

During the quarter ended March 31, 2018, the Company sold two SHOP assets for \$35 million, resulting in total gain on sales of \$21 million.

During the quarter ended June 30, 2018, the Company sold eight SHOP assets for \$268 million and two senior housing triple-net assets for \$35 million, resulting in total gain on sales of \$25 million.

During the quarter ended September 30, 2018, the Company sold four life science assets for \$269 million, 11 SHOP assets for \$76 million and two MOBs for \$21 million, resulting in total gain on sales of \$95 million.

During the quarter ended December 31, 2018, the Company sold two SHOP facilities for \$15 million, two MOBs for \$4 million, and one undeveloped land parcel for \$3 million, resulting in no material gain or loss on sales.



Additionally, during 2018, the Company sold 19 senior housing assets to a third-party buyer for \$377 million, resulting in a gain on sale of \$40 million.

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**Impairments of Real Estate**

2019

During the three months ended March 31, 2019, the Company determined that the carrying value of two MOB's that are candidates for potential future sale was no longer recoverable due to the Company's shortened intended hold period under the held-for-use impairment model. Accordingly, the Company wrote-down the carrying amount of these two assets to their respective fair value, which resulted in an aggregate impairment charge of \$9 million. The fair value of the assets was based on forecasted sales prices which are considered to be Level 2 measurements within the fair value hierarchy.

**Brookdale MTCA Transactions**

In November 2017, the Company and Brookdale Senior Living, Inc. ("Brookdale") entered into a Master Transactions and Cooperation Agreement (the "MTCA") to provide the Company with the ability to significantly reduce its concentration of assets leased to and/or managed by Brookdale (the "Brookdale Transactions"). In connection with the overall transaction pursuant to the MTCA, the Company and Brookdale, and certain of their respective subsidiaries, agreed to the following:

- The Company, which owned 90% of the interests in its RIDEA I and RIDEA III joint ventures with Brookdale at the time the MTCA was executed, agreed to purchase Brookdale's 10% noncontrolling interest in each joint venture for an aggregate purchase price of \$95 million. At the time the MTCA was executed, these joint ventures collectively owned and operated 58 independent living, assisted living, memory care and/or skilled nursing facilities (the "RIDEA Facilities"). The Company completed its acquisitions of the RIDEA III noncontrolling interest for \$32 million in December 2017 and the RIDEA I noncontrolling interest for \$63 million in March 2018;

The Company received the right to sell, or transition to other operators, 32 of the 78 total assets under an Amended and Restated Master Lease and Security Agreement (the "Amended Master Lease") with Brookdale and 36 of the RIDEA Facilities (and terminate related management agreements with an affiliate of Brookdale without penalty), certain of which were sold during 2018 and 2019 and are included in the disposition transactions discussed above; The Company provided an aggregate \$5 million annual reduction in rent on three assets, effective January 1, 2018; and

Brookdale agreed to purchase two of the assets under the Amended Master Lease for \$35 million and four of the RIDEA Facilities for \$240 million, all of which were sold in 2018 and are included in the 2018 disposition transactions discussed above.

Additionally, during 2018, the Company terminated the previous management agreements or leases with Brookdale on 37 assets contemplated under the MTCA and completed the transition of 20 SHOP assets and 17 senior housing triple-net assets to other managers.

Table of Contents**NOTE 4. Leases****Lease Income**

The following table summarizes the Company's lease income:

|  | Three Months Ended<br>March 31, |           |
|--|---------------------------------|-----------|
|  | 2019                            | 2018      |
| Operating lease income                     | \$294,222                       | \$316,752 |
| Interest income on direct financing leases | 13,524                          | 13,266    |

**Direct Financing Leases**

Net investment in DFLs consists of the following (dollars in thousands):

|  | March 31,<br>2019 |
|--|-------------------|
| Present value of minimum lease payments receivable | \$273,629         |
| Present value of estimated residual value          | 114,364           |
| Less deferred selling profits                      | (24,598 )         |
| Net investment in direct financing leases          | \$363,395         |
| Properties subject to direct financing leases      | 15                |

|   | December 31,<br>2018 |
|---|----------------------|
| Minimum lease payments receivable             | \$1,013,976          |
| Estimated residual value                      | 507,484              |
| Less unearned income                          | (807,642 )           |
| Net investment in direct financing leases     | \$713,818            |
| Properties subject to direct financing leases | 29                   |

*Direct Financing Lease Internal Ratings*

The following table summarizes the Company's internal ratings for DFLs at March 31, 2019 (dollars in thousands):

| Segment                       | Carrying Amount | Percentage of DFL Portfolio | Internal Ratings |                 |              |
|-------------------------------|-----------------|-----------------------------|------------------|-----------------|--------------|
|                               |                 |                             | Performing DFLs  | Watch List DFLs | Workout DFLs |
| Senior housing triple-net     | \$278,791       | 77                          | \$278,791        | \$ —            | —            |
| Other non-reportable segments | 84,604          | 23                          | 84,604           | —               | —            |
|                               | \$363,395       | 100                         | \$363,395        | \$ —            | —            |

Beginning September 30, 2013, the Company placed a 14-property senior housing triple-net DFL (the "DFL Watchlist Portfolio") on nonaccrual status and "Watch List" status. The Company determined that the collection of all rental payments was and continues to be no longer reasonably assured; therefore, rental revenue for the DFL Watchlist Portfolio is being recognized on a cash basis. During the three months ended March 31, 2019 and 2018, the Company recognized income from DFLs of \$4 million and \$3 million, respectively. During the three months ended March 31, 2019 and 2018, the Company received cash payments of \$5 million from the DFL Watchlist Portfolio. The carrying value of the DFL Watchlist Portfolio was zero and \$351 million at March 31, 2019 and December 31, 2018, respectively.

*Direct Financing Lease Transition*

During the first quarter of 2019, the Company transitioned the DFL Watchlist Portfolio to a RIDEA structure, requiring the Company to recognize net assets equal to the lower of the net assets' fair value or the carrying value of the net investment in the DFL. As a result, the Company derecognized the \$351 million carrying value of the net investment in DFL related to the 14 properties and recognized a combination of net real estate (\$331 million) and net

intangibles assets (\$20 million) for the same aggregate amount,

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with no gain or loss recognized. As a result of the transaction, the 14 properties were transitioned from the senior housing triple-net segment to the SHOP segment during the first quarter of 2019.

*Direct Financing Lease Receivable Maturities*

The following table summarizes future minimum lease payments contractually due under DFLs at March 31, 2019 (in thousands):

| Year   | Amount     |
|--|------------|
| 2019 (nine months)                                 | \$29,365   |
| 2020   | 32,558     |
| 2021   | 31,989     |
| 2022   | 25,346     |
| 2023   | 24,774     |
| Thereafter   | 416,286    |
| Undiscounted minimum lease payments receivable     | 560,318    |
| Less: imputed interest                             | (286,689 ) |
| Present value of minimum lease payments receivable | \$273,629  |

The following table summarizes future minimum lease payments contractually due under DFLs at December 31, 2018 (in thousands):

| Year       | Amount       |
|------------|--------------|
| 2019       | \$ 114,970   |
| 2020       | 63,308       |
| 2021       | 63,687       |
| 2022       | 58,135       |
| 2023       | 58,570       |
| Thereafter | 655,306      |
|            | \$ 1,013,976 |

*Residual Value Risk*

Quarterly, the Company reviews the estimated unguaranteed residual value of assets under DFLs to determine if there have been any material changes compared to the prior quarter. As needed, the Company and/or the related tenants will invest necessary funds to maintain the residual value of each asset.

**Operating Leases***Future Minimum Rents*

The following table summarizes future minimum lease payments to be received, excluding operating expense reimbursements, from tenants under non-cancelable operating leases as of March 31, 2019 (in thousands):

| Year               | Amount      |
|--------------------|-------------|
| 2019 (nine months) | \$733,816   |
| 2020               | 952,756     |
| 2021               | 884,923     |
| 2022               | 782,066     |
| 2023               | 703,054     |
| Thereafter         | 2,505,848   |
|                    | \$6,562,463 |

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The following table summarizes future minimum lease payments to be received, excluding operating expense reimbursements, from tenants under non-cancelable operating leases as of December 31, 2018 (in thousands):

| Year       | Amount      |
|------------|-------------|
| 2019       | \$971,417   |
| 2020       | 928,102     |
| 2021       | 853,451     |
| 2022       | 751,972     |
| 2023       | 675,537     |
| Thereafter | 2,320,847   |
|            | \$6,501,326 |

**Lease Costs**

The following tables provide information regarding the Company's leases to which it is the lessee, such as corporate offices and ground leases (dollars in thousands):

|                                    | Three Months<br>Ended<br>March 31, |         |
|------------------------------------|------------------------------------|---------|
| Lease Expense Information:         | 2019                               | 2018    |
| Total lease expense <sup>(1)</sup> | \$4,803                            | \$5,024 |

<sup>(1)</sup> Lease expense related to corporate assets is included in general and administrative expenses and lease expense related to ground leases is included within operating expenses in the Company's consolidated statements of operations.

|   | Three Months<br>Ended<br>March 31, |         |
|---|------------------------------------|---------|
| Supplemental Cash Flow Information:                                   | 2019                               | 2018    |
| Cash paid for amounts included in the measurement of lease liability: |                                    |         |
| Operating cash flows for operating leases                             | \$3,963                            | \$4,253 |
| ROU asset obtained in exchange for new lease liability:               |                                    |         |
| Operating leases  | \$880                              | \$—     |

| Weighted Average Lease Term and Discount Rate: | March 31,<br>2019 |
|--|-------------------|
| Weighted average remaining lease term (years): |                   |
| Operating leases                               | 52                |
| Weighted average discount rate:                |                   |
| Operating leases                               | 4.36 %            |

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The following table summarizes future minimum lease obligations under non-cancelable ground and other operating leases as of March 31, 2019 (in thousands):

| Year  | Amount     |
|---|------------|
| 2019 (nine months)                          | \$5,937    |
| 2020  | 7,816      |
| 2021  | 7,888      |
| 2022  | 8,028      |
| 2023  | 8,198      |
| Thereafter                                  | 471,083    |
| Undiscounted minimum lease payments payable | 508,950    |
| Less: imputed interest                      | (356,113 ) |
| Present value of lease liability            | \$152,837  |

The following table summarizes future minimum lease obligations under non-cancelable ground and other operating leases as of December 31, 2018 (in thousands):

| Year       | Amount    |
|------------|-----------|
| 2019       | \$5,597   |
| 2020       | 5,687     |
| 2021       | 5,776     |
| 2022       | 5,862     |
| 2023       | 5,983     |
| Thereafter | 466,130   |
|            | \$495,035 |

**Depreciation Expense**

While the Company leases the majority of its property, plant, and equipment to various tenants under operating leases and DFLs, in certain situations, the Company owns and operates property, plant, and equipment for general corporate purposes. Corporate assets are recorded within other assets, net within the Company's consolidated balance sheets and depreciation expense for those assets is recorded in general and administrative expenses in the Company's consolidated statements of operations. Included within other assets, net as of both March 31, 2019 and December 31, 2018 is \$3 million and \$2 million, respectively, of accumulated depreciation related to corporate assets. Included within general and administrative expenses for the three months ended March 31, 2019 and 2018 is \$0.4 million and \$0.2 million, respectively, of depreciation expense related to corporate assets.

**NOTE 5. Loans Receivable**

The following table summarizes the Company's loans receivable (in thousands):

|  | March 31, 2019      |               |          | December 31, 2018   |               |          |
|--|---------------------|---------------|----------|---------------------|---------------|----------|
|  | Real Estate Secured | Other Secured | Total    | Real Estate Secured | Other Secured | Total    |
| Mezzanine  | \$—                 | \$20,545      | \$20,545 | \$—                 | \$21,013      | \$21,013 |
| Participating development loans and other <sup>(1)</sup> | 65,635              | —             | 65,635   | 42,037              | —             | 42,037   |
| Unamortized discounts, fees and costs                    | —                   | (41 )         | (41 )    | —                   | (52 )         | (52 )    |
|  | \$65,635            | \$20,504      | \$86,139 | \$42,037            | \$20,961      | \$62,998 |

(1) At March 31, 2019, the Company had \$53 million remaining of commitments to fund a \$115 million senior living development project.

Table of Contents*Loans Receivable Internal Ratings*

The following table summarizes the Company's internal ratings for loans receivable at March 31, 2019 (dollars in thousands):

| Investment Type     | Carrying Amount | Percentage of Loan Portfolio | Internal Ratings |                  |               |
|---------------------|-----------------|------------------------------|------------------|------------------|---------------|
|                     |                 |                              | Performing Loans | Watch List Loans | Workout Loans |
| Real estate secured | \$65,635        | 76                           | \$65,635         | \$ —             | —             |
| Other secured       | 20,504          | 24                           | 20,504           | —                | —             |
|                     | \$86,139        | 100                          | \$86,139         | \$ —             | —             |

*U.K. Bridge Loan*

In 2016, the Company provided a £105 million (\$131 million at closing) bridge loan to MMCG (the "U.K. Bridge Loan") to fund the acquisition of a portfolio of seven care homes in the U.K. Under the U.K. Bridge Loan, the Company retained a three year call option to acquire those seven care homes at a future date for £105 million, subject to certain conditions precedent being met. In March 2018, upon resolution of all conditions precedent, the Company began the process of exercising its call option to acquire the seven care homes and concluded that it should consolidate the real estate. As a result, the Company derecognized the outstanding loan receivable of £105 million and recognized a £29 million (\$41 million) loss on consolidation. Refer to Note 14 for the complete impact of consolidating the seven care homes during the first quarter of 2018.

In June 2018, the Company completed the process of exercising the above-mentioned call option. The seven care homes acquired through the call option were included in the U.K. JV transaction (see Note 3).

**NOTE 6. Investments in and Advances to Unconsolidated Joint Ventures**

The Company owns interests in the following entities that are accounted for under the equity method (dollars in thousands):

| Entity <sup>(1)</sup>                          | Property Count | Ownership % | Carrying Amount |                   |
|--|----------------|-------------|-----------------|-------------------|
|  |                |             | March 31, 2019  | December 31, 2018 |
| CCRC JV  | 15             | 49          | \$358,172       | \$365,764         |
| U.K. JV <sup>(2)</sup>                         | 68             | 49          | 102,692         | 101,735           |
| MBK JV   | 5              | 50          | 34,935          | 35,435            |
| Other SHOP JVs <sup>(3)</sup>                  | 5              | 50 - 90     | 24,684          | 25,493            |
| Medical Office JVs <sup>(4)</sup>              | 3              | 20 - 67     | 10,039          | 10,160            |
| K&Y JVs <sup>(5)</sup>                         | 3              | 80          | 1,431           | 1,430             |
| Advances to unconsolidated joint ventures, net |                |             | 13              | 71                |
|  |                |             | \$531,966       | \$540,088         |

(1) These entities are not consolidated because the Company does not control, through voting rights or other means, the joint ventures.

(2) See Note 3 for discussion of the formation of the U.K. JV and the Company's equity method investment.

(3) Includes four unconsolidated SHOP joint ventures (and the Company's ownership percentage): (i) Vintage Park Development JV (85%); (ii) Waldwick JV (85%); (iii) Otay Ranch JV (90%); and (iv) MBK Development JV (50%).

(4) Includes three unconsolidated medical office joint ventures (and the Company's ownership percentage): HCP Ventures IV, LLC (20%); HCP Ventures III, LLC (30%); and Suburban Properties, LLC (67%).

(5) At March 31, 2019, includes two unconsolidated joint ventures. At December 31, 2018, includes three unconsolidated joint ventures.



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Intangible assets primarily consist of lease-up intangibles and above market tenant lease intangibles. Intangible liabilities primarily consist of below market lease intangibles. The following tables summarize the Company's intangible lease assets and liabilities (in thousands):

| Intangible lease assets                   | March 31,<br>2019 | December 31,<br>2018 |
|---|-------------------|----------------------|
| Gross intangible lease assets             | \$491,998         | \$556,114            |
| Accumulated depreciation and amortization | (216,433 )        | (251,035 )           |
| Intangible assets, net                    | \$275,565         | \$305,079            |

| Intangible lease liabilities              | March 31,<br>2019 | December 31,<br>2018 |
|---|-------------------|----------------------|
| Gross intangible lease liabilities        | \$82,777          | \$94,444             |
| Accumulated depreciation and amortization | (33,289 )         | (39,781 )            |
| Intangible liabilities, net               | \$49,488          | \$54,663             |

On January 1, 2019, in conjunction with the adoption of ASU 2016-12 (see Note 2), the Company reclassified \$39 million of intangible assets, net and \$6 million of intangible liabilities, net related to above and below market ground leases to right-of-use asset, net.

**NOTE 8. Debt***Bank Line of Credit and Term Loan*

The Company's \$2.0 billion unsecured revolving line of credit facility (the "Facility") matures on October 19, 2021 and contains two, six months extension options. Borrowings under the Facility accrue interest at LIBOR plus a margin that depends on the Company's credit ratings. The Company pays a facility fee on the entire revolving commitment that depends on its credit ratings. Based on the Company's credit ratings at March 31, 2019, the margin on the Facility was 0.875% and the facility fee was 0.15%. The Facility also includes a feature that allows the Company to increase the borrowing capacity by an aggregate amount of up to \$750 million, subject to securing additional commitments. At March 31, 2019, the Company had \$277 million, including £55 million (\$72 million), outstanding under the Facility, with a weighted average effective interest rate of 3.20%.

The Facility contains certain financial restrictions and other customary requirements, including cross-default provisions to other indebtedness. Among other things, these covenants, using terms defined in the agreements: (i) limit the ratio of Consolidated Total Indebtedness to Consolidated Total Asset Value to 60%; (ii) limit the ratio of Secured Debt to Consolidated Total Asset Value to 30%; (iii) limit the ratio of Unsecured Debt to Consolidated Unencumbered Asset Value to 60%; (iv) require a minimum Fixed Charge Coverage ratio of 1.5 times; and (v) require a Minimum Consolidated Tangible Net Worth of \$6.5 billion. At March 31, 2019, the Company believes it was in compliance with each of these restrictions and requirements of the Facility.

On July 3, 2018, the Company exercised its one-time right under its term loan to repay the outstanding British pound sterling ("GBP") balance and re-borrow in U.S. Dollars ("USD") with all other key terms unchanged, which resulted in repayment of the £169 million balance and re-borrowing of \$224 million. In November 2018, the Company repaid the \$224 million unsecured term loan, bringing the total term loan balance to zero.

*Senior Unsecured Notes*

At March 31, 2019, the Company had senior unsecured notes outstanding with an aggregate principal balance of \$5.3 billion. The senior unsecured notes contain certain covenants including limitations on debt, maintenance of unencumbered assets, cross-acceleration provisions and other customary terms. The Company believes it was in compliance with these covenants at March 31, 2019.



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There were no senior unsecured notes payoffs during the three months ended March 31, 2019. The following table summarizes the Company's senior unsecured notes payoffs during the year ended December 31, 2018 (dollars in thousands):

| Date                         | Amount    | Coupon Rate |
|------------------------------|-----------|-------------|
| July 16, 2018 <sup>(1)</sup> | \$700,000 | 5.375%      |
| November 8, 2018             | \$450,000 | 3.750%      |

<sup>(1)</sup>The Company recorded a \$44 million loss on debt extinguishment related to the repurchase of senior notes.

There were no senior unsecured notes issuances during the three months ended March 31, 2019 or year ended December 31, 2018.

*Mortgage Debt*

At March 31, 2019, the Company had \$132 million in aggregate principal of mortgage debt outstanding, which is secured by 15 healthcare facilities with an aggregate carrying value of \$276 million.

Mortgage debt generally requires monthly principal and interest payments, is collateralized by real estate assets and is generally non-recourse. Mortgage debt typically restricts transfer of the encumbered assets, prohibits additional liens, restricts prepayment, requires payment of real estate taxes, requires maintenance of the assets in good condition, requires insurance on the assets and includes conditions to obtain lender consent to enter into or terminate material leases. Some of the mortgage debt may require tenants or operators to maintain compliance with the applicable leases or operating agreements of such real estate assets.

*Debt Maturities*

The following table summarizes the Company's stated debt maturities and scheduled principal repayments at March 31, 2019 (in thousands):

| Year                                     | Bank Line of Credit <sup>(1)</sup> | Senior Unsecured Notes <sup>(2)</sup> | Mortgage Debt <sup>(3)</sup> | Total <sup>(4)</sup> |
|--|------------------------------------|---------------------------------------|------------------------------|----------------------|
| 2019 (nine months)                       | \$—                                | \$—                                   | \$2,686                      | \$2,686              |
| 2020                                     | —                                  | 800,000                               | 3,609                        | 803,609              |
| 2021                                     | 276,500                            | —                                     | 10,957                       | 287,457              |
| 2022                                     | —                                  | 900,000                               | 2,691                        | 902,691              |
| 2023                                     | —                                  | 800,000                               | 2,811                        | 802,811              |
| Thereafter                               | —                                  | 2,800,000                             | 109,705                      | 2,909,705            |
|  | 276,500                            | 5,300,000                             | 132,459                      | 5,708,959            |
| (Discounts), premium and debt costs, net | —                                  | (39,378 )                             | 5,066                        | (34,312 )            |
|  | \$276,500                          | \$5,260,622                           | \$137,525                    | \$5,674,647          |

<sup>(1)</sup>Includes £55 million translated into USD.

<sup>(2)</sup>Effective interest rates on the notes ranged from 2.79% to 6.87% with a weighted average effective interest rate of 4.03% and a weighted average maturity of five years.

<sup>(3)</sup>Effective interest rates on the mortgage debt ranged from 2.47% to 5.91% with a weighted average effective interest rate of 4.19% and a weighted average maturity of 19 years.

<sup>(4)</sup>Excludes \$89 million of other debt that have no scheduled maturities.

**NOTE 9. Commitments and Contingencies***Legal Proceedings*

From time to time, the Company is a party to, or has a significant relationship to, legal proceedings, lawsuits and other claims. Except as described below, the Company is not aware of any legal proceedings or claims that it believes may have, individually or taken together, a material adverse effect on the Company's financial condition, results of operations or cash flows. The Company's policy is to expense legal costs as they are incurred.



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*Class Action.* On May 9, 2016, a purported stockholder of the Company filed a putative class action complaint, *Boynton Beach Firefighters' Pension Fund v. HCP, Inc., et al.*, Case No. 3:16-cv-01106-JJH, in the U.S. District Court for the Northern District of Ohio against the Company, certain of its officers, HCR ManorCare, Inc. ("HCRMC"), and certain of its officers, asserting violations of the federal securities laws. The suit asserts claims under sections 10(b) and 20(a) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and alleges that the Company made certain false or misleading statements relating to the value of and risks concerning its investment in HCRMC by allegedly failing to disclose that HCRMC had engaged in billing fraud, as alleged by the U.S. Department of Justice ("DoJ") in a suit against HCRMC arising from the False Claims Act that the DoJ voluntarily dismissed with prejudice. The plaintiff in the class action suit demands compensatory damages (in an unspecified amount), costs and expenses (including attorneys' fees and expert fees), and equitable, injunctive, or other relief as the Court deems just and proper. On November 28, 2017, the Court appointed Societe Generale Securities GmbH (SGSS Germany) and the City of Birmingham Retirement and Relief Systems (Birmingham) as Co-Lead Plaintiffs in the class action. The motion to dismiss was fully briefed on May 21, 2018 and oral arguments were held on October 23, 2018. Subsequently, on December 6, 2018, HCRMC and its officers were voluntarily dismissed from the class action lawsuit without prejudice to such claims being refiled. The Company believes the suit to be without merit and intends to vigorously defend against it.

*Derivative Actions.* On June 16, 2016 and July 5, 2016, purported stockholders of the Company filed two derivative actions, respectively, *Subodh v. HCR ManorCare Inc., et al.*, Case No. 30-2016-00858497-CU-PT-CXC and *Stearns v. HCR ManorCare, Inc., et al.*, Case No. 30-2016-00861646-CU-MC-CJC, in the Superior Court of California, County of Orange, against certain of the Company's current and former directors and officers and HCRMC. The Company is named as a nominal defendant. As both derivative actions contained substantially the same allegations, they have been consolidated into a single action (the "California derivative action"). The consolidated action alleges that the defendants engaged in various acts of wrongdoing, including, among other things, breaching fiduciary duties by publicly making false or misleading statements of fact regarding HCRMC's finances and prospects, and failing to maintain adequate internal controls. On April 18, 2017, the Court approved the parties' stipulation to stay the case pending disposition of the motion to dismiss the class action litigation.

On April 10, 2017, a purported stockholder of the Company filed a derivative action, *Weldon v. Martin et al.*, Case No. 3:17-cv-755, in federal court in the Northern District of Ohio, Western Division, against certain of the Company's current and former directors and officers and HCRMC. The Company is named as a nominal defendant. The *Weldon* complaint asserts similar claims to those asserted in the California derivative action. In addition, the complaint asserts a claim under Section 14(a) of the Exchange Act, alleging that the Company made false statements in its 2016 proxy statement by not disclosing that the Company's performance issues in 2015 were the direct result of alleged billing fraud at HCRMC. On April 18, 2017, the Court re-assigned and transferred this action to the judge presiding over the related federal securities class action. On July 11, 2017, the Court approved a stipulation by the parties to stay the case pending disposition of the motion to dismiss the class action.

On July 21, 2017, a purported stockholder of the Company filed another derivative action, *Kelley v. HCR ManorCare, Inc., et al.*, Case No. 8:17-cv-01259, in federal court in the Central District of California, against certain of the Company's current and former directors and officers and HCRMC. The Company is named as a nominal defendant. The *Kelley* complaint asserts similar claims to those asserted in *Weldon* and in the California derivative action. Like *Weldon*, the *Kelley* complaint also additionally alleges that the Company made false statements in its 2016 proxy statement, and asserts a claim for a violation of Section 14(a) of the Exchange Act. On November 28, 2017, the federal court in the Central District of California granted Defendants' motion to transfer the action to the Northern District of Ohio (i.e., the court where the class action and other federal derivative action are pending). The Court in the Northern District of Ohio is currently considering whether to consolidate the *Weldon* and *Kelley* actions, appointment of lead plaintiffs and counsel, and whether the stay in *Weldon* should continue as to either or both actions.

The Company's Board of Directors received letters dated August 17, 2016, April 19, 2017, and April 20, 2017 from private law firms acting on behalf of clients who are purported stockholders of the Company, each asserting allegations similar to those made in the California derivative action matters discussed above. Each letter demands that the Board of Directors take action to assert the Company's rights. The Board of Directors completed its evaluation and

rejected the demand letters in December of 2017.

The Company believes that the plaintiffs lack standing or the lawsuits and demands are without merit, but cannot predict the outcome of these proceedings or reasonably estimate any potential loss at this time. Accordingly, no loss contingency has been recorded for these matters as of March 31, 2019, as the likelihood of loss is not considered probable or estimable.

Table of Contents**NOTE 10. Equity***At-The-Market Equity Offering Program*

In June 2015, the Company established an at-the-market equity offering program (“ATM Program”) to sell shares of its common stock from time to time through a consortium of banks acting as sales agents or directly to the banks acting as principals. In May 2018, the Company renewed its ATM Program (the “2018 ATM Program”). During the year ended December 31, 2018, the Company issued 5.4 million shares of common stock at a weighted average net price of \$28.27 for net proceeds of \$154 million.

In February 2019, the Company terminated the 2018 ATM Program and established a new ATM Program (the “2019 ATM Program”) pursuant to which shares of common stock having an aggregate gross sales price of up to \$1.0 billion may be sold (i) by the Company through a consortium of banks acting as sales agents or directly to the banks acting as principals, or (ii) by a consortium of banks acting as forward sellers on behalf of any forward purchasers pursuant to a forward sale agreement. The use of a forward sale agreement would allow the Company to lock in a share price on the sale of shares at the time the agreement is effective, but defer receiving the proceeds from the sale of shares until a later date.

During the three months ended March 31, 2019, the Company utilized the forward provisions under the 2019 ATM Program to allow for the sale of up to an aggregate of 3.6 million shares of its common stock at an initial weighted average net price of \$31.19 per share, after commissions. Each forward sale has a one year term, during which time the Company must settle the forward sale by delivery of physical shares of common stock to the forward seller or, at the Company’s election, in cash or net shares. The forward sale price that the Company expects to receive upon settlement will be the initial forward price established upon the effective date, subject to adjustments for: (i) accrued interest, (ii) the forward purchasers’ stock borrowing costs, and (iii) certain fixed price reductions during the term of the agreement. At March 31, 2019, no shares had been issued to settle any of the forward sales, all of which remain outstanding.

At March 31, 2019, approximately \$888 million of our common stock remained available for sale under the 2019 ATM Program.

Subsequent to March 31, 2019, the Company utilized the forward provisions under the 2019 ATM Program to allow for the sale of up to an additional 1.5 million shares of its common stock at an initial weighted average net price of \$30.63 per share, after commissions. Each forward sale has a one year term, during which time the Company must settle the forward sale by delivery of physical shares of common stock to the forward seller or, at the Company’s election, in cash or net shares.

*2018 Forward Equity Offering*

In December 2018, the Company entered into a forward sales agreement to sell up to an aggregate of 15.25 million shares of its common stock (including shares issued through the exercise of underwriters’ options) at an initial net price of \$28.60 per share, after underwriting discounts and commissions. The agreement has a one year term that expires on December 13, 2019 during which time the Company may settle the forward sales agreement by delivery of physical shares of common stock to the forward seller or, at the Company’s election, by settling in cash or net shares. The forward sale price that the Company expects to receive upon settlement of the agreement will be the initial net price of \$28.60, subject to adjustments for: (i) accrued interest, (ii) the forward purchasers’ stock borrowing costs, and (iii) certain fixed price reductions during the term of the agreement. At March 31, 2019, no shares have been issued under the forward sales agreement, which remains outstanding.

In December 2018, contemporaneous with the forward equity offering discussed above, the Company completed an offering of 2 million shares of common stock at a net price of \$28.60 per share, resulting in net proceeds of \$57 million.

*Accumulated Other Comprehensive Income (Loss)*

The following table summarizes the Company’s accumulated other comprehensive income (loss) (in thousands):

|   | March 31,<br>2019 | December 31,<br>2018 |
|---|-------------------|----------------------|
| Cumulative foreign currency translation adjustment <sup>(1)</sup> | \$(1,021)         | \$(1,683)            |

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|  |            |            |
|--|------------|------------|
| Unrealized gains (losses) on derivatives, net                      | (373 )     | (467 )     |
| Supplemental Executive Retirement plan minimum liability and other | (2,489 )   | (2,558 )   |
| Total accumulated other comprehensive income (loss)                | \$(3,883 ) | \$(4,708 ) |

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(1) See Note 3 for a discussion of the U.K. JV transaction.



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**NOTE 11. Segment Disclosures**

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The Company evaluates its business and allocates resources based on its reportable business segments: (i) senior housing triple-net, (ii) SHOP, (iii) life science and (iv) medical office. The Company has non-reportable segments that are comprised primarily of the Company's debt investments, hospital properties, unconsolidated joint ventures, and U.K. investments. The accounting policies of the segments are the same as those in Note 2 to the Consolidated Financial Statements in the Company's 2018 Annual Report on Form 10-K filed with the SEC, as updated by Note 2 herein.

During the first quarter of 2019, as a result of a change in how operating results are reported to the chief operating decision makers for the purpose of evaluating performance and allocating resources, the Company reclassified operating results related to two facilities from its other non-reportable segment to its medical office segment. Accordingly, all prior period segment information has been recast to conform to current period presentation.

During the three months ended March 31, 2019, 18 senior housing triple-net facilities were transferred to the Company's SHOP segment as a result of terminating the triple-net leases and transitioning the assets to a RIDEA structure. During the three months ended March 31, 2018, there were no transfers of assets between segments. When an asset is transferred from one segment to another, the results associated with that asset are included in the original segment until the date of transfer. Results generated after the transfer date are included in the new segment.

The Company evaluates performance based upon: (i) property NOI and (ii) Adjusted NOI. NOI is defined as real estate revenues (inclusive of rental and related revenues, resident fees and services, and income from direct financing leases), less property level operating expenses (which exclude transition costs); NOI excludes all other financial statement amounts included in net income (loss). Adjusted NOI is calculated as NOI after eliminating the effects of straight-line rents, DFL non-cash interest, amortization of market lease intangibles, termination fees, actuarial reserves for insurance claims that have been incurred but not reported, and the impact of deferred community fee income and expense.

NOI and Adjusted NOI exclude the Company's share of income (loss) from unconsolidated joint ventures, which is recognized as equity income (loss) from unconsolidated joint ventures in the consolidated statements of operations. Non-segment assets consist of assets in the Company's other non-reportable segments and corporate non-segment assets. Corporate non-segment assets consist primarily of corporate assets, including cash and cash equivalents, restricted cash, accounts receivable, net, marketable equity securities and, if any, real estate assets and liabilities held for sale. See Note 15 for other information regarding concentrations of credit risk.

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The following tables summarize information for the reportable segments (in thousands):

For the three months ended March 31, 2019:

|  | Senior<br>Housing<br>Triple-Net | SHOP      | Life Science | Medical<br>Office | Other<br>Non-reportable | Corporate<br>Non-segment | Total      |
|--|---------------------------------|-----------|--------------|-------------------|-------------------------|--------------------------|------------|
| Real estate revenues <sup>(1)</sup>                        | \$58,892                        | \$126,181 | \$94,473     | \$142,195         | \$12,700                | \$—                      | \$434,441  |
| Operating expenses   | (993 )                          | (96,948 ) | (21,992 )    | (48,987 )         | (7 )                    | —                        | (168,927 ) |
| NOI  | 57,899                          | 29,233    | 72,481       | 93,208            | 12,693                  | —                        | 265,514    |
| Adjustments to NOI <sup>(2)</sup>                          | 564                             | 1,152     | (2,478 )     | (1,771 )          | 195                     | —                        | (2,338 )   |
| Adjusted NOI   | 58,463                          | 30,385    | 70,003       | 91,437            | 12,888                  | —                        | 263,176    |
| Addback adjustments  | (564 )                          | (1,152 )  | 2,478        | 1,771             | (195 )                  | —                        | 2,338      |
| Interest income  | —                               | —         | —            | —                 | 1,713                   | —                        | 1,713      |
| Interest expense   | (589 )                          | (663 )    | (73 )        | (111 )            | —                       | (47,891 )                | (49,327 )  |
| Depreciation and amortization                              | (16,683 )                       | (24,086 ) | (36,246 )    | (53,101 )         | (1,835 )                | —                        | (131,951 ) |
| General and administrative                                 | —                               | —         | —            | —                 | —                       | (21,355 )                | (21,355 )  |
| Transaction costs  | —                               | —         | —            | —                 | —                       | (4,518 )                 | (4,518 )   |
| Recoveries (impairments), net                              | —                               | —         | —            | (8,858 )          | —                       | —                        | (8,858 )   |
| Gain (loss) on sales of real estate, net                   | 3,557                           | 4,487     | —            | —                 | —                       | —                        | 8,044      |
| Other income (expense), net                                | —                               | —         | —            | —                 | —                       | 3,133                    | 3,133      |
| Income tax benefit (expense)                               | —                               | —         | —            | —                 | —                       | 3,458                    | 3,458      |
| Equity income (loss) from<br>unconsolidated joint ventures | —                               | —         | —            | —                 | (863 )                  | —                        | (863 )     |
| Net income (loss)  | \$44,184                        | \$8,971   | \$36,162     | \$31,138          | \$11,708                | \$(67,173 )              | \$64,990   |

(1) Represents rental and related revenues, resident fees and services, and income from DFLs.

(2) Represents straight-line rents, DFL non-cash interest, amortization of market lease intangibles, net, actuarial reserves for insurance claims that have been incurred but not reported, deferral of community fees, net and termination fees.

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For the three months ended March 31, 2018:

|  | Senior<br>Housing<br>Triple-Net | SHOP       | Life Science | Medical<br>Office | Other<br>Non-reportable | Corporate<br>Non-segment | Total      |
|--|---------------------------------|------------|--------------|-------------------|-------------------------|--------------------------|------------|
| Real estate revenues <sup>(1)</sup>                        | \$74,289                        | \$144,670  | \$99,622     | \$133,220         | \$21,031                | \$—                      | \$472,832  |
| Operating expenses   | (1,045 )                        | (101,746 ) | (21,809 )    | (47,878 )         | (74 )                   | —                        | (172,552 ) |
| NOI  | 73,244                          | 42,924     | 77,813       | 85,342            | 20,957                  | —                        | 300,280    |
| Adjustments to NOI <sup>(2)</sup>                          | (1,865 )                        | (1,607 )   | (3,751 )     | (1,932 )          | (531 )                  | —                        | (9,686 )   |
| Adjusted NOI   | 71,379                          | 41,317     | 74,062       | 83,410            | 20,426                  | —                        | 290,594    |
| Addback adjustments  | 1,865                           | 1,607      | 3,751        | 1,932             | 531                     | —                        | 9,686      |
| Interest income  | —                               | —          | —            | —                 | 6,365                   | —                        | 6,365      |
| Interest expense   | (600 )                          | (988 )     | (83 )        | (120 )            | (728 )                  | (72,583 )                | (75,102 )  |
| Depreciation and amortization                              | (21,906 )                       | (27,628 )  | (36,080 )    | (47,198 )         | (10,438 )               | —                        | (143,250 ) |
| General and administrative                                 | —                               | —          | —            | —                 | —                       | (29,175 )                | (29,175 )  |
| Transaction costs  | —                               | —          | —            | —                 | —                       | (2,195 )                 | (2,195 )   |
| Gain (loss) on sales of real estate, net                   | —                               | 20,815     | —            | —                 | —                       | —                        | 20,815     |
| Other income (expense), net                                | —                               | —          | —            | —                 | (40,567 )               | 160                      | (40,407 )  |
| Income tax benefit (expense)                               | —                               | —          | —            | —                 | —                       | 5,336                    | 5,336      |
| Equity income (loss) from<br>unconsolidated joint ventures | —                               | —          | —            | —                 | 570                     | —                        | 570        |
| Net income (loss)  | \$50,738                        | \$35,123   | \$41,650     | \$38,024          | \$(23,841 )             | \$(98,457 )              | \$43,237   |

(1) Represents rental and related revenues, resident fees and services, and income from DFLs.

(2) Represents straight-line rents, DFL non-cash interest, amortization of market lease intangibles, net, actuarial reserves for insurance claims that have been incurred but not reported, deferral of community fees, net and termination fees.

The following table summarizes the Company's revenues by segment (in thousands):

| Segment                       | Three Months Ended<br>March 31, |           |
|-------------------------------|---------------------------------|-----------|
|                               | 2019                            | 2018      |
| Senior housing triple-net     | \$58,892                        | \$74,289  |
| SHOP                          | 126,181                         | 144,670   |
| Life science                  | 94,473                          | 99,622    |
| Medical office                | 142,195                         | 133,220   |
| Other non-reportable segments | 14,413                          | 27,396    |
| Total revenues                | \$436,154                       | \$479,197 |

See Note 3 for significant transactions impacting the Company's segment assets during the periods presented.

Table of Contents**NOTE 12. Earnings Per Common Share**

Basic income (loss) per common share (“EPS”) is computed based upon the weighted average number of common shares outstanding. Diluted income (loss) per common share is computed based upon the weighted average number of common shares outstanding plus the impact of forward equity sales agreements using the treasury stock method and common shares issuable from the assumed conversion of DownREIT units, stock options, certain performance restricted stock units and unvested restricted stock units. Only those instruments having a dilutive impact on our basic income (loss) per share are included in diluted income (loss) per share during the periods presented.

Restricted stock and certain performance restricted stock units are considered participating securities, because dividend payments are not forfeited even if the underlying award does not vest, and require use of the two-class method when computing basic and diluted earnings per share.

During the first quarter of 2019, the Company utilized the forward sale provisions under the 2019 ATM Program to sell up to an aggregate of 3.6 million shares with a one year term. Additionally, in December 2018, the Company entered into a forward equity sales agreement to sell up to an aggregate of 15.25 million shares of its common stock by no later than December 13, 2019. The Company expects to settle the forward sales with shares of common stock prior to their respective expiration dates. See Note 10 for further details.

The Company considered the potential dilution resulting from the forward agreements to the calculation of earnings per share. At inception, the agreements do not have an effect on the computation of basic EPS as no shares are delivered until settlement. However, the Company uses the treasury stock method to determine the dilution, if any, resulting from the forward sales agreements during the period of time prior to settlement. The aggregate effect on the Company’s diluted weighted-average common shares for the three months ended March 31, 2019, was 1.1 million weighted-average incremental shares from the forward equity sales agreements.

The following table illustrates the computation of basic and diluted earnings per share (in thousands, except per share amounts):

|  | <b>Three Months Ended</b> |             |
|--|---------------------------|-------------|
|  | <b>March 31,</b>          |             |
|  | <b>2019</b>               | <b>2018</b> |
| <b>Numerator</b>   |                           |             |
| Net income (loss)  | \$64,990                  | \$43,237    |
| Noncontrolling interests' share in earnings                  | (3,520 )                  | (3,005 )    |
| Net income (loss) attributable to HCP, Inc.                  | 61,470                    | 40,232      |
| Less: Participating securities' share in earnings            | (441 )                    | (391 )      |
| Net income (loss) applicable to common shares                | \$61,029                  | \$39,841    |
| <b>Denominator</b>   |                           |             |
| Basic weighted average shares outstanding                    | 477,766                   | 469,557     |
| Dilutive potential common shares - equity awards             | 272                       | 138         |
| Dilutive potential common shares - forward equity agreements | 1,093                     | —           |
| Diluted weighted average common shares                       | 479,131                   | 469,695     |
| <b>Basic earnings per common share</b>                       |                           |             |
| Basic  | \$0.13                    | \$0.08      |
| Diluted  | \$0.13                    | \$0.08      |

For the three months ended March 31, 2019 and 2018, 6 million and 7 million shares, respectively, issuable upon conversion of DownREIT units were not included because they are anti-dilutive. Additionally, for the three months ended March 31, 2019, 18 million shares of common stock issuable pursuant to the settlement of forward equity sales agreements were not included because they are anti-dilutive (see discussion above). For all periods presented in the above table, approximately 1 million shares of common stock subject to outstanding equity awards (restricted stock units and stock options) were not included because they are anti-dilutive.



Table of Contents**NOTE 13. Supplemental Cash Flow Information**

The following table provides supplemental cash flow information (in thousands):

|   | Three Months Ended<br>March 31, |          |
|---|---------------------------------|----------|
|   | 2019                            | 2018     |
| <i>Supplemental cash flow information:</i>  |                                 |          |
| Interest paid, net of capitalized interest  | \$53,475                        | \$92,701 |
| Income taxes paid (refunded)  | (769 )                          | 340      |
| Capitalized interest  | 8,369                           | 3,578    |
| <i>Supplemental schedule of non-cash investing and financing activities:</i>                    |                                 |          |
| Accrued construction costs  | 94,904                          | 62,160   |
| Derecognition of U.K. Bridge Loan receivable  | —                               | 147,474  |
| Consolidation of net assets related to U.K. Bridge Loan   | —                               | 106,457  |
| Vesting of restricted stock units and conversion of non-managing member units into common stock | 4,341                           | 258      |
| Conversion of DFLs to real estate   | 350,540                         | —        |

See discussion related to the U.K. Bridge Loan in Notes 5 and 14.

The following table summarizes cash, cash equivalents and restricted cash (in thousands):

|  | March 31, |           |
|--|-----------|-----------|
|  | 2019      | 2018      |
| Cash and cash equivalents                  | \$120,117 | \$86,021  |
| Restricted cash                            | 26,535    | 31,947    |
| Cash, cash equivalents and restricted cash | \$146,652 | \$117,968 |

**NOTE 14. Variable Interest Entities***Unconsolidated Variable Interest Entities*

At March 31, 2019, the Company had investments in: (i) 30 properties leased to VIE tenants, (ii) four unconsolidated VIE joint ventures, (iii) marketable debt securities of one VIE, and (iv) one loan to a VIE borrower. The Company has determined that it is not the primary beneficiary of and therefore does not consolidate these VIEs because it does not have the ability to control the activities that most significantly impact their economic performance. Except for the Company's equity interest in the unconsolidated joint ventures (CCRC OpCo, Vintage Park Development JV, Waldwick JV and the LLC investment discussed below), it has no formal involvement in these VIEs beyond its investments.

The Company leases 30 properties to a total of four tenants that have also been identified as VIEs ("VIE tenants"). These VIE tenants are "thinly capitalized" entities that rely on the operating cash flows generated from the senior housing facilities to pay operating expenses, including the rent obligations under their leases.

The Company holds a 49% ownership interest in CCRC OpCo, a joint venture entity formed in August 2014 that operates senior housing properties in a RIDEA structure and has been identified as a VIE. The equity members of CCRC OpCo "lack power" because they share certain operating rights with Brookdale, as manager of the CCRCs. The assets of CCRC OpCo primarily consist of the CCRCs that it owns and leases, resident fees receivable, notes receivable, and cash and cash equivalents; its obligations primarily consist of operating lease obligations to CCRC PropCo, debt service payments and capital expenditures for the properties, and accounts payable and expense accruals associated with the cost of its CCRCs' operations. Assets generated by the CCRC operations (primarily rents from CCRC residents) of CCRC OpCo may only be used to settle its contractual obligations (primarily from debt service payments, capital expenditures, and rental costs and operating expenses incurred to manage such facilities).



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The Company holds an 85% ownership interest in a joint venture (Vintage Park Development JV), which has been identified as a VIE as power is shared with a member that does not have a substantive equity investment at risk. The assets of the joint venture primarily consist of a leased property (net real estate), rents receivable, and cash and cash equivalents; its obligations primarily consist of debt-service payments. Any assets generated by the joint venture may only be used to settle its respective contractual obligations (primarily debt service payments).

The Company holds an 85% ownership interest in a development joint venture (Waldwick JV), which has been identified as a VIE as power is shared with a member that does not have a substantive equity investment at risk. The assets of the joint venture primarily consist of an in-progress senior housing facility development project that it owns and cash and cash equivalents; its obligations primarily consist of accounts payable and expense accruals associated with the cost of its development obligations. Any assets generated by the joint venture may only be used to settle its respective contractual obligations (primarily development expenses and debt service payments).

The Company holds a limited partner ownership interest in an unconsolidated LLC that has been identified as a VIE. The Company's involvement in the entity is limited to its equity investment as a limited partner, and it does not have any substantive participating rights or kick-out rights over the general partner. The assets and liabilities of the entity primarily consist of those associated with its senior housing real estate and development activities. Any assets generated by the entity may only be used to settle its contractual obligations (primarily development expenses and debt service payments).

The Company holds commercial mortgage-backed securities ("CMBS") issued by Federal Home Loan Mortgage Corporation (commonly referred to as Freddie MAC) through a special purpose entity that has been identified as a VIE because it is "thinly capitalized." The CMBS issued by the VIE are backed by mortgage debt obligations on real estate assets.

The Company provided seller financing of \$10 million related to its sale of seven senior housing triple-net facilities. The financing was provided in the form of a secured five year mezzanine loan to a "thinly capitalized" borrower created to acquire the facilities.

The classification of the related assets and liabilities and the maximum loss exposure as a result of the Company's involvement with these VIEs at March 31, 2019 was as follows (in thousands):

| VIE Type                                      | Asset/Liability Type                                      | Maximum Loss Exposure and Carrying Amount <sup>(1)</sup> |
|---|---|--|
| VIE tenants - DFLs <sup>(2)</sup>             | Net investment in DFLs                                    | \$ 249,803   |
| VIE tenants - operating leases <sup>(2)</sup> | Lease intangibles, net and straight-line rent receivables | 6,909  |
| CCRC OpCo                                     | Investments in unconsolidated joint ventures              | 175,011  |
| Unconsolidated development joint ventures     | Investments in unconsolidated joint ventures              | 15,206   |
| Loan - seller financing                       | Loans receivable, net                                     | 10,000   |
| CMBS and LLC investment                       | Marketable debt and LLC investment                        | 34,397   |

(1) The Company's maximum loss exposure represents the aggregate carrying amount of such investments (including accrued interest).

(2) The Company's maximum loss exposure may be mitigated by re-leasing the underlying properties to new tenants upon an event of default.

At March 31, 2019, the Company had not provided, and is not required to provide, financial support through a liquidity arrangement or otherwise, to its unconsolidated VIEs, including circumstances in which it could be exposed to further losses (e.g., cash shortfalls).

See Notes 4, 5 and 6 for additional descriptions of the nature, purpose and operating activities of the Company's unconsolidated VIEs and interests therein.



Table of Contents*Consolidated Variable Interest Entities*

HCP, Inc.'s consolidated total assets and total liabilities at March 31, 2019 and December 31, 2018 include certain assets of VIEs that can only be used to settle the liabilities of the related VIE. The VIE creditors do not have recourse to HCP, Inc. Total assets and total liabilities include VIE assets and liabilities as follows (in thousands):

|  | March 31, 2019 | December 31,<br>2018 |
|--|----------------|----------------------|
| Assets   |                |                      |
| Buildings and improvements                                   | \$2,001,875    | \$1,949,582          |
| Development costs and construction in progress               | 43,481         | 39,584               |
| Land   | 196,484        | 151,746              |
| Accumulated depreciation and amortization                    | (424,325 )     | (398,143 )           |
| Net real estate  | 1,817,515      | 1,742,769            |
| Investments in and advances to unconsolidated joint ventures | 1,534          | 1,550                |
| Accounts receivable, net                                     | 6,811          | 7,904                |
| Cash and cash equivalents                                    | 32,831         | 23,772               |
| Restricted cash  | 3,386          | 3,399                |
| Intangible assets, net                                       | 96,197         | 111,333              |
| Right-of-use asset, net                                      | 93,796         | —                    |
| Other assets, net  | 44,312         | 43,149               |
| Total assets   | \$2,096,382    | \$1,933,876          |
| Liabilities  |                |                      |
| Mortgage debt  | 44,500         | 44,598               |
| Intangible liabilities, net                                  | 17,014         | 19,128               |
| Lease liability  | 90,043         | —                    |
| Accounts payable and accrued liabilities                     | 56,542         | 66,736               |
| Deferred revenue   | 23,536         | 24,215               |
| Total liabilities  | \$231,635      | \$154,677            |

*HCP Ventures V, LLC.* The Company holds a 51% ownership interest in and is the managing member of a joint venture entity formed in October 2015 that owns and leases MOB's ("HCP Ventures V"). The Company classifies HCP Ventures V as a VIE due to the non-managing member lacking substantive participation rights in the management of HCP Ventures V or kick-out rights over the managing member. The Company consolidates HCP Ventures V as the primary beneficiary because it has the ability to control the activities that most significantly impact the VIE's economic performance. The assets of HCP Ventures V primarily consist of leased properties (net real estate), rents receivable, and cash and cash equivalents; its obligations primarily consist of capital expenditures for the properties. Assets generated by HCP Ventures V may only be used to settle its contractual obligations (primarily from capital expenditures).

*Vintage Park JV.* The Company holds a 90% ownership interest in and is the managing member of a joint venture entity formed in January 2015 ("Vintage Park JV") that owns an 85% interest in an unconsolidated development VIE. The Company classifies Vintage Park JV as a VIE due to the non-managing member lacking substantive participation rights in the management of the Vintage Park JV or kick-out rights over the managing member. The Company consolidates Vintage Park JV as the primary beneficiary because it has the ability to control the activities that most significantly impact the VIE's economic performance. The assets of Vintage Park JV primarily consist of an investment in the Vintage Park Development JV and cash and cash equivalents; its obligations primarily consist of funding the ongoing development of the Vintage Park Development JV. Assets generated by the Vintage Park JV may only be used to settle its contractual obligations (primarily from the funding of the Vintage Park Development JV).

*Watertown JV.* The Company holds a 95% ownership interest in and is the managing member of joint venture entities formed in November 2017 that own and operate a senior housing property in a RIDEA structure ("Watertown JV"). Watertown PropCo is a VIE as the Company and the non-managing member share in control of the entity, but

substantially all of the entity's activities are performed on behalf of the Company. Watertown OpCo is a VIE as the non-managing member, through its equity interest, lacks substantive participation rights in the management of Watertown OpCo or kick-out rights over the managing member. The Company consolidates Watertown PropCo and Watertown OpCo as the primary beneficiary because it has the ability to control the activities that most significantly impact these VIEs' economic performance. The assets of Watertown PropCo primarily consist of a leased

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property (net real estate), rents receivable, and cash and cash equivalents; its obligations primarily consist of notes payable to a non-VIE consolidated subsidiary of the Company. The assets of Watertown OpCo primarily consist of leasehold interests in a senior housing facility (operating lease), resident fees receivable, and cash and cash equivalents; its obligations primarily consist of lease payments to Watertown PropCo and operating expenses of its senior housing facilities (accounts payable and accrued expenses). Assets generated by the senior housing operations (primarily from senior housing resident rents) of the Watertown structure may only be used to settle its contractual obligations (primarily from the rental costs, operating expenses incurred to manage such facilities and debt costs).

*Life Science JVs.* The Company holds a 99% ownership interest in multiple joint venture entities that own and lease life science assets (the “Life Science JVs”). The Life Science JVs are VIEs as the members share in control of the entities, but substantially all of the activities are performed on behalf of the Company. The Company consolidates the Life Science JVs as the primary beneficiary because it has the ability to control the activities that most significantly impact these VIEs’ economic performance. The assets of the Life Science JVs primarily consist of leased properties (net real estate), rents receivable, and cash and cash equivalents; their obligations primarily consist of debt service payments and capital expenditures for the properties. Assets generated by the Life Science JVs may only be used to settle their contractual obligations (primarily from capital expenditures).

*MSREI MOB JV.* The Company holds a 51% ownership interest in, and is the managing member of, a joint venture entity formed in August 2018 that owns and leases MOBs (the “MSREI JV” - see Note 3). The MSREI JV is a VIE due to the non-managing member lacking substantive participation rights in the management of the joint venture or kick-out rights over the managing member. The Company consolidates the MSREI JV as the primary beneficiary because it has the ability to control the activities that most significantly impact the VIE’s economic performance. The assets of the MSREI JV primarily consist of leased properties (net real estate), rents receivable, and cash and cash equivalents; its obligations primarily consist of capital expenditures for the properties. Assets generated by the MSREI JV may only be used to settle its contractual obligations (primarily from capital expenditures).

*Consolidated Lessee.* The Company leases one senior housing property to a lessee entity under a cash flow lease through which the Company receives monthly rent equal to the residual cash flows of the property. The lessee entity is classified as a VIE as it is a “thinly capitalized” entity. The Company consolidates the lessee entity as it has the ability to control the activities that most significantly impact the economic performance of the lessee entity. The lessee entity’s assets primarily consist of leasehold interests in a senior housing facility (operating leases), resident fees receivable, and cash and cash equivalents; its obligations primarily consist of lease payments to the Company and operating expenses of the senior housing facility (accounts payable and accrued expenses). Assets generated by the senior housing operations (primarily from senior housing resident rents) may only be used to settle its contractual obligations (primarily from the rental costs, operating expenses incurred to manage such facilities and debt costs).

*DownREITs.* The Company holds a controlling ownership interest in and is the managing member of five limited liability companies (“DownREITs”). The Company classifies the DownREITs as VIEs due to the non-managing members lacking substantive participation rights in the management of the DownREITs or kick-out rights over the managing member. The Company consolidates the DownREITs as the primary beneficiary because it has the ability to control the activities that most significantly impact these VIEs’ economic performance. The assets of the DownREITs primarily consist of leased properties (net real estate), rents receivable, and cash and cash equivalents; their obligations primarily consist of debt service payments and capital expenditures for the properties. Assets generated by the DownREITs (primarily from resident rents) may only be used to settle their contractual obligations (primarily from debt service and capital expenditures).

*Other Consolidated Real Estate Partnerships.* The Company holds a controlling ownership interest in and is the general partner (or managing member) of multiple partnerships that own and lease real estate assets (the “Partnerships”). The Company classifies the Partnerships as VIEs due to the limited partners (non-managing members) lacking substantive participation rights in the management of the Partnerships or kick-out rights over the general partner (managing member). The Company consolidates the Partnerships as the primary beneficiary because it has the ability to control the activities that most significantly impact these VIEs’ economic performance. The assets of the Partnerships primarily consist of leased properties (net real estate), rents receivable, and cash and cash equivalents; their obligations primarily consist of debt service payments and capital expenditures for the properties. Assets

generated by the Partnerships (primarily from resident rents) may only be used to settle their contractual obligations (primarily from debt service and capital expenditures).

*Other consolidated VIEs.* The Company made a loan to an entity that entered into a tax credit structure (“Tax Credit Subsidiary”) and a loan to an entity that made an investment in a development joint venture (“Development JV”) both of which are considered VIEs. The Company consolidates the Tax Credit Subsidiary and Development JV as the primary beneficiary because it has the ability to control the activities that most significantly impact the VIEs’ economic performance. The assets and liabilities of the Tax Credit Subsidiary and Development JV substantially consist of a development in progress, notes receivable, prepaid expenses, notes payable, and accounts payable and accrued liabilities generated from their operating activities. Any assets generated by the operating activities of the Tax Credit Subsidiary and Development JV may only be used to settle their contractual obligations.

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*U.K. Bridge Loan.* In 2016, the Company provided a £105 million (\$131 million at closing) bridge loan to MMCG to fund the acquisition of a portfolio of seven care homes in the U.K. MMCG created a special purpose entity to acquire the portfolio and funded it entirely using the Company’s bridge loan. As such, the special purpose entity had historically been identified as a VIE because it was “thinly capitalized.” The Company retained a three year call option to acquire all the shares of the special purpose entity, which it could only exercise upon the occurrence of certain events. During the quarter ended March 31, 2018, the Company concluded that the conditions required to exercise the call option had been met and initiated the call option process to acquire the special purpose entity. In conjunction with initiating the process to legally exercise its call option and the satisfaction of required contingencies, the Company concluded that it was the primary beneficiary of the special purpose entity and therefore, should consolidate the entity. As such, during the quarter ended March 31, 2018, the Company derecognized the previously outstanding loan receivable, recognized the special purpose entity’s assets and liabilities at their respective fair values, and recognized a £29 million (\$41 million) loss on consolidation, net of a tax benefit of £2 million (\$3 million), to account for the difference between the carrying value of the loan receivable and the fair value of net assets and liabilities assumed. The loss on consolidation was recognized within other income (expense), net and the tax benefit was recognized within income tax benefit (expense). The fair value of net assets and liabilities consolidated during the first quarter of 2018 consisted of £81 million (\$114 million) of net real estate, £4 million (\$5 million) of intangible assets, and £9 million (\$13 million) of net deferred tax liabilities.

In June 2018, the Company completed the exercise of the above-mentioned call option and formally acquired full ownership of the special purpose entity. As such, the Company reconsidered whether the special purpose entity was a VIE and concluded that it was no longer “thinly capitalized” as the previously outstanding bridge loan converted to equity at risk and, therefore, was no longer a VIE. The real estate assets held by the special purpose entity were contributed to the U.K. JV formed by the Company in June 2018 (see Note 3).

**NOTE 15. Concentration of Credit Risk**

Concentrations of credit risk arise when one or more tenants, operators or obligors related to the Company’s investments are engaged in similar business activities or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations, including those to the Company, to be similarly affected by changes in economic conditions. The Company regularly monitors various segments of its portfolio to assess potential concentrations of credit risks.

The following tables provide information regarding the Company’s concentrations of credit risk with respect to certain tenants:

| Tenant                   | Percentage of Total Assets |                   |                           |                   |
|--------------------------|----------------------------|-------------------|---------------------------|-------------------|
|                          | Total Company              |                   | Senior Housing Triple-Net |                   |
|                          | March 31, 2019             | December 31, 2018 | March 31, 2019            | December 31, 2018 |
| Brookdale <sup>(1)</sup> | 6                          | 6                 | 31                        | 27                |

  

| Tenant                   | Percentage of Revenues            |                                   |                                   |                                   |
|--------------------------|-----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|
|                          | Total Company                     |                                   | Senior Housing Triple-Net         |                                   |
|                          | Three Months Ended March 31, 2019 | Three Months Ended March 31, 2018 | Three Months Ended March 31, 2019 | Three Months Ended March 31, 2018 |
| Brookdale <sup>(1)</sup> | 4                                 | 7                                 | 32                                | 43                                |

(1) Excludes senior housing facilities operated by Brookdale in the Company’s SHOP segment as discussed below. Percentages of segment and total company revenues include partial-year revenue earned from senior housing triple-net facilities that were sold during 2018.

At both March 31, 2019 and December 31, 2018, Brookdale managed or operated, in the Company’s SHOP

segment, approximately 7% of the Company's real estate investments (based on total assets). Because an operator manages the Company's facilities in exchange for the receipt of a management fee, the Company is not directly exposed to the credit risk of its operators in the same manner or to the same extent as its triple-net tenants. At March 31, 2019, Brookdale provided comprehensive facility management and accounting services with respect to 27 of the Company's consolidated SHOP facilities and 16 SHOP facilities owned by its unconsolidated joint ventures, for which the Company or joint venture pay annual management fees pursuant to long-term management agreements. Most of the management agreements have terms ranging from 10 to 15 years, with three to four 5-year renewal periods. The base management fees are 4.5% to 5.0% of gross revenues (as defined) generated by the RIDEA properties. In addition, there are incentive management fees payable to Brookdale if operating results of the RIDEA properties exceed pre-established EBITDAR (as defined) thresholds.

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To mitigate the credit risk of leasing properties to certain senior housing and post-acute/skilled nursing operators, leases with operators are often combined into portfolios that contain cross-default terms, so that if a tenant of any of the properties in a portfolio defaults on its obligations under its lease, the Company may pursue its remedies under the lease with respect to any of the properties in the portfolio. Certain portfolios also contain terms whereby the net operating profits of the properties are combined for the purpose of securing the funding of rental payments due under each lease.

**NOTE 16. Fair Value Measurements**

Financial assets and liabilities measured at fair value on a recurring basis in the consolidated balance sheets are immaterial at March 31, 2019.

The table below summarizes the carrying amounts and fair values of the Company's financial instruments (in thousands):

|   | March 31, 2019 <sup>(3)</sup> |            | December 31, 2018 <sup>(3)</sup> |            |
|---|-------------------------------|------------|----------------------------------|------------|
|   | Carrying Value                | Fair Value | Carrying Value                   | Fair Value |
| Loans receivable, net <sup>(2)</sup>          | \$86,139                      | \$ 86,139  | \$62,998                         | \$ 62,998  |
| Marketable debt securities <sup>(2)</sup>     | 19,337                        | 19,337     | 19,202                           | 19,202     |
| Bank line of credit <sup>(2)</sup>            | 276,500                       | 276,500    | 80,103                           | 80,103     |
| Senior unsecured notes <sup>(1)</sup>         | 5,260,625                     | 5,484,915  | 5,258,550                        | 5,302,485  |
| Mortgage debt <sup>(2)</sup>                  | 137,525                       | 133,652    | 138,470                          | 136,161    |
| Other debt <sup>(2)</sup>                     | 89,223                        | 89,223     | 90,785                           | 90,785     |
| Interest-rate swap liabilities <sup>(2)</sup> | 1,217                         | 1,217      | 1,310                            | 1,310      |

(1) Level 1: Fair value calculated based on quoted prices in active markets.

Level 2: Fair value based on (i) for marketable debt securities, quoted prices for similar or identical instruments in active or inactive markets, respectively, or (ii) for loans receivable, net, mortgage debt and swaps, calculated utilizing standardized pricing models in which significant inputs or value drivers are observable in active markets. For bank line of credit, term loan and other debt, the carrying values are a reasonable estimate of fair value because the borrowings are primarily based on market interest rates and the Company's credit rating.

(3) During the three months ended March 31, 2019 and year ended December 31, 2018, there were no material transfers of financial assets or liabilities within the fair value hierarchy.

**NOTE 17. Derivative Financial Instruments**

The following table summarizes the Company's outstanding swap contracts at March 31, 2019 (dollars in thousands):

| Date Entered             | Maturity Date | Hedge Designation | Notional | Pay Rate | Receive Rate   | Fair Value <sup>(1)</sup> |
|--------------------------|---------------|-------------------|----------|----------|----------------|---------------------------|
| July 2005 <sup>(2)</sup> | July 2020     | Cash Flow         | \$43,000 | 3.82%    | BMA Swap Index | \$(1,217 )                |

(1) Derivative liabilities are recorded in accounts payable and accrued liabilities on the consolidated balance sheets.

(2) Represents three interest-rate swap contracts, which hedge fluctuations in interest payments on variable-rate secured debt due to overall changes in hedged cash flows.

The Company uses derivative instruments to mitigate the effects of interest rate fluctuations on specific forecasted transactions as well as recognized financial obligations or assets. Utilizing derivative instruments allows the Company to manage the risk of fluctuations in interest rates related to the potential impact these changes could have on future earnings and forecasted cash flows. The Company does not use derivative instruments for speculative or trading purposes. Assuming a one percentage point shift in the underlying interest rate curve, the estimated change in fair value of each of the underlying derivative instruments would not exceed \$1 million.

At March 31, 2019, £55 million of the Company's GBP-denominated borrowings under the Facility are designated as a hedge of a portion of the Company's net investments in GBP-functional currency unconsolidated subsidiaries to mitigate its exposure to fluctuations in the GBP to USD exchange rate. For instruments that are designated and qualify as net investment hedges, the variability in the foreign currency to USD exchange rate of the instrument is recorded as part of the cumulative translation adjustment component of accumulated other comprehensive income (loss).

Accordingly, the remeasurement value of the designated £55 million GBP-denominated borrowings due primarily to

fluctuations in the GBP to USD exchange rate are reported in accumulated

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other comprehensive income (loss) as the hedging relationship is considered to be effective. The balance in accumulated other comprehensive income (loss) will be reclassified to earnings when the Company sells its remaining investment in the U.K.

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**Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations**

*All references in this report to “HCP,” “we,” “us” or “our” mean HCP, Inc., together with its consolidated subsidiaries. Unless the context suggests otherwise, references to “HCP, Inc.” mean the parent company without its subsidiaries.*

**Cautionary Language Regarding Forward-Looking Statements**

Statements in this Quarterly Report on Form 10-Q that are not historical factual statements are “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Forward-looking statements include, among other things, statements regarding our and our officers’ intent, belief or expectation as identified by the use of words such as “may,” “will,” “project,” “expect,” “believe,” “intend,” “anticipate,” “seek,” “forecast,” “plan,” “potential,” “estimate,” “could” other comparable and derivative terms or the negatives thereof. Forward-looking statements reflect our current expectations and views about future events and are subject to risks and uncertainties that could significantly affect our future financial condition and results of operations. While forward-looking statements reflect our good faith belief and assumptions we believe to be reasonable based upon current information, we can give no assurance that our expectations or forecasts will be attained. As more fully set forth under Part I, Item 1A. “Risk Factors” in our Annual Report on Form 10-K for the fiscal year ended December 31, 2018, risks and uncertainties that may cause our actual results to differ materially from the expectations contained in the forward-looking statements include, among other things:

- our reliance on a concentration of a small number of tenants and operators for a significant percentage of our revenues and net operating income;
  - the financial condition of our existing and future tenants, operators and borrowers, including potential bankruptcies and downturns in their businesses, and their legal and regulatory proceedings, which results in uncertainties regarding our ability to continue to realize the full benefit of such tenants’ and operators’ leases and borrowers’ loans;
- the ability of our existing and future tenants, operators and borrowers to conduct their respective businesses in a manner sufficient to maintain or increase their revenues and manage their expenses in order to generate sufficient income to make rent and loan payments to us and our ability to recover investments made, if applicable, in their operations;
- our concentration in the healthcare property sector, particularly in senior housing, life sciences and medical office buildings, which makes our profitability more vulnerable to a downturn in a specific sector than if we were investing in multiple industries;
- operational risks associated with third party management contracts, including the additional regulation and liabilities of our RIDEA lease structures;
- the effect on us and our tenants and operators of legislation, executive orders and other legal requirements, including compliance with the Americans with Disabilities Act, fire, safety and health regulations, environmental laws, the Affordable Care Act, licensure, certification and inspection requirements, and laws addressing entitlement programs and related services, including Medicare and Medicaid, which may result in future reductions in reimbursements or fines for noncompliance;
- our ability to identify replacement tenants and operators and the potential renovation costs and regulatory approvals associated therewith;
- the risks associated with property development and redevelopment, including costs above original estimates, project delays and lower occupancy rates and rents than expected;
- the potential impact of uninsured or underinsured losses;
- the risks associated with our investments in joint ventures and unconsolidated entities, including our lack of sole decision making authority and our reliance on our partners’ financial condition and continued cooperation;
- competition for the acquisition and financing of suitable healthcare properties as well as competition for tenants and operators, including with respect to new leases and mortgages and the renewal or rollover of existing leases;
- our ability to achieve the benefits of acquisitions or other investments within expected time frames or at all, or within expected cost projections;

the potential impact on us and our tenants, operators and borrowers from current and future litigation matters, including the possibility of larger than expected litigation costs, adverse results and related developments; changes in federal, state or local laws and regulations, including those affecting the healthcare industry that affect our costs of compliance or increase the costs, or otherwise affect the operations, of our tenants and operators;

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our ability to foreclose on collateral securing our real estate-related loans;  
volatility or uncertainty in the capital markets, the availability and cost of capital as impacted by interest rates,  
changes in our credit ratings, and the value of our common stock, and other conditions that may adversely impact our  
ability to fund our obligations or consummate transactions, or reduce the earnings from potential transactions;  
changes in global, national and local economic and other conditions, including currency exchange rates;  
our ability to manage our indebtedness level and changes in the terms of such indebtedness;  
competition for skilled management and other key personnel;  
our reliance on information technology systems and the potential impact of system failures, disruptions or breaches;  
and  
our ability to maintain our qualification as a real estate investment trust (“REIT”).

Except as required by law, we do not undertake, and hereby disclaim, any obligation to update any forward-looking statements, which speak only as of the date on which they are made.

The information set forth in this Item 2 is intended to provide readers with an understanding of our financial condition, changes in financial condition and results of operations. We will discuss and provide our analysis in the following order:

Executive Summary

2019 Transaction Overview

Dividends

Results of Operations

Liquidity and Capital Resources

Off-Balance Sheet Arrangements

Non-GAAP Financial Measures Reconciliations

Critical Accounting Policies

Recent Accounting Pronouncements

**Executive Summary**

HCP, Inc., a Standard & Poor’s (“S&P”) 500 company, invests primarily in real estate serving the healthcare industry in the United States. We are a Maryland corporation organized in 1985 and qualify as a self-administered real estate investment trust (“REIT”). We acquire, develop, lease, own and manage healthcare real estate. At March 31, 2019, our portfolio of investments, including properties in our unconsolidated joint ventures (“JVs”), consisted of interests in 734 properties.

We invest and manage our real estate portfolio for the long-term to maximize the benefit to our stockholders and support the growth of our dividends. The core elements of our strategy are to: (i) acquire, develop, lease, own and manage a diversified portfolio of quality healthcare properties across multiple geographic locations and business segments, including senior housing, life science, and medical office, among others; (ii) maintain an investment grade balance sheet with adequate liquidity and long-term fixed rate debt financing with staggered maturities in order to support the longer-term nature of our investments, while reducing our exposure to interest rate volatility and refinancing risk at any point in the interest rate or credit cycles; (iii) align ourselves with leading healthcare companies, operators and service providers which, over the long-term, should result in higher relative rental rates, net operating cash flows and appreciation of property values; and (iv) pursue operational excellence to maximize the value of our investments.

We believe our real estate portfolio holds the potential for increased future cash flows as it is well-maintained and in desirable locations. Our strategy for maximizing the benefits from these opportunities is to: (i) work with new or existing tenants and operators to address their space and capital needs; and (ii) provide high-quality property management services in order to motivate tenants to renew, expand or relocate into our properties.

The delivery of healthcare services requires real estate and, as a result, tenants and operators depend on real estate, in part, to maintain and grow their businesses. We believe that the healthcare real estate market provides investment opportunities due to the: (i) compelling long-term demographics driving the demand for healthcare services; (ii) specialized nature of healthcare real estate investing; and (iii) ongoing consolidation of the fragmented healthcare real estate sector.



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We primarily invest in healthcare real estate through long-term ownership, acquisitions and development. We both wholly-own investments and co-invest through joint ventures with institutional or development investors. When consistent with our investment strategies, we may occasionally provide real estate secured financing to healthcare real estate developers or owners. Additionally, we may opportunistically acquire other real estate entities or their assets. We monitor, but do not limit, our investments based on the percentage of our total assets that may be invested in any one property type, investment vehicle or geographic location, the number of properties that may be leased to a single tenant or operator, or loans that may be made to a single borrower. In allocating capital, we target opportunities with the most attractive risk/reward profile for our portfolio as a whole. We may take additional measures to mitigate risk, including diversifying our investments (by sector, geography, tenant or operator), structuring transactions as master leases, requiring tenant or operator insurance and indemnifications, and obtaining credit enhancements in the form of guarantees, letters of credit or security deposits.

Our REIT qualification requires us to distribute at least 90% of our REIT taxable income (excluding net capital gains); therefore, we do not retain a significant amount of capital. As a result, we regularly access the public equity and debt markets to raise the funds necessary to finance acquisitions and debt investments, develop and redevelop properties, and refinance maturing debt.

We maintain a disciplined balance sheet by actively managing our debt to equity levels and maintaining multiple sources of liquidity. Our debt obligations are primarily long-term fixed rate with staggered maturities.

We finance our investments based on our evaluation of available sources of funding. For short-term purposes, we may utilize our revolving line of credit facility, arrange for other short-term borrowings from banks or other sources, or issue equity securities pursuant to our at-the-market equity offering program. We arrange for longer-term financing by offering debt and equity securities, placing mortgage debt and obtaining capital from institutional lenders and joint venture partners.

**2019 Transaction Overview*****Discovery Portfolio Acquisition***

In April 2019, we acquired a portfolio of nine senior housing properties, with a total of 1,242 units, for \$445 million. The properties are located across Florida, Georgia and Texas and will be operated by Discovery Senior Living, LLC (“Discovery”).

***Oakmont Portfolio Acquisition and Transitions***

On May 1, 2019, we acquired three newly-built, senior housing communities for \$113 million. The portfolio will be operated by Oakmont Senior Living LLC (“Oakmont”) and includes 132 assisted living units and 68 memory care units with an average occupancy of 96%. Additionally, the Company transitioned four senior housing triple-net properties to RIDEA structures with Oakmont continuing as the operator.

***Other Real Estate Transactions***

In January and February 2019, we acquired a life science facility for \$71 million and development rights at an adjacent undeveloped land parcel for consideration of up to \$27 million. The existing facility and land parcel are located in Cambridge, Massachusetts.

During the first quarter of 2019, the Company transitioned 18 senior housing triple-net assets, including a 14-property direct financing lease (“DFL”) portfolio, to a RIDEA structure, with Sunrise Senior Living, LLC (“Sunrise”) as the operator. The Company expects to transition an additional 17-property DFL portfolio to a RIDEA structure with Sunrise later in 2019.

During the quarter ended March 31, 2019, we sold nine senior housing operating portfolio (“SHOP”) assets for \$68 million, two senior housing triple-net assets for \$26 million and an undeveloped life science land parcel for \$35 million.

In 2018, we entered into definitive agreements to acquire two life science buildings in South San Francisco, California, adjacent to The Shore at Sierra Point development, for \$245 million. We expect to close the transaction during the second quarter of 2019.

***Financing Activities***

In February 2019, we terminated our previous at-the-market equity program established in February 2018 (the “2018 ATM Program”) and established a new ATM Program (the “2019 ATM Program”) pursuant to which shares of common

stock having an aggregate gross sales price of up to \$1.0 billion may be sold (i) by the Company through a consortium of banks acting as sales agents or directly to the banks acting as principals, or (ii) by a consortium of banks acting as forward sellers on behalf of any forward purchasers pursuant to a forward sale agreement.

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During the three months ended March 31, 2019, we utilized the forward provisions under the 2019 ATM Program to allow for the sale of up to an aggregate of 3.6 million shares of our common stock at an initial weighted average net price of \$31.19 per share, after commissions. Each forward sale has a one year term.

Subsequent to March 31, 2019, we utilized the forward provisions under the 2019 ATM Program to allow for the sale of up to an additional 1.5 million shares of our common stock at an initial weighted average net price of \$30.63 per share, after commissions.

**Development Activities**

As part of the previously-announced development program with HCA Healthcare, during the first quarter of 2019, we signed definitive agreements to develop three additional medical office buildings (“MOBs”), two of which are on-campus, with an aggregate estimated cost of \$70 million. Construction on these projects is expected to commence in the second quarter of 2019.

**Dividends**

The following table summarizes our common stock cash dividends declared in 2019:

| Declaration Date | Record Date | Amount<br>Per Share | Dividend<br>Payment Date |
|------------------|-------------|---------------------|--------------------------|
| January 30       | February 19 | \$ 0.37             | February 28              |
| April 25         | May 6       | 0.37                | May 21                   |

**Results of Operations**

We evaluate our business and allocate resources among our reportable business segments: (i) senior housing triple-net, (ii) SHOP, (iii) life science and (iv) medical office. Under the life science and medical office segments, we invest through the acquisition and development of life science facilities and medical office buildings, which generally require a greater level of property management. Our senior housing facilities are managed utilizing triple-net leases and RIDEA structures. We have other non-reportable segments that are comprised primarily of our debt investments, hospital properties, unconsolidated joint ventures and United Kingdom (“U.K.”) investments. We evaluate performance based upon: (i) property net operating income from continuing operations (“NOI”) and (ii) Adjusted NOI (cash NOI) in each segment. The accounting policies of the segments are the same as those described in the summary of significant accounting policies in Note 2 of our Annual Report on Form 10-K for the year ended December 31, 2018 filed with the United States (“U.S.”) Securities and Exchange Commission (“SEC”), as updated by Note 2 herein.

**Non-GAAP Financial Measures***Net Operating Income*

NOI and Adjusted NOI are non-U.S. generally accepted accounting principles (“GAAP”) supplemental financial measures used to evaluate the operating performance of real estate. NOI is defined as real estate revenues (inclusive of rental and related revenues, resident fees and services, and income from direct financing leases), less property level operating expenses (which exclude transition costs); NOI excludes all other financial statement amounts included in net income (loss) as presented in Note 11 to the Consolidated Financial Statements. Management believes NOI provides relevant and useful information because it reflects only income and operating expense items that are incurred at the property level and presents them on an unlevered basis. Adjusted NOI is calculated as NOI after eliminating the effects of straight-line rents, DFL non-cash interest, amortization of market lease intangibles, termination fees, actuarial reserves for insurance claims that have been incurred but not reported, and the impact of deferred community fee income and expense. Adjusted NOI is oftentimes referred to as “Cash NOI.” NOI and Adjusted NOI exclude our share of income (loss) generated by unconsolidated joint ventures, which is recognized in equity income (loss) from unconsolidated joint ventures in the consolidated statements of operations. We use NOI and Adjusted NOI to make decisions about resource allocations, to assess and compare property level performance, and to evaluate our same property portfolio (“SPP”), as described below. We believe that net income (loss) is the most directly comparable GAAP measure to NOI and Adjusted NOI. NOI and Adjusted NOI should not be viewed as alternative measures of operating performance to net income (loss) as defined by GAAP since they do not reflect various excluded items. Further, our definitions of NOI and Adjusted NOI may not be comparable to the definitions used by other REITs or real estate companies, as they may use different methodologies for calculating NOI and Adjusted NOI. For a reconciliation of NOI and Adjusted NOI to net income (loss) by segment, refer to Note 11 to the Consolidated Financial Statements.



Operating expenses generally relate to leased medical office and life science properties and SHOP facilities. We generally recover all or a portion of our leased medical office and life science property expenses through tenant recoveries. We present expenses as operating or general and administrative based on the underlying nature of the expense.

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SPP NOI and Adjusted (Cash) NOI information allows us to evaluate the performance of our property portfolio under a consistent population by eliminating changes in the composition of our consolidated portfolio of properties. SPP NOI excludes certain non-property specific operating expenses that are allocated to each operating segment on a consolidated basis.

Properties are included in SPP once they are stabilized for the full period in both comparison periods. Newly acquired operating assets are generally considered stabilized at the earlier of lease-up (typically when the tenant(s) control(s) the physical use of at least 80% of the space) or 12 months from the acquisition date. Newly completed developments and redevelopments are considered stabilized at the earlier of lease-up or 24 months from the date the property is placed in service. Properties that experience a change in reporting structure, such as a transition from a triple-net lease to a RIDEA reporting structure, are considered stabilized after 12 months in operations under a consistent reporting structure. A property is removed from SPP when it is classified as held for sale, sold, placed into redevelopment, experiences a casualty event that significantly impacts operations or changes its reporting structure (such as triple-net to SHOP). For a reconciliation of SPP to total portfolio Adjusted NOI and other relevant disclosures by segment, refer to our Segment Analysis below.

*Funds From Operations (“FFO”)*

FFO encompasses NAREIT FFO and FFO as adjusted, each of which is described in detail below. We believe FFO applicable to common shares, diluted FFO applicable to common shares, and diluted FFO per common share are important supplemental non-GAAP measures of operating performance for a REIT. Because the historical cost accounting convention used for real estate assets utilizes straight-line depreciation (except on land), such accounting presentation implies that the value of real estate assets diminishes predictably over time. Since real estate values instead have historically risen and fallen with market conditions, presentations of operating results for a REIT that use historical cost accounting for depreciation could be less informative. The term FFO was designed by the REIT industry to address this issue.

*NAREIT FFO.* FFO, as defined by the National Association of Real Estate Investment Trusts (“NAREIT”), is net income (loss) applicable to common shares (computed in accordance with GAAP), excluding gains or losses from sales of depreciable property, including any current and deferred taxes directly associated with sales of depreciable property, impairments of, or related to, depreciable real estate, plus real estate and other real estate-related depreciation and amortization, and adjustments to compute our share of NAREIT FFO and FFO as adjusted (see below) from joint ventures. Adjustments for joint ventures are calculated to reflect our pro-rata share of both our consolidated and unconsolidated joint ventures. We reflect our share of NAREIT FFO for unconsolidated joint ventures by applying our actual ownership percentage for the period to the applicable reconciling items on an entity by entity basis. For consolidated joint ventures in which we do not own 100%, we reflect our share of the equity by adjusting our NAREIT FFO to remove the third party ownership share of the applicable reconciling items based on actual ownership percentage for the applicable periods. Our pro-rata share information is prepared on a basis consistent with the comparable consolidated amounts, is intended to reflect our proportionate economic interest in the operating results of properties in our portfolio and is calculated by applying our actual ownership percentage for the period. We do not control the unconsolidated joint ventures, and the pro-rata presentations of reconciling items included in NAREIT FFO do not represent our legal claim to such items. The joint venture members or partners are entitled to profit or loss allocations and distributions of cash flows according to the joint venture agreements, which provide for such allocations generally according to their invested capital.

The presentation of pro-rata information has limitations, which include, but are not limited to, the following: (i) the amounts shown on the individual line items were derived by applying our overall economic ownership interest percentage determined when applying the equity method of accounting and do not necessarily represent our legal claim to the assets and liabilities, or the revenues and expenses and (ii) other companies in our industry may calculate their pro-rata interest differently, limiting the usefulness as a comparative measure. Because of these limitations, the pro-rata financial information should not be considered independently or as a substitute for our financial statements as reported under GAAP. We compensate for these limitations by relying primarily on our GAAP financial statements, using the pro-rata financial information as a supplement.

NAREIT FFO does not represent cash generated from operating activities in accordance with GAAP, is not necessarily indicative of cash available to fund cash needs and should not be considered an alternative to net income (loss). We compute NAREIT FFO in accordance with the current NAREIT definition; however, other REITs may report NAREIT FFO differently or have a different interpretation of the current NAREIT definition from ours. *FFO as adjusted.* In addition, we present NAREIT FFO on an adjusted basis before the impact of non-comparable items including, but not limited to, transaction-related items, impairments (recoveries) of non-depreciable assets, losses (gains) from the sale of non-depreciable assets, severance and related charges, prepayment costs (benefits) associated with early retirement or payment of debt, litigation costs (recoveries), casualty-related charges (recoveries), foreign currency remeasurement losses (gains) and changes in tax legislation (“FFO as adjusted”). Transaction-related items include transaction expenses and gains/charges incurred as a result of mergers and acquisitions and lease amendment or termination activities. Prepayment costs (benefits) associated with early retirement of debt include the write-off of unamortized deferred financing fees, or additional costs, expenses, discounts, make-whole payments, penalties or premiums incurred as a result of early retirement or payment of debt. Management believes

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that FFO as adjusted provides a meaningful supplemental measurement of our FFO run-rate and is frequently used by analysts, investors and other interested parties in the evaluation of our performance as a REIT. At the same time that NAREIT created and defined its FFO measure for the REIT industry, it also recognized that “management of each of its member companies has the responsibility and authority to publish financial information that it regards as useful to the financial community.” We believe stockholders, potential investors and financial analysts who review our operating performance are best served by an FFO run-rate earnings measure that includes certain other adjustments to net income (loss), in addition to adjustments made to arrive at the NAREIT defined measure of FFO. FFO as adjusted is used by management in analyzing our business and the performance of our properties, and we believe it is important that stockholders, potential investors and financial analysts understand this measure used by management. We use FFO as adjusted to: (i) evaluate our performance in comparison with expected results and results of previous periods, relative to resource allocation decisions, (ii) evaluate the performance of our management, (iii) budget and forecast future results to assist in the allocation of resources, (iv) assess our performance as compared with similar real estate companies and the industry in general and (v) evaluate how a specific potential investment will impact our future results. Other REITs or real estate companies may use different methodologies for calculating an adjusted FFO measure, and accordingly, our FFO as adjusted may not be comparable to those reported by other REITs. For a reconciliation of net income (loss) to NAREIT FFO and FFO as adjusted and other relevant disclosure, refer to “Non-GAAP Financial Measures Reconciliations” below.

*Funds Available for Distribution (“FAD”)*

FAD is defined as FFO as adjusted after excluding the impact of the following: (i) amortization of deferred compensation expense, (ii) amortization of deferred financing costs, net, (iii) straight-line rents, (iv) deferred income taxes, (v) amortization of acquired market lease intangibles, net, (vi) non-cash interest related to DFLs and lease incentive amortization (reduction of straight-line rents), (vii) actuarial reserves for insurance claims that have been incurred but not reported, and (viii) deferred revenues, excluding amounts amortized into rental income that are associated with tenant funded improvements owned/recognized by us and up-front cash payments made by tenants to reduce their contractual rents. Also, FAD: (i) is computed after deducting recurring capital expenditures, including second generation leasing costs and second generation tenant and capital improvements, and (ii) includes lease restructure payments and adjustments to compute our share of FAD from our unconsolidated joint ventures and those related to CCRC non-refundable entrance fees. Certain prior period amounts in the “Non-GAAP Financial Measures Reconciliation” below for FAD have been reclassified to conform to the current period presentation. More specifically, recurring capital expenditures, including second generation leasing costs and second generation tenant and capital improvements (“FAD capital expenditures”) excludes our share from unconsolidated joint ventures (reported in “other FAD adjustments”). Adjustments for joint ventures are calculated to reflect our pro-rata share of both our consolidated and unconsolidated joint ventures. We reflect our share of FAD for unconsolidated joint ventures by applying our actual ownership percentage for the period to the applicable reconciling items on an entity by entity basis. We reflect our share for consolidated joint ventures in which we do not own 100% of the equity by adjusting our FAD to remove the third party ownership share of the applicable reconciling items based on actual ownership percentage for the applicable periods (reported in “other FAD adjustments”). See FFO for further disclosure regarding our use of pro-rata share information and its limitations. Other REITs or real estate companies may use different methodologies for calculating FAD, and accordingly, our FAD may not be comparable to those reported by other REITs. Although our FAD computation may not be comparable to that of other REITs, management believes FAD provides a meaningful supplemental measure of our performance and is frequently used by analysts, investors, and other interested parties in the evaluation of our performance as a REIT. We believe FAD is an alternative run-rate earnings measure that improves the understanding of our operating results among investors and makes comparisons with: (i) expected results, (ii) results of previous periods and (iii) results among REITs more meaningful. FAD does not represent cash generated from operating activities determined in accordance with GAAP and is not necessarily indicative of cash available to fund cash needs as it excludes the following items which generally flow through our cash flows from operating activities: (i) adjustments for changes in working capital or the actual timing of the payment of income or expense items that are accrued in the period, (ii) transaction-related costs, (iii) litigation settlement expenses, (iv) severance-related expenses and (v) actual cash receipts from interest income recognized on loans receivable (in

contrast to our FAD adjustment to exclude non-cash interest and depreciation related to our investments in direct financing leases). Furthermore, FAD is adjusted for recurring capital expenditures, which are generally not considered when determining cash flows from operations or liquidity. FAD is a non-GAAP supplemental financial measure and should not be considered as an alternative to net income (loss) determined in accordance with GAAP. For a reconciliation of net income (loss) to FAD and other relevant disclosure, refer to “Non-GAAP Financial Measures Reconciliations” below.

Table of Contents**Comparison of the Three Months Ended March 31, 2019 to the Three Months Ended March 31, 2018  
Overview***Three Months Ended March 31, 2019 and 2018*

The following table summarizes results for the three months ended March 31, 2019 and 2018 (dollars in thousands):

|   | Three Months<br>Ended March 31, |          |           |
|---|---------------------------------|----------|-----------|
|   | 2019                            | 2018     | Change    |
| Net income (loss) applicable to common shares | \$61,029                        | \$39,841 | \$21,188  |
| NAREIT FFO                                    | 206,036                         | 219,434  | (13,398 ) |
| FFO as adjusted                               | 212,025                         | 227,352  | (15,327 ) |
| FAD   | 191,471                         | 201,736  | (10,265 ) |

Net income applicable to common shares ("EPS") increased primarily as a result of the following:

- a one-time loss on consolidation of seven care homes in the U.K. during the first quarter of 2018;
- a reduction in interest expense as a result of debt repayments during 2018 and a lower average balance under our revolving credit facility;
- decreased depreciation and amortization expense as a result of dispositions of real estate throughout 2018 and 2019 partially offset by: (i) assets acquired during 2018 and 2019 and (ii) development and redevelopment projects placed into service during 2018;
- increased NOI from: (i) 2018 and 2019 acquisitions, (ii) development and redevelopment projects placed in service during 2018, and (iii) new leasing activity during 2018 and 2019; and
- a reduction in severance and related charges.

The increase in EPS was partially offset by:

- a reduction in net gain on sales of real estate during the first quarter of 2019 compared to the first quarter of 2018;
- a reduction in NOI in our SHOP segment, primarily as a result of occupancy declines and higher labor costs;
- impairment charges related to two MOBs during the first quarter of 2019; and
- a reduction in income as a result of: (i) asset sales during 2018 and 2019 and (ii) selling interests into the U.K. JV and MSREI JV during 2018 (see Note 3 to the Consolidated Financial Statements).

NAREIT FFO decreased primarily as a result of the aforementioned events impacting EPS, except for the following, which are excluded from NAREIT FFO:

- depreciation and amortization expense;
- impairments of MOBs;
- gain on sales of real estate, including related tax impacts; and
- loss on consolidation of real estate.

FFO as adjusted decreased primarily as a result of the aforementioned events impacting NAREIT FFO, except for the following, which is excluded from FFO as adjusted:

- severance and related charges.

FAD decreased primarily as a result of the aforementioned events impacting FFO as adjusted, except for the impact of straight-line rents, which is excluded from FAD.

*Segment Analysis*

The tables below provide selected operating information for our SPP and total property portfolio for each of our business segments. Our SPP for the three months ended March 31, 2019 consists of 522 properties representing properties acquired or placed in service and stabilized on or prior to January 1, 2018 and that remained in operation under a consistent reporting structure through March 31, 2019. Our total property portfolio consists of 635 and 749 properties at March 31, 2019 and 2018, respectively.

Table of Contents**Senior Housing Triple-Net**

The following table summarizes results at and for the three months ended March 31, 2019 and 2018 (dollars in thousands, except per unit data):

|   | <b>SPP</b>                          |             |               | <b>Total Portfolio<sup>(1)</sup></b> |             |               |
|---|-------------------------------------|-------------|---------------|--------------------------------------|-------------|---------------|
|   | <b>Three Months Ended March 31,</b> |             |               | <b>Three Months Ended March 31,</b>  |             |               |
|   | <b>2019</b>                         | <b>2018</b> | <b>Change</b> | <b>2019</b>                          | <b>2018</b> | <b>Change</b> |
| Real estate revenues <sup>(2)</sup>     | \$56,049                            | \$55,560    | \$489         | \$58,892                             | \$74,289    | \$(15,397)    |
| Operating expenses                      | (88 )                               | (92 )       | 4             | (993 )                               | (1,045 )    | 52            |
| NOI                                     | 55,961                              | 55,468      | 493           | 57,899                               | 73,244      | (15,345 )     |
| Adjustments to NOI                      | (1,839 )                            | (2,633 )    | 794           | 564                                  | (1,865 )    | 2,429         |
| Adjusted NOI                            | \$54,122                            | \$52,835    | \$1,287       | 58,463                               | 71,379      | (12,916 )     |
| Non-SPP adjusted NOI                    |                                     |             |               | (4,341 )                             | (18,544 )   | 14,203        |
| SPP adjusted NOI                        |                                     |             |               | \$54,122                             | \$52,835    | \$1,287       |
| Adjusted NOI % change                   |                                     |             | 2.4 %         |                                      |             |               |
| Property count <sup>(3)</sup>           | 126                                 | 126         |               | 126                                  | 181         |               |
| Average capacity (units) <sup>(4)</sup> | 12,940                              | 12,943      |               | 14,642                               | 18,331      |               |
| Average annual rent per unit            | \$16,757                            | \$16,357    |               | \$16,243                             | \$15,803    |               |

(1) Total Portfolio includes results of operations from disposed properties and properties that transitioned segments through the disposition or transition date.

(2) Represents rental and related revenues and income from DFLs.

(3) From our 2018 presentation of SPP, we removed 13 senior housing triple-net properties that were sold and 40 senior housing triple-net properties that were transitioned to SHOP.

(4) Represents average capacity as reported by the respective tenants or operators for the three-month period.

SPP NOI and Adjusted NOI increased primarily as a result of annual rent escalations.

Total Portfolio NOI and Adjusted NOI decreased primarily as a result of the following Non-SPP impacts:

• the transfer of 22 and 18 senior housing triple-net facilities to our SHOP segment during 2018 and 2019, respectively, and

• senior housing triple-net facilities sold during 2018 and 2019.

The decrease in Total Portfolio NOI and Adjusted NOI is partially offset by the aforementioned increases to SPP.

Table of Contents**Senior Housing Operating Portfolio**

The following table summarizes results at and for the three months ended March 31, 2019 and 2018 (dollars in thousands, except per unit data):

|   | <b>SPP</b>                          |             |               | <b>Total Portfolio<sup>(1)</sup></b> |             |               |
|---|-------------------------------------|-------------|---------------|--------------------------------------|-------------|---------------|
|   | <b>Three Months Ended March 31,</b> |             |               | <b>Three Months Ended March 31,</b>  |             |               |
|   | <b>2019</b>                         | <b>2018</b> | <b>Change</b> | <b>2019</b>                          | <b>2018</b> | <b>Change</b> |
| Resident fees and services              | \$70,165                            | \$70,838    | \$(673 )      | \$126,181                            | \$144,670   | \$(18,489)    |
| Operating expenses                      | (48,690 )                           | (47,524 )   | (1,166 )      | (96,948 )                            | (101,746 )  | 4,798         |
| NOI                                     | 21,475                              | 23,314      | (1,839 )      | 29,233                               | 42,924      | (13,691 )     |
| Adjustments to NOI                      | 169                                 | 123         | 46            | 1,152                                | (1,607 )    | 2,759         |
| Adjusted NOI                            | \$21,644                            | \$23,437    | \$(1,793)     | 30,385                               | 41,317      | (10,932 )     |
| Non-SPP adjusted NOI                    |                                     |             |               | (8,741 )                             | (17,880 )   | 9,139         |
| SPP adjusted NOI                        |                                     |             |               | \$21,644                             | \$23,437    | \$(1,793 )    |
| Adjusted NOI % change                   |                                     |             | (7.7 )%       |                                      |             |               |
| Property count <sup>(2)</sup>           | 50                                  | 50          |               | 102                                  | 100         |               |
| Average capacity (units) <sup>(3)</sup> | 6,405                               | 6,404       |               | 11,271                               | 13,597      |               |
| Average annual rent per unit            | \$44,056                            | \$43,840    |               | \$45,123                             | \$41,867    |               |

(1) Total Portfolio includes results of operations from disposed properties and properties that transitioned segments through the disposition or transition date.

(2) From our 2018 presentation of SPP, we removed 13 SHOP properties that were sold and 10 SHOP properties that were placed in redevelopment.

(3) Represents average capacity as reported by the respective tenants or operators for the three-month period.

**SPP NOI and Adjusted NOI decreased primarily as a result of the following:**

- occupancy declines and higher labor costs; partially offset by
- increased rates for resident fees.

Total Portfolio NOI and Adjusted NOI decreased primarily as a result of the aforementioned impacts to SPP and the following Non-SPP impacts:

- decreased NOI from assets sold in 2018 and 2019; partially offset by
- increased NOI from the transfer of 22 and 18 senior housing triple-net assets to our SHOP segment during 2018 and 2019, respectively.



Table of Contents**Life Science**

The following table summarizes results at and for the three months ended March 31, 2019 and 2018 (dollars and square feet in thousands, except per square foot data):

|  | <b>SPP</b>                          |             |               | <b>Total Portfolio</b>              |             |               |
|--|-------------------------------------|-------------|---------------|-------------------------------------|-------------|---------------|
|  | <b>Three Months Ended March 31,</b> |             |               | <b>Three Months Ended March 31,</b> |             |               |
|  | <b>2019</b>                         | <b>2018</b> | <b>Change</b> | <b>2019</b>                         | <b>2018</b> | <b>Change</b> |
| Rental and related revenues                                      | \$73,340                            | \$69,072    | \$4,268       | \$94,473                            | \$99,622    | \$(5,149)     |
| Operating expenses   | (16,465 )                           | (15,345 )   | (1,120 )      | (21,992 )                           | (21,809 )   | (183 )        |
| NOI  | 56,875                              | 53,727      | 3,148         | 72,481                              | 77,813      | (5,332 )      |
| Adjustments to NOI   | (446 )                              | (765 )      | 319           | (2,478 )                            | (3,751 )    | 1,273         |
| Adjusted NOI   | \$56,429                            | \$52,962    | \$3,467       | 70,003                              | 74,062      | (4,059 )      |
| Non-SPP adjusted NOI   |                                     |             |               | (13,574 )                           | (21,100 )   | 7,526         |
| SPP adjusted NOI   |                                     |             |               | \$56,429                            | \$52,962    | \$3,467       |
| Adjusted NOI % change  |                                     |             | 6.5 %         |                                     |             |               |
| Property count <sup>(1)</sup>                                    | 97                                  | 97          |               | 125                                 | 131         |               |
| Average occupancy  | 96.1 %                              | 93.9 %      |               | 96.6 %                              | 93.7 %      |               |
| Average occupied square feet                                     | 5,645                               | 5,515       |               | 6,655                               | 7,289       |               |
| Average annual total revenues per occupied square foot           | \$52                                | \$50        |               | \$55                                | \$53        |               |
| Average annual base rent per occupied square foot <sup>(2)</sup> | \$42                                | \$40        |               | \$44                                | \$43        |               |

(1) From our 2018 presentation of SPP, we removed 12 life science facilities that were sold and three life science facilities that were placed in redevelopment.

(2) Base rent does not include tenant recoveries, additional rents in excess of floors and non-cash revenue adjustments (i.e., straight-line rents, amortization of market lease intangibles, DFL non-cash interest and deferred revenues).

SPP NOI and Adjusted NOI increased primarily as a result of the following:

- increased occupancy and new leasing activity; and
- specific to adjusted NOI, annual rent escalations.

Total Portfolio NOI and Adjusted NOI decreased primarily as a result of the aforementioned increases to SPP and the following Non-SPP impacts:

- decreased NOI from: (i) facilities sales in 2018 and (ii) the placement of facilities into redevelopment in 2018 and 2019; partially offset by
- increased NOI from: (i) increased occupancy in developments and redevelopments placed into service in 2018 and 2019, and (ii) acquisitions in 2018 and 2019.

Table of Contents**Medical Office**

The following table summarizes results at and for the three months ended March 31, 2019 and 2018 (dollars and square feet in thousands, except per square foot data):

|  | <b>SPP</b>                          |             |               | <b>Total Portfolio</b>              |             |               |
|--|-------------------------------------|-------------|---------------|-------------------------------------|-------------|---------------|
|  | <b>Three Months Ended March 31,</b> |             |               | <b>Three Months Ended March 31,</b> |             |               |
|  | <b>2019</b>                         | <b>2018</b> | <b>Change</b> | <b>2019</b>                         | <b>2018</b> | <b>Change</b> |
| Rental and related revenues                                      | \$ 121,976                          | \$ 118,557  | \$ 3,419      | \$ 142,195                          | \$ 133,220  | \$ 8,975      |
| Operating expenses   | (40,919 )                           | (40,288 )   | (631 )        | (48,987 )                           | (47,878 )   | (1,109 )      |
| NOI  | 81,057                              | 78,269      | 2,788         | 93,208                              | 85,342      | 7,866         |
| Adjustments to NOI   | (1,258 )                            | (1,703 )    | 445           | (1,771 )                            | (1,932 )    | 161           |
| Adjusted NOI   | \$ 79,799                           | \$ 76,566   | \$ 3,233      | 91,437                              | 83,410      | 8,027         |
| Non-SPP adjusted NOI   |                                     |             |               | (11,638 )                           | (6,844 )    | (4,794 )      |
| SPP adjusted NOI   |                                     |             |               | \$ 79,799                           | \$ 76,566   | \$ 3,233      |
| Adjusted NOI % change  |                                     |             | 4.2 %         |                                     |             |               |
| Property count <sup>(1)</sup>                                    | 236                                 | 236         |               | 269                                 | 256         |               |
| Average occupancy  | 92.5 %                              | 93.1 %      |               | 92.1 %                              | 92.5 %      |               |
| Average occupied square feet                                     | 16,777                              | 16,852      |               | 19,104                              | 18,343      |               |
| Average annual total revenues per occupied square foot           | \$ 29                               | \$ 28       |               | \$ 29                               | \$ 28       |               |
| Average annual base rent per occupied square foot <sup>(2)</sup> | \$ 24                               | \$ 23       |               | \$ 25                               | \$ 24       |               |

(1) From our 2018 presentation of SPP, we removed four MOB's that were sold and two MOB's that were placed into redevelopment.

(2) Base rent does not include tenant recoveries, additional rents in excess of floors and non-cash revenue adjustments (i.e., straight-line rents, amortization of market lease intangibles, DFL non-cash interest and deferred revenues).

SPP NOI and Adjusted NOI increased primarily as a result of mark-to-market lease renewals. Additionally, SPP adjusted NOI increased as a result of annual rent escalations.

Total Portfolio NOI and Adjusted NOI increased primarily as a result of the aforementioned increases to SPP and the following Non-SPP impacts:

- increased NOI from 2018 acquisitions; and
- increased occupancy in former redevelopment and development properties that have been placed into service; partially offset by
- decreased NOI from MOB sales during 2018.

Table of Contents**Other Income and Expense Items**

The following table summarizes the results of our other income and expense items for the three months ended March 31, 2019 and 2018 (in thousands):

|   | Three months ended March 31, |          |           |
|---|------------------------------|----------|-----------|
|   | 2019                         | 2018     | Change    |
| Interest income   | \$1,713                      | \$6,365  | \$(4,652) |
| Interest expense  | 49,327                       | 75,102   | (25,775)  |
| Depreciation and amortization                           | 131,951                      | 143,250  | (11,299)  |
| General and administrative                              | 21,355                       | 29,175   | (7,820)   |
| Transaction costs                                       | 4,518                        | 2,195    | 2,323     |
| Impairments (recoveries), net                           | 8,858                        | —        | 8,858     |
| Gain (loss) on sales of real estate, net                | 8,044                        | 20,815   | (12,771)  |
| Other income (expense), net                             | 3,133                        | (40,407) | 43,540    |
| Income tax benefit (expense)                            | 3,458                        | 5,336    | (1,878)   |
| Equity income (loss) from unconsolidated joint ventures | (863)                        | 570      | (1,433)   |
| Noncontrolling interests' share in earnings             | (3,520)                      | (3,005)  | (515)     |

*Interest income*

Interest income decreased for the three months ended March 31, 2019 primarily as a result of: (i) the conversion of the U.K. Bridge Loan into real estate during the first quarter of 2018 and (ii) the paydown of a participating development loan during the first quarter of 2018.

*Interest expense*

Interest expense decreased for the three months ended March 31, 2019 as a result of senior unsecured notes, term loan, and mortgage debt repayments during 2018 and a lower average balance under our revolving credit facility.

*Depreciation and amortization expense*

Depreciation and amortization expense decreased for the three months ended March 31, 2019 primarily as a result of dispositions of real estate throughout 2018 and 2019 (including selling interests into the U.K. JV in 2018), partially offset by: (i) assets acquired during 2018 and 2019 (primarily in our life science and medical office segments) and (ii) development and redevelopment projects placed into service during 2018 (primarily in our life science and medical office segments).

*General and administrative expenses*

General and administrative expenses decreased for the three months ended March 31, 2019 primarily as a result of a reduction in severance and related charges (the three months ended March 31, 2018 included charges related to the departure of our former Executive Chairman in March 2018).

*Transaction costs*

Transaction costs increased for the three months ended March 31, 2019 primarily as a result of costs associated with transitioning senior housing triple-net assets to our SHOP segment.

*Impairments (recoveries), net*

We recognized impairments on two MOB's identified as candidates for potential future sale during the three months ended March 31, 2019. There were no impairments recognized in the three months ended March 31, 2018.

*Gain (loss) on sales of real estate, net*

During the three months ended March 31, 2019, we sold: (i) nine SHOP assets for \$68 million, (ii) two senior housing triple-net assets for \$26 million, and (iii) one undeveloped life science land parcel for \$35 million, resulting in total net gain on sales of \$8 million. During the three months ended March 31, 2018, we sold two SHOP facilities, resulting in total net gain on sales of \$21 million.

Table of Contents*Other income (expense), net*

Other income (expense), net, increased for the three months ended March 31, 2019 primarily as a result of a loss on consolidation of seven U.K. care homes in March 2018 (see Note 14 to the Consolidated Financial Statements for additional information).

**Liquidity and Capital Resources**

We anticipate that our cash flow from operations, available cash balances and cash from our various financing activities will be adequate for at least the next 12 months for purposes of: (i) funding recurring operating expenses; (ii) meeting debt service requirements; and (iii) satisfying our distributions to our stockholders and non-controlling interest members. During the three months ended March 31, 2019, distributions to shareholders and noncontrolling interest holders exceeded cash flows from operations by approximately \$24 million. Distributions were made using a combination of cash flows from operations, funds available under revolving line of credit, proceeds from the sale of properties, and other sources of cash available to us.

Our principal investing needs for the next 12 months are to:

fund capital expenditures, including tenant improvements and leasing costs; and  
fund future acquisition, transactional and development activities.

We anticipate satisfying these future investing needs using one or more of the following:

cash flow from operations;  
sale or exchange of ownership interests in properties;  
draws on our credit facilities;  
issuance of additional debt, including unsecured notes and mortgage debt; and/or  
issuance of common or preferred stock.

Access to capital markets impacts our cost of capital and ability to refinance maturing indebtedness, as well as our ability to fund future acquisitions and development through the issuance of additional securities or secured debt.

Credit ratings impact our ability to access capital and directly impact our cost of capital as well. For example, our revolving line of credit facility accrues interest at a rate per annum equal to LIBOR plus a margin that depends upon our credit ratings. We also pay a facility fee on the entire revolving commitment that depends upon our credit ratings. At April 30, 2019, we had senior unsecured credit ratings of Baa1 from Moody's, BBB+ from S&P Global and BBB from Fitch.

**Cash Flow Summary**

The following summary discussion of our cash flows is based on the consolidated statements of cash flows and is not meant to be an all-inclusive discussion of the changes in our cash flows for the periods presented below.

The following table sets forth changes in cash flows (in thousands):

|   | Three Months Ended March 31, |            |            |
|---|------------------------------|------------|------------|
|   | 2019                         | 2018       | Change     |
| Net cash provided by (used in) operating activities | \$ 158,582                   | \$ 196,164 | \$(37,582) |
| Net cash provided by (used in) investing activities | (160,277 )                   | 10,728     | (171,005 ) |
| Net cash provided by (used in) financing activities | 8,521                        | (171,238 ) | 179,759    |

**Operating Cash Flows**

The decrease in operating cash flow is primarily the result of a reduction in income related to (i) dispositions during 2018 and 2019 and (ii) occupancy declines and higher labor costs within our SHOP segment, as well as the timing of payments to satisfy accounts payable and accrued liabilities. The decrease in operating cash flow is partially offset by: (i) 2018 and 2019 acquisitions, (ii) annual rent increases, (iii) developments and redevelopments placed in service during 2018 and 2019, and (iv) decreased interest paid as a result of debt repayments during 2018. Our cash flow from operations is dependent upon the occupancy levels of our buildings, rental rates on leases, our tenants' performance on their lease obligations, the level of operating expenses and other factors.

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*Investing Cash Flows*

The following are significant investing activities for the three months ended March 31, 2019:

• made investments of \$289 million primarily related to the acquisition, development, and redevelopment of real estate; and

• received net proceeds of \$129 million primarily from sales of real estate assets.

The following are significant investing activities for the three months ended March 31, 2018:

• received net proceeds of \$163 million primarily from the sale of our Tandem Mezzanine Loan and sales of real estate assets; and

• made investments of \$159 million primarily for the development of real estate.

*Financing Cash Flows*

The following are significant financing activities for the three months ended March 31, 2019:

• made net borrowings of \$193 million under our bank line of credit, senior unsecured notes and mortgage debt; and

• paid cash dividends on common stock of \$177 million.

The following are significant financing activities for the three months ended March 31, 2018:

• made net borrowings of \$70 million under our bank line of credit;

• paid \$63 million to purchase Brookdale's noncontrolling interest in RIDEA I; and

• paid cash dividends on common stock of \$174 million.

***Debt***

See Note 8 to the Consolidated Financial Statements for additional information about our outstanding debt.

Approximately 95% and 83% of our consolidated debt, inclusive of \$43 million and \$43 million of variable rate debt swapped to fixed through interest rate swaps, was fixed rate debt as of March 31, 2019 and 2018, respectively. At March 31, 2019, our fixed rate debt and variable rate debt had weighted average interest rates of 4.04% and 3.19%, respectively. At March 31, 2018, our fixed rate debt and variable rate debt had weighted average interest rates of 4.20% and 2.78%, respectively. For a more detailed discussion of our interest rate risk, see "Quantitative and Qualitative Disclosures About Market Risk" in Item 3 below.

***Equity***

At March 31, 2019, we had 478 million shares of common stock outstanding, equity totaled \$6.4 billion, and our equity securities had a market value of \$15.2 billion.

At March 31, 2019, non-managing members held an aggregate of 4 million units in five limited liability companies ("DownREITs") for which we are the managing member. The DownREIT units are exchangeable for an amount of cash approximating the then-current market value of shares of our common stock or, at our option, shares of our common stock (subject to certain adjustments, such as stock splits and reclassifications). At March 31, 2019, the DownREIT units were convertible into 6 million shares of our common stock.

***At-The-Market Program***

In February 2019, we terminated our 2018 ATM Program and concurrently established our 2019 ATM Program. In addition to the issuance and sale of shares of our common stock, we may also enter into one or more forward sales agreements with the sales agents for the sale of our shares of common stock under our 2019 ATM Program.

During the three months ended March 31, 2019, we utilized the forward provisions under the 2019 ATM Program to allow for the sale of up to an aggregate of 3.6 million shares of our common stock at an initial weighted average net price of \$31.19 per share, after commissions. Each forward sale has a one year term, during which time we must settle the forward sale by delivery of physical shares of common stock to the forward seller or, at our election, in cash or net shares. The forward sale price that we expect to receive upon settlement will be the initial forward price established upon the effective date, subject to adjustments for: (i) accrued interest, (ii) the forward purchasers' stock borrowing costs, and (iii) certain fixed price reductions during the term of the agreement. At March 31, 2019, no shares had been issued to settle any of the forward sales, all of which remain outstanding.

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At March 31, 2019, approximately \$888 million of our common stock remained available for sale under the 2019 ATM Program. Actual future sales will depend upon a variety of factors, including but not limited to market conditions, the trading price of our common stock and our capital needs. We have no obligation to sell any of these remaining shares under our at-the-market program.

Subsequent to March 31, 2019, we utilized the forward provisions under the 2019 ATM Program to allow for the sale of up to an additional 1.5 million shares of our common stock at an initial weighted average net price of \$30.63 per share, after commissions.

See Note 10 to the Consolidated Financial Statements for additional information about our 2019 ATM Program.

In December 2018, we entered into a forward sales agreement to sell up to an aggregate of 15.25 million shares of our common stock (including shares issued through the exercise of underwriters' options) at an initial net price of \$28.60 per share, after underwriting discounts and commissions. The agreement has a one year term and expires on December 13, 2019 during which time we may settle the forward sales agreement by delivery of physical shares of common stock to the forward seller or, at the our election, by settling in cash or net shares. The forward sale price that we expect to receive upon settlement of the agreement will be the initial net price of \$28.60, subject to adjustments for: (i) accrued interest, (ii) the forward purchasers' stock borrowing costs, and (iii) certain fixed price reductions during the term of the agreement. At March 31, 2019, no shares have been issued under the forward sales agreement, which remains outstanding.

### *Shelf Registration*

We filed a prospectus with the SEC as part of a registration statement on Form S-3, using an automatic shelf registration process. Our current shelf registration statement expires in May 2021, at which time we expect to file a new shelf registration statement. Under the "shelf" process, we may sell any combination of the securities described in the prospectus through one or more offerings. The securities described in the prospectus include common stock, preferred stock, depositary shares, debt securities and warrants.

### **Off-Balance Sheet Arrangements**

We own interests in certain unconsolidated joint ventures as described in Note 6 to the Consolidated Financial Statements. Except in limited circumstances, our risk of loss is limited to our investment in the joint ventures and any outstanding loans receivable. In addition, we have certain properties which serve as collateral for debt that is owed by a previous owner of certain of our facilities. Our risk of loss for these certain properties is limited to the outstanding debt balance plus penalties, if any. We have no other material off-balance sheet arrangements that we expect would materially affect our liquidity and capital resources except for commitments and operating leases included in our Annual Report on Form 10-K for the year ended December 31, 2018 in "Contractual Obligations" under "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations."

Table of Contents**Non-GAAP Financial Measures Reconciliations**

The following is a reconciliation from net income (loss) applicable to common shares, the most directly comparable financial measure calculated and presented in accordance with GAAP, to NAREIT FFO, FFO as adjusted and FAD (in thousands, except per share data):

|   | Three Months Ended March 31,<br>2019 |   | 2018       |
|---|--------------------------------------|---|------------|
| Net income (loss) applicable to common shares   | \$ 61,029                            |   | \$ 39,841  |
| Real estate related depreciation and amortization                                       | 131,951                              |   | 143,250    |
| Real estate related depreciation and amortization on unconsolidated joint ventures      | 15,077                               |   | 17,388     |
| Real estate related depreciation and amortization on noncontrolling interests and other | (4,920)                              | ) | (2,543)    |
| Other real estate-related depreciation and amortization                                 | 2,085                                |   | 1,296      |
| Loss (gain) on sales of real estate, net  | (8,044)                              | ) | (20,815)   |
| Loss (gain) upon consolidation of real estate, net <sup>(1)</sup>                       |                                      |   | 41,017     |
| Impairments (recoveries) of depreciable real estate, net                                | 8,858                                |   | —          |
| NAREIT FFO applicable to common shares  | 206,036                              |   | 219,434    |
| Distributions on dilutive convertible units and other                                   | 1,795                                |   | —          |
| Diluted NAREIT FFO applicable to common shares  | \$ 207,831                           |   | \$ 219,434 |
| Weighted average shares outstanding - diluted NAREIT FFO                                | 483,671                              |   | 469,695    |
| Impact of adjustments to NAREIT FFO:  |                                      |   |            |
| Transaction-related items   | \$ 5,889                             |   | \$ 1,942   |
| Other impairments (recoveries) and losses   | —                                    |   | (3,298)    |

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|   |         |         |            |
|---|---------|---------|------------|
| (gains), net <sup>(2)</sup>                                   |         |         |            |
| Severance and related charges <sup>(3)</sup>                  | —       |         | 8,738      |
| Litigation costs (recoveries)                                 | 128     |         | 406        |
| Foreign currency remeasurement losses (gains)                 | (28     | )       | 130        |
| Total adjustments   | \$      | 5,989   | \$ 7,918   |
| FFO as adjusted applicable to common shares                   | \$      | 212,025 | \$ 227,352 |
| Distributions on dilutive convertible units and other         | 1,780   |         | 1,711      |
| Diluted FFO as adjusted applicable to common shares           | \$      | 213,805 | \$ 229,063 |
| Weighted average shares outstanding - diluted FFO as adjusted | 483,671 |         | 474,363    |



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|   | <b>Three Months Ended</b> |             |
|---|---------------------------|-------------|
|   | <b>March 31,</b>          |             |
|   | <b>2019</b>               | <b>2018</b> |
| FFO as adjusted applicable to common shares           | \$212,025                 | \$227,352   |
| Amortization of deferred compensation <sup>(4)</sup>  | 3,590                     | 3,420       |
| Amortization of deferred financing costs              | 2,699                     | 3,336       |
| Straight-line rents                                   | (6,246 )                  | (10,686 )   |
| FAD capital expenditures                              | (19,220 )                 | (19,118 )   |
| Lease restructure payments                            | 288                       | 299         |
| CCRC entrance fees <sup>(5)</sup>                     | 3,496                     | 3,027       |
| Deferred income taxes                                 | (3,732 )                  | (2,140 )    |
| Other FAD adjustments <sup>(6)</sup>                  | (1,429 )                  | (3,754 )    |
| FAD applicable to common shares                       | 191,471                   | 201,736     |
| Distributions on dilutive convertible units and other | 1,794                     | —           |
| Diluted FAD applicable to common shares               | \$193,265                 | \$201,736   |

Weighted average shares outstanding - diluted FAD 483,671 469,695

|   | <b>Three Months</b> |             |
|---|---------------------|-------------|
|   | <b>Ended</b>        |             |
|   | <b>March 31,</b>    |             |
|   | <b>2019</b>         | <b>2018</b> |
| Diluted earnings per common share                                     | \$0.13              | \$0.08      |
| Depreciation and amortization   | 0.30                | 0.34        |
| Loss (gain) on sales of real estate, net                              | (0.02 )             | (0.04 )     |
| Loss (gain) upon consolidation of real estate, net <sup>(1)</sup>     | —                   | 0.09        |
| Impairments (recoveries) of depreciable real estate, net              | 0.02                | —           |
| Diluted NAREIT FFO per common share                                   | \$0.43              | \$0.47      |
| Transaction-related items   | 0.01                | —           |
| Other impairments (recoveries) and losses (gains), net <sup>(2)</sup> | —                   | (0.01 )     |
| Severance and related charges <sup>(3)</sup>                          | —                   | 0.02        |
| Diluted FFO as adjusted per common share                              | \$0.44              | \$0.48      |

(1) For the three months ended March 31, 2018, represents the loss on consolidation of seven U.K. care homes.

(2) For the three months ended March 31, 2018, represents the impairment recovery of our Tandem Health Care mezzanine loan.

(3) For the three months ended March 31, 2018, primarily relates to the departure of our former Executive Chairman, which consisted of \$6 million of cash severance and \$3 million of equity award vestings.

(4) Excludes amounts related to the acceleration of deferred compensation for restricted stock units that vested upon the departure of certain former employees, which have already been excluded from FFO as adjusted in severance and related charges.

(5) Represents our 49% share of non-refundable entrance fees, as the fees are collected by our CCRC JV, net of reserves and CCRC JV entrance fee amortization.

(6) Primarily includes our share of FAD capital expenditures from unconsolidated joint ventures, partially offset by noncontrolling interests' share of FAD capital expenditures from consolidated joint ventures.

For a reconciliation of NOI and Adjusted NOI to net income (loss), refer to Note 11 to the Consolidated Financial Statements. For a reconciliation of SPP NOI and Adjusted NOI to total portfolio NOI and Adjusted NOI by segment, refer to the analysis of each segment in "Results of Operations" above.

Table of Contents**Critical Accounting Policies and Recent Accounting Pronouncements**

The preparation of financial statements in conformity with U.S. GAAP requires our management to use judgment in the application of accounting policies, including making estimates and assumptions. We base estimates on the best information available to us at the time, our experience and on various other assumptions believed to be reasonable under the circumstances. These estimates affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting periods. If our judgment or interpretation of the facts and circumstances relating to various transactions or other matters had been different, it is possible that different accounting would have been applied, resulting in a different presentation of our consolidated financial statements. From time to time, we re-evaluate our estimates and assumptions. In the event estimates or assumptions prove to be different from actual results, adjustments are made in subsequent periods to reflect more current estimates and assumptions about matters that are inherently uncertain. A summary of our critical accounting policies is included in our Annual Report on Form 10-K for the year ended December 31, 2018 in “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations” and Note 2 to the Consolidated Financial Statements. There have been no significant changes to our critical accounting policies during 2019 other than those resulting from new accounting standards (see Note 2 to the Consolidated Financial Statements).

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

We are exposed to various market risks, including the potential loss arising from adverse changes in interest rates and foreign currency exchange rates, specifically the British pound sterling (“GBP”). We use derivative financial instruments in the normal course of business to mitigate interest rate and foreign currency risk. We do not use derivative financial instruments for speculative or trading purposes. Derivatives are recorded on the consolidated balance sheets at fair value (see Note 17 to the Consolidated Financial Statements).

To illustrate the effect of movements in the interest rate markets, we performed a market sensitivity analysis on our hedging instruments. We applied various basis point spreads to the underlying interest rate curves of the derivative portfolio in order to determine the change in fair value. Assuming a one percentage point change in the underlying interest rate curve, the estimated change in fair value of each of the underlying derivative instruments would not be material.

*Interest Rate Risk.* At March 31, 2019, our exposure to interest rate risk is primarily on our variable rate debt. At March 31, 2019, \$43 million of our variable-rate debt was hedged by interest rate swap transactions. The interest rate swaps are designated as cash flow hedges, with the objective of managing the exposure to interest rate risk by converting the interest rates on our variable-rate debt to fixed interest rates.

Interest rate fluctuations will generally not affect our future earnings or cash flows on our fixed rate debt and assets until their maturity or earlier prepayment and refinancing. If interest rates have risen at the time we seek to refinance our fixed rate debt, whether at maturity or otherwise, our future earnings and cash flows could be adversely affected by additional borrowing costs. Conversely, lower interest rates at the time of refinancing may reduce our overall borrowing costs. However, interest rate changes will affect the fair value of our fixed rate instruments. A one percentage point increase or decrease in interest rates would change the fair value of our fixed rate debt by approximately \$252 million and \$269 million, respectively, and would not materially impact earnings or cash flows. Conversely, changes in interest rates on variable rate debt and investments would change our future earnings and cash flows, but not materially impact the fair value of those instruments. Assuming a one percentage point increase in the interest rate related to the variable-rate debt and variable-rate investments, and assuming no other changes in the outstanding balance at March 31, 2019, our annual interest expense and interest income would increase by approximately \$3 million and \$1 million, respectively.

*Foreign Currency Risk.* At March 31, 2019, our exposure to foreign currencies primarily relates to U.K. investments in leased real estate and related GBP denominated cash flows. Our foreign currency exposure is partially mitigated through the use of GBP-denominated borrowings. Based solely on our operating results for the three months ended March 31, 2019, including the impact of existing hedging arrangements, if the value of the GBP relative to the U.S. dollar were to increase or decrease by 10% compared to the average exchange rate during the three months ended March 31, 2019, the increase or decrease to our cash flows would not be material.

*Market Risk.* We have investments in marketable debt securities classified as held-to-maturity because we have the positive intent and ability to hold the securities to maturity. Held-to-maturity securities are recorded at amortized cost and adjusted for the amortization of premiums and discounts through maturity. We consider a variety of factors in evaluating an other-than-temporary decline in value, such as: the length of time and the extent to which the market value has been less than our current adjusted carrying value; the issuer's financial condition, capital strength and near-term prospects; any recent events specific to that issuer and economic conditions of its industry; and our investment horizon in relationship to an anticipated near-term recovery in the market value, if any. At March 31, 2019, both the fair value and carrying value of marketable debt securities was \$19 million.

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**Item 4. Controls and Procedures**

*Disclosure Controls and Procedures.* We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports under the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and that such information is accumulated and communicated to our management, including our Chief Executive Officer (Principal Executive Officer) and Chief Financial Officer (Principal Financial Officer), to allow for timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As required by Rules 13a-15(b) and 15d-15(b) of the Exchange Act, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer (Principal Executive Officer) and Chief Financial Officer (Principal Financial Officer), of the effectiveness of the design and operation of our disclosure controls and procedures as of March 31, 2019. Based upon that evaluation, our Chief Executive Officer (Principal Executive Officer) and Chief Financial Officer (Principal Financial Officer) concluded that our disclosure controls and procedures were effective at the reasonable assurance level as of March 31, 2019.

*Changes in Internal Control Over Financial Reporting.* There were no changes in our internal control over financial reporting (as such term as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents**PART II. OTHER INFORMATION****Item 1. Legal Proceedings**

See the “Legal Proceedings” section of Note 9 to the Consolidated Financial Statements for information regarding legal proceedings, which information is incorporated by reference in this Item 1.

**Item 1A. Risk Factors**

There are no material changes to the risk factors previously disclosed in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2018.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds****(a)**

None.

**(b)**

None.

**(c)**

The following table sets forth information with respect to purchases of our common stock made by us or on our behalf during the three months ended March 31, 2019.

| Period Covered      | Total Number Of Shares Purchased <sup>(1)</sup> | Average Price Paid Per Share | Total Number Of Shares (Or Units) Purchased As Part Of Publicly Announced Plans Or Programs | Maximum Number (Or Approximate Dollar Value) Of Shares (Or Units) That May Yet Be Purchased Under The Plans Or Programs |
|---------------------|---|------------------------------|---|---|
| January 1-31, 2019  | 44  | \$29.88                      | —   | —   |
| February 1-28, 2019 | 94,787  | 30.79                        | —   | —   |
| March 1-31, 2019    | —   | —                            | —   | —   |
| Total               | 94,831  | \$30.79                      | —   | —   |

<sup>(1)</sup> Represents shares of our common stock withheld under our equity incentive plans to offset tax withholding obligations that occur upon vesting of restricted shares. The value of the shares withheld is based on the closing price of our common stock on the last trading day prior to the date the relevant transaction occurred.

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**Item 6. Exhibits**

- 3.1 Articles of Restatement of HCP, dated June 1, 2012, as supplemented by the Articles Supplementary, dated July 31, 2017 (incorporated herein by reference to Exhibit 3.1 to HCP's Quarterly Report on Form 10-Q filed November 2, 2017).
- 3.2 Fifth Amended and Restated Bylaws of HCP, as amended through July 27, 2017 (incorporated herein by reference to Exhibit 3.2 to HCP's Quarterly Report on Form 10-Q filed November 2, 2017).
- 10.1 Form of 2014 Performance Incentive Plan NEO 3-Year LTIP RSU Agreement (adopted 2019).\*†
- 10.2 Form of 2014 Performance Incentive Plan NEO Retentive LTIP RSU Agreement (adopted 2019).\*†
- 31.1 Certification by Thomas M. Herzog, HCP's Principal Executive Officer, Pursuant to Securities Exchange Act Rule 13a-14(a).\*
- 31.2 Certification by Peter A. Scott, HCP's Principal Financial Officer, Pursuant to Securities Exchange Act Rule 13a-14(a).\*
- 32.1 Certification by Thomas M. Herzog, HCP's Principal Executive Officer, Pursuant to Securities Exchange Act Rule 13a-14(b) and 18 U.S.C. Section 1350.\*\*
- 32.2 Certification by Peter A. Scott, HCP's Principal Financial Officer, Pursuant to Securities Exchange Act Rule 13a-14(b) and 18 U.S.C. Section 1350.\*\*
- 101.INS XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.\*
- 101.SCH XBRL Taxonomy Extension Schema Document.\*
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document.\*
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document.\*
- 101.LAB XBRL Taxonomy Extension Labels Linkbase Document.\*
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document.\*

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\* Filed herewith.

\*\* Furnished herewith.

† Management contract or compensatory plan or arrangement.

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: May 2, 2019 HCP, Inc.

(Registrant)

/s/ THOMAS M. HERZOG  
Thomas M. Herzog  
*President and Chief Executive Officer*  
*(Principal Executive Officer)*

/s/ PETER A. SCOTT  
Peter A. Scott  
*Executive Vice President and*  
*Chief Financial Officer*  
*(Principal Financial Officer)*

/s/ SHAWN G. JOHNSTON  
Shawn G. Johnston  
*Executive Vice President and*  
*Chief Accounting Officer*  
*(Principal Accounting Officer)*