



Douglas Emmett

ANNUAL REPORT 2018

Dear Fellow Shareholders,

We had a very successful year in 2018:

- We grew our Funds from Operations by 12.7% and our Adjusted Funds from Operations by 7.4%, raised our dividend by 4% and still have one of the best dividend coverage ratios in our peer group.
- We signed 800 office leases, with straight line rents averaging 31% higher than the prior lease for the same space.
- With the exception of a loan on a residential development project, we have no term loans due until 2022. Our leverage remains low, and we have plenty of dry powder for external growth.
- Our development platform has matured to the point where it's making meaningful additions to FFO:
 - We've completed construction of 491 new units at our Moanalua Apartment community in Honolulu, which now has almost 1,200 units. With the upgrades to our existing buildings and new amenities, this is now one of the most modern and desirable workforce housing communities in Hawaii.
 - In Brentwood, construction of our 376 unit, 34 story luxury apartment tower is in full swing. This will be the first new high rise residential property west of the 405 freeway in more than 40 years, and represents one of the most exceptional residential development opportunities in all of West Los Angeles.
 - We are already seeing accelerated rent growth from our efforts to reposition several office buildings where we felt targeted investment could significantly increase rental rates.
- Sustainability efforts remained a major priority as we continued to reduce our carbon footprint and deliver meaningful savings. We reduced our electrical usage per square foot by another 2.1%, an impressive eleventh consecutive year of lower consumption. The EPA certified over 95% of our eligible office space as ENERGY STAR compliant, placing almost all of our buildings in the top 25 percent of office buildings nationwide in energy efficiency.



Looking forward, 2019 promises to be another strong year:

- The fundamentals in our markets remain solid. We see significant demand and strong rent growth. Tenant demand remains diverse and includes the fastest growing industries in the United States. Our markets remain some of the most supply constrained in the nation, and the current construction pipeline for new office is de minimis.
- We are moving forward with exciting plans to add approximately 500 new workforce apartments in downtown Honolulu by converting a 25-story, 490,000 square foot office tower to for-rent housing. This project will address the severe rental housing shortage in Honolulu, and support the City's efforts to transform downtown into a vibrant 24-hour community.
- A number of office property redevelopments that were started in 2018 will soon be complete, and the early returns are very promising. We plan to pursue more repositioning opportunities during 2019 and beyond, which will provide significant incremental revenue growth and a very high return on our invested capital. We are also tracking potential acquisitions that could continue the strong external growth we have achieved in recent years.

As I do every year, I promise that the Douglas Emmett team will continue to be committed to the high standards that have been our hallmark for over 45 years.

Sincerely,

A handwritten signature in black ink, appearing to read 'J. Kaplan', with a long horizontal line extending to the right.

Jordan L. Kaplan, President & CEO

DOUGLAS EMMETT, INC.

2018 ANNUAL REPORT

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Glossary

Abbreviations used in this Report:

ADA	Americans with Disabilities Act of 1990
AOCI	Accumulated Other Comprehensive Income (Loss)
ASC	Accounting Standards Codification
ASU	Accounting Standards Update
ATM	At-the-Market
BOMA	Building Owners and Managers Association
CEO	Chief Executive Officer
CFO	Chief Financial Officer
Code	Internal Revenue Code of 1986, as amended
DEI	Douglas Emmett, Inc.
EPS	Earnings Per Share
FASB	Financial Accounting Standards Board
FDIC	Federal Deposit Insurance Corporation
FFO	Funds from Operations
Fund X	Douglas Emmett Fund X, LLC
Funds	Unconsolidated institutional real estate funds (Fund X, Partnership X and Opportunity Fund)
GAAP	Generally Accepted Accounting Principles (United States)
IPO	Initial Public Offering
JV	Joint Venture
LIBOR	London Interbank Offered Rate
LTIP Units	Long-Term Incentive Plan Units
NAREIT	National Association of Real Estate Investment Trusts
NYSE	New York Stock Exchange
OCI	Other Comprehensive Income (Loss)
OP Units	Operating Partnership Units
Operating Partnership	Douglas Emmett Properties, LP
Opportunity Fund	Fund X Opportunity Fund, LLC
Partnership X	Douglas Emmett Partnership X, LP
PCAOB	Public Company Accounting Oversight Board (United States)
QRS	Qualified REIT subsidiary(ies)
REIT	Real Estate Investment Trust
Report	Annual Report on Form 10-K
SEC	Securities and Exchange Commission
Securities Act	Securities Act of 1933, as amended
S&P 500	Standard & Poor's 500 Index
TRS	Taxable REIT subsidiary(ies)
US	United States
USD	United States Dollar
VIE	Variable Interest Entity(ies)

Glossary

Defined terms used in this Report:

Annualized Rent	Annualized cash base rent (excluding tenant reimbursements, parking and other income) before abatements under leases commenced as of the reporting date. Annualized rent for our triple net office leases is calculated by adding expense reimbursements and estimates of normal building expenses paid by tenants to base rent. Annualized rent does not include lost rent recovered from insurance and rent for building management use.
Consolidated Portfolio	Includes the properties in our consolidated results, which includes the properties owned by our consolidated JVs.
Funds From Operations (FFO)	We calculate FFO in accordance with the standards established by NAREIT by excluding gains (or losses) on sales of investments in real estate, excluding gains (or losses) from changes in control of investments in real estate, real estate depreciation and amortization (other than amortization of right-of-use assets for which we are the lessee and amortization of deferred loan costs) from our net income (including adjusting for the effect of such items attributable to consolidated joint ventures and unconsolidated real estate funds, but not for noncontrolling interests included in our Operating Partnership). FFO is a non-GAAP supplemental financial measure that we report because it is useful to our investors. See Management's Discussion and Analysis of Financial Condition and Results of Operations for a discussion of FFO.
Net Operating Income (NOI)	We calculate NOI, a Non-GAAP measure, as revenue less operating expenses attributable to the properties that we own and operate. NOI is calculated by excluding the following from our net income: general and administrative expense, depreciation and amortization expense, other income, other expense, income, including depreciation, from unconsolidated real estate funds, interest expense, gains (or losses) on sales of investments in real estate and net income attributable to noncontrolling interests. NOI is a non-GAAP supplemental financial measure that we report because it is useful to our investors. See Management's Discussion and Analysis of Financial Condition and Results of Operations for a discussion of our Same Property NOI.
Occupancy Rate	The percentage leased, excluding signed leases not yet commenced, as of the reporting date. Management space is considered leased and occupied, while space taken out of service during a repositioning is excluded from both the numerator and denominator for calculating percentage leased and occupied.
Recurring Capital Expenditures	Building improvements required to maintain revenues once a property has been stabilized, and excludes capital expenditures for (i) acquired buildings being stabilized, (ii) newly developed space, (iii) upgrades to improve revenues or operating expenses, (iv) casualty damage or (v) bringing the property into compliance with governmental requirements.
Rentable Square Feet	Based on the BOMA remeasurement and consists of leased square feet (including square feet with respect to signed leases not commenced as of the reporting date), available square feet, building management use square feet and square feet of the BOMA adjustment on leased space.
Same Properties	Our wholly-owned properties that have been owned and operated by us in a consistent manner, and reported in our consolidated results during the entire span of both periods being compared. We exclude from our same property subset any properties (i) acquired during the comparative periods; (ii) sold, held for sale, contributed or otherwise removed from our consolidated financial statements during the comparative periods; or (iii) that underwent a major repositioning project that we believed significantly affected its results during the comparative periods.
Short-Term Leases	Represents leases that expired on or before the reporting date or had a term of less than one year, including hold over tenancies, month to month leases and other short term occupancies.
Total Portfolio	Includes our Consolidated Portfolio plus the properties owned by our Funds.

Forward Looking Statements

This Report contains forward-looking statements within the meaning of the Section 27A of the Securities Act and Section 21E of the Exchange Act. You can find many (but not all) of these statements by looking for words such as “believe”, “expect”, “anticipate”, “estimate”, “approximate”, “intend”, “plan”, “would”, “could”, “may”, “future” or other similar expressions in this Report. We claim the protection of the safe harbor contained in the Private Securities Litigation Reform Act of 1995. We caution investors that any forward-looking statements used in this Report, or those that we make orally or in writing from time to time, are based on our beliefs and assumptions, as well as information currently available to us. Actual outcomes will be affected by known and unknown risks, trends, uncertainties and factors beyond our control or ability to predict. Although we believe that our assumptions are reasonable, they are not guarantees of future performance and some will inevitably prove to be incorrect. As a result, our future results can be expected to differ from our expectations, and those differences may be material. Accordingly, investors should use caution when relying on previously reported forward-looking statements, which were based on results and trends at the time they were made, to anticipate future results or trends. Some of the risks and uncertainties that could cause our actual results, performance or achievements to differ materially from those expressed or implied by forward-looking statements include the following:

- adverse economic or real estate developments affecting Southern California or Honolulu, Hawaii;
- competition from other real estate investors in our markets;
- decreasing rental rates or increasing tenant incentive and vacancy rates;
- defaults on, early terminations of, or non-renewal of leases by tenants;
- increases in interest rates or operating costs;
- insufficient cash flows to service our outstanding debt or pay rent on ground leases;
- difficulties in raising capital;
- inability to liquidate real estate or other investments quickly;
- adverse changes to rent control laws and regulations;
- environmental uncertainties;
- natural disasters;
- insufficient insurance, or increases in insurance costs;
- inability to successfully expand into new markets and submarkets;
- difficulties in identifying properties to acquire and failure to complete acquisitions successfully;
- failure to successfully operate acquired properties;
- risks associated with property development;
- risks associated with JVs;
- conflicts of interest with our officers and reliance on key personnel;
- changes in zoning and other land use laws;
- adverse results of litigation or governmental proceedings;
- failure to comply with laws, regulations and covenants that are applicable to our properties;
- possible terrorist attacks or wars;
- possible cyber attacks or intrusions;
- adverse changes to accounting rules;
- weaknesses in our internal controls over financial reporting;
- failure to maintain our REIT status under federal tax laws; and
- adverse changes to tax laws, including those related to property taxes.

For further discussion of these and other risk factors see Item 1A. "Risk Factors" in our 2018 Annual Report on Form 10-K. This Report and all subsequent written and oral forward-looking statements attributable to us or any person acting on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section. We do not undertake any obligation to release publicly any revisions to our forward-looking statements to reflect events or circumstances after the date of this Report.

Business description

Douglas Emmett, Inc. is a fully integrated, self-administered and self-managed REIT. We are one of the largest owners and operators of high-quality office and multifamily properties located in premier coastal submarkets in Los Angeles and Honolulu. Through our interest in our Operating Partnership and its subsidiaries, our consolidated JVs, and our unconsolidated Funds, we focus on owning, acquiring, developing and managing a significant market share of top-tier office properties and premier multifamily communities in neighborhoods with significant supply constraints, high-end executive housing and key lifestyle amenities. Our properties are located in the Beverly Hills, Brentwood, Burbank, Century City, Olympic Corridor, Santa Monica, Sherman Oaks/Encino, Warner Center/Woodland Hills and Westwood submarkets of Los Angeles County, California, and in Honolulu, Hawaii. We intend to increase our market share in our existing submarkets and may enter into other submarkets with similar characteristics where we believe we can gain significant market share. The terms "us," "we" and "our" as used in this Report refer to Douglas Emmett, Inc. and its subsidiaries on a consolidated basis.

At December 31, 2018, we owned a Consolidated Portfolio consisting of (i) a 16.6 million square foot office portfolio, (ii) 3,595 multifamily apartment units and (iii) fee interests in two parcels of land from which we receive rent under ground leases. We also manage and own equity interests in our unconsolidated Funds which, at December 31, 2018, owned an additional 1.8 million square feet of office space. We manage our unconsolidated Funds alongside our Consolidated Portfolio, and we therefore present the statistics for our office portfolio on a Total Portfolio basis. For more information, see Item 2 "Properties" in our 2018 Annual Report on Form 10-K. As of December 31, 2018, our portfolio consisted of the following (not including the two parcels of land from which we receive rent under ground leases):

	Consolidated Portfolio	Total Portfolio
<u>Office</u> (includes ancillary retail space)		
Wholly-owned properties	53	53
Consolidated JV properties	10	10
Unconsolidated Fund properties	—	8
	63	71
Rentable square feet (in thousands)	16,617	18,455
 <u>Multifamily</u>		
Wholly-owned properties	10	10
Units	3,595	3,595

Business Strategy

We employ a focused business strategy that we have developed and implemented over the past four decades:

- **Concentration of High Quality Office and Multifamily Properties in Premier Submarkets.**

First we select submarkets that are supply constrained, with high barriers to entry, key lifestyle amenities, proximity to high-end executive housing and a strong, diverse economic base. Virtually no entitled Class A office space is currently under construction in any of our targeted submarkets. Our submarkets are dominated by small, affluent tenants, whose rents are very small relative to their revenues and often not the paramount factor in their leasing decisions. At December 31, 2018, our office portfolio median size tenant was approximately 2,600 square feet. Our office tenants operate in diverse industries, including among others legal, financial services, entertainment, real estate, accounting and consulting, health services, retail, technology and insurance, reducing our dependence on any one industry. In 2016, 2017 and 2018, no tenant accounted for more than 10% of our total revenues.

- **Disciplined Strategy of Acquiring Substantial Market Share.**

Once we select a submarket, we follow a disciplined strategy of gaining substantial market share to provide us with extensive local transactional market information, pricing power in lease and vendor negotiations and an enhanced ability to identify and negotiate investment opportunities. As a result, we average approximately a 39% share of the Class A office space in our submarkets based on the square feet of exposure in our total portfolio to each submarket.

- **Proactive Asset and Property Management.**

Our fully integrated and focused operating platform provides the unsurpassed tenant service demanded in our submarkets, with in-house leasing, proactive asset and property management and internal design and construction services, which we believe provides us with a competitive advantage in managing our property portfolio. Our in-house leasing agents and legal specialists allow us to lease a large property portfolio with a diverse group of smaller tenants, closing an average of approximately three office leases each business day, and our in-house construction company allows us to compress the time required for building out many smaller spaces, resulting in reduced vacancy periods. Our property management group oversees day-to-day property management of both our office and multifamily portfolios, allowing us to benefit from the operational efficiencies permitted by our submarket concentration.

Available Information

All reports that we file with the SEC will be available on the SEC website at www.sec.gov. We make available on our website at www.douglasemmett.com our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments thereto, free of charge, as soon as reasonably practicable after we file such reports with, or furnish them to, the SEC. None of the information on or hyperlinked from our website is incorporated into this Report. Our Annual Report on Form 10-K may also be obtained free of charge by written request to:

Stuart McElhinney
Vice President, Investor Relations
310-255-7751
smcelhinney@douglasemmett.com

Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Market for Common Stock; Dividends

Our common stock is traded on the NYSE under the symbol “DEI”. On December 31, 2018, the closing price of our common stock was \$34.13. The table below presents the dividends declared for our common stock as reported by the NYSE:

	<u>First Quarter</u>	<u>Second Quarter</u>	<u>Third Quarter</u>	<u>Fourth Quarter</u>
2018				
Dividend declared	\$ 0.25	\$ 0.25	\$ 0.25	\$ 0.26
2017				
Dividend declared	\$ 0.23	\$ 0.23	\$ 0.23	\$ 0.25

Holders of Record

We had 15 holders of record of our common stock on February 8, 2019. Many of the shares of our common stock are held in “street” name and accordingly, the number of beneficial owners of such shares is not known or included in the foregoing number.

Sales of Unregistered Securities

On December 20, 2017, in connection with the purchase of an office property located at 9401 Wilshire Boulevard, Beverly Hills, California, our Operating Partnership issued \$2.6 million OP Units valued at \$105.7 million to the seller of the office property, as partial consideration for the purchase. Each OP Unit can be exchanged into one share of our common stock (or its cash equivalent at our option). This issuance did not involve underwriters, underwriter discounts or commissions or any public offering. We believe that the issuance of OP Units is exempt from the registration requirements of the Securities Act under Rule 506 of Regulation D promulgated under the Securities Act and Section 4(2) of the Securities Act as a transaction by an issuer not involving any public offering. There was no advertising, general promotion or other marketing undertaken in connection with the issuance. The investor represented and warranted that (i) it acquired the OP Units for investment purposes only and not for the purpose of further distribution; (ii) it had sufficient knowledge and experience in financial and business matters and the ability to bear the economic risk of its investment, and (iii) that the OP Units were taken for investment purposes and not with a view to resale in violation of applicable securities laws.

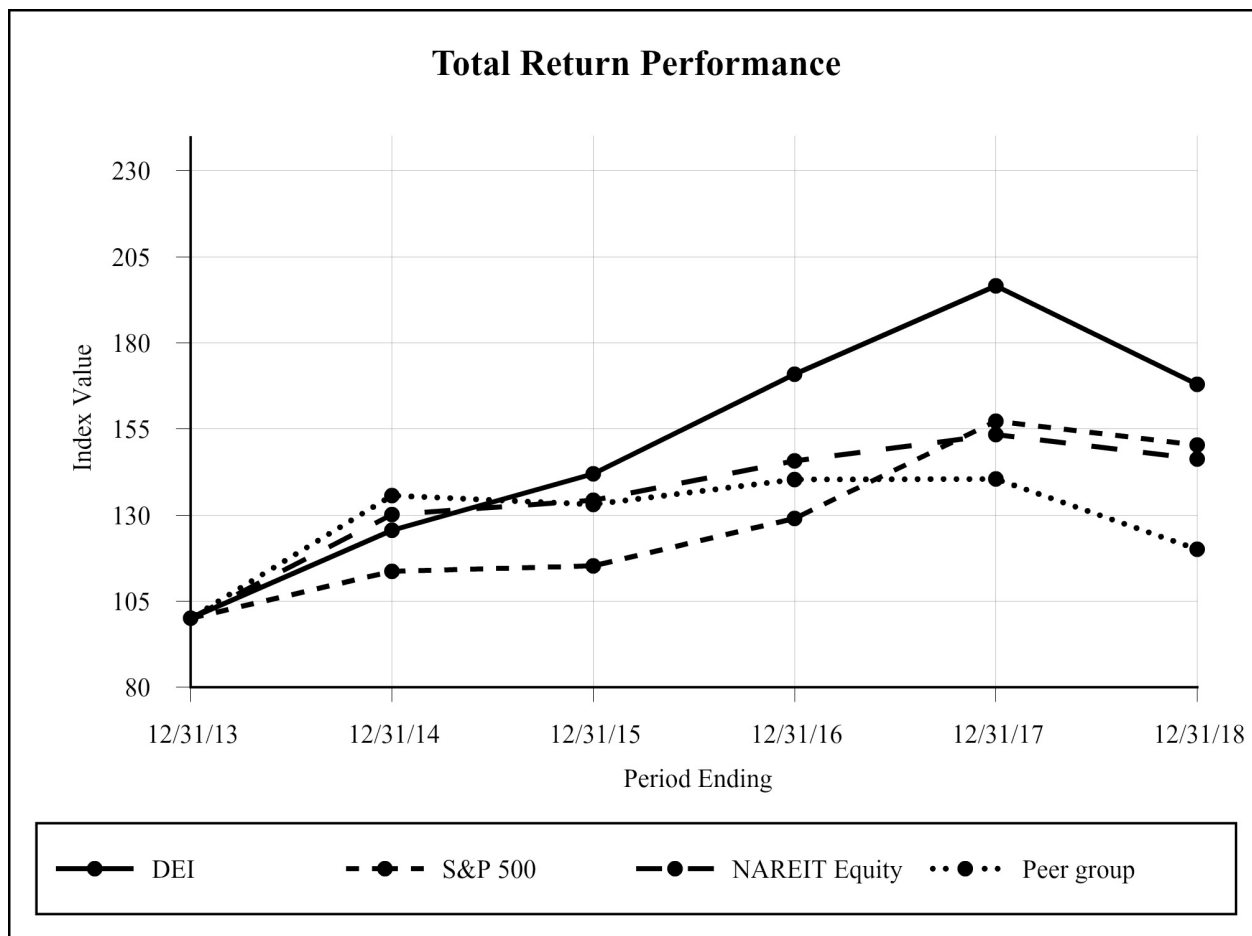
Repurchases of Equity Securities

None.

Performance Graph

The information below shall not be deemed to be “soliciting material” or to be “filed” with the SEC or subject to Regulation 14A or 14C, other than as provided in Item 201 of Regulation S-K, or to the liabilities of Section 18 of the Exchange Act, except to the extent we specifically request that such information be treated as soliciting material or specifically incorporate it by reference into a filing under the Securities Act or the Exchange Act.

The graph below compares the cumulative total return on our common stock from December 31, 2013 to December 31, 2018 to the cumulative total return of the S&P 500, NAREIT Equity and an appropriate “peer group” index (assuming a \$100 investment in our common stock and in each of the indexes on December 31, 2013, and that all dividends were reinvested into additional shares of common stock at the frequency with which dividends are paid on the common stock during the applicable fiscal year). The total return performance presented in this graph is not necessarily indicative of, and is not intended to suggest, the total future return performance.



Index	Period Ending					
	12/31/13	12/31/14	12/31/15	12/31/16	12/31/17	12/31/18
DEI	100.00	125.59	141.97	170.85	196.54	167.91
S&P 500	100.00	113.69	115.26	129.05	157.22	150.33
NAREIT Equity ⁽¹⁾	100.00	130.14	134.30	145.74	153.36	146.27
Peer group ⁽²⁾	100.00	135.67	133.05	140.31	140.49	120.04

(1) FTSE NAREIT Equity REITs index.

(2) Consists of Boston Properties, Inc. (BXP), Kilroy Realty Corporation (KRC), SL Green Realty Corp. (SLG), Vornado Trust (VNO) and Hudson Pacific Properties, Inc (HPP).

Selected Financial Data

The table below presents selected consolidated financial and operating data and should be read in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and our financial statements included on pages 10 and 28 of this Report, respectively.

	Year Ended December 31,				
	2018	2017	2016	2015	2014
Consolidated Statements of Operations Data					
(In thousands):					
Total office revenues	\$ 777,931	\$ 715,546	\$ 645,633	\$ 540,975	\$ 519,405
Total multifamily revenues	\$ 103,385	\$ 96,506	\$ 96,918	\$ 94,799	\$ 80,117
Total revenues	\$ 881,316	\$ 812,052	\$ 742,551	\$ 635,774	\$ 599,522
Operating income	\$ 251,944	\$ 241,023	\$ 220,817	\$ 189,527	\$ 167,854
Net income attributable to common stockholders	\$ 116,086	\$ 94,443	\$ 85,397	\$ 58,384	\$ 44,621
Per Share Data:					
Net income attributable to common stockholders per share - basic	\$ 0.68	\$ 0.58	\$ 0.57	\$ 0.40	\$ 0.31
Net income attributable to common stockholders per share - diluted	\$ 0.68	\$ 0.58	\$ 0.55	\$ 0.39	\$ 0.30
Weighted average common shares outstanding (in thousands):					
Basic	169,893	160,905	149,299	146,089	144,013
Diluted	169,902	161,230	153,190	150,604	148,121
Dividends declared per common share	\$ 1.01	\$ 0.94	\$ 0.89	\$ 0.85	\$ 0.81

	As of December 31,				
	2018	2017	2016	2015	2014
Balance Sheet Data (In thousands):					
Total assets	\$ 8,261,709	\$ 8,292,641	\$ 7,613,705	\$ 6,066,161	\$ 5,938,973
Secured notes payable and revolving credit facility, net	\$ 4,134,030	\$ 4,117,390	\$ 4,369,537	\$ 3,611,276	\$ 3,419,667
Property Data:					
Number of consolidated properties ⁽¹⁾	73	73	69	64	63

(1) All properties are wholly-owned by our Operating Partnership, except for ten office properties owned by our consolidated JVs. The consolidated properties do not include the eight properties owned by our unconsolidated Funds.

Management’s Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with our consolidated financial statements and related notes on page 28 of this Report. Our results of operations for the years ended December 31, 2018, 2017 and 2016 were affected by property acquisitions and dispositions - see Note 3 to our consolidated financial statements in this Report for more information.

Business Description

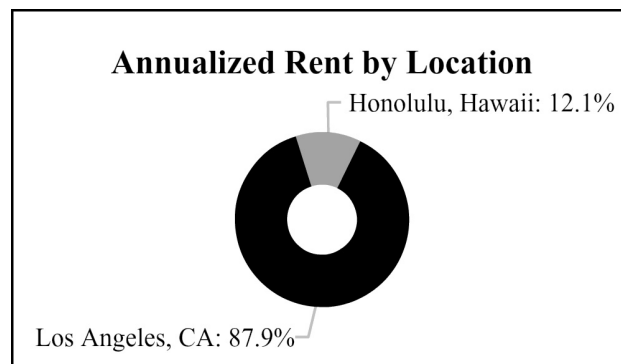
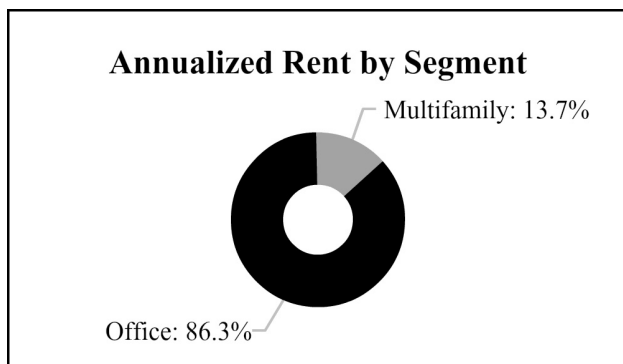
Douglas Emmett, Inc. is a fully integrated, self-administered and self-managed REIT. Through our interest in our Operating Partnership and its subsidiaries, our consolidated JVs and our unconsolidated Funds, we are one of the largest owners and operators of high-quality office and multifamily properties in Los Angeles County, California and in Honolulu, Hawaii. We focus on owning, acquiring, developing and managing a substantial share of top-tier office properties and premier multifamily communities in neighborhoods that possess significant supply constraints, high-end executive housing and key lifestyle amenities. As of December 31, 2018, our portfolio consisted of the following:

	Consolidated Portfolio ⁽¹⁾	Total Portfolio ⁽²⁾
<u>Office</u>		
Class A Properties ⁽³⁾	63	71
Rentable Square Feet (in thousands)	16,617	18,455
Leased rate	91.9%	91.7%
Occupied rate	90.4%	90.3%
<u>Multifamily</u>		
Properties ⁽³⁾	10	10
Units	3,595	3,595
Leased rate	99.0%	99.0%
Occupied rate	97.0%	97.0%

- (1) Our Consolidated Portfolio includes the properties in our consolidated results. Through our subsidiaries, we own 100% of these properties except for ten office properties totaling 2.8 million square feet, which we own through three consolidated JVs. Our Consolidated Portfolio also includes two parcels of land from which we receive ground rent from ground leases to the owners of a Class A office building and a hotel.
- (2) Our Total Portfolio includes our Consolidated Portfolio as well as eight properties totaling 1.8 million square feet owned by our unconsolidated Funds. See Note 5 to our consolidated financial statements in this Report for more information about our unconsolidated Funds.
- (3) Our office and multifamily portfolios include ancillary retail space.

Annualized rent

As of December 31, 2018, annualized rent from our Consolidated Portfolio was derived as follows:



Financings, Developments and Repositionings

Financings

In February 2018, we borrowed 335 million under a secured, non-recourse interest-only loan maturing in March 2025. The loan bears interest at LIBOR + 1.30%, which was effectively fixed at 3.84% for five years through interest rate swaps. The loan is secured by a wholly-owned office property. We used the proceeds from the loan and our credit line to pay off two loans totaling \$426 million which were scheduled to mature in 2019. See Note 7 to our consolidated financial statements in this Report for more information regarding our debt.

Developments

- In West Los Angeles, we are building a 34 story high-rise apartment building with 376 apartments. The tower is being built on a site that is directly adjacent to our existing office building and a 712 unit residential property that we own. We expect the cost of the development to be approximately \$180.0 million to \$200.0 million, which does not include the cost of the land which we have owned since 1997. As part of the project, we are investing additional capital to build a one acre park on Wilshire Boulevard that will be available to the public and provide a valuable amenity to our surrounding properties and community. We expect construction to take about 3 years.
- At our Moanalua Hillside Apartments in Honolulu, as of the date of this Report, we completed the construction of an additional 491 new apartments in addition to our existing 680 apartments. We also invested additional capital to upgrade the existing buildings, improve the parking and landscaping, built a new leasing and management office, and constructed a new fitness center and two pools.
- In downtown Honolulu, we are converting a 25 story, 490 thousand square foot office tower into approximately 500 rental apartments. We expect the conversion to occur in phases over a number of years as the office space is vacated. We currently estimate the construction costs to be approximately \$80.0 million to \$110.0 million, although the inherent uncertainties of development are compounded by the multi-year and phased nature of the conversion. Assuming timely approvals, we expect the first units to be delivered in 2020. This project will help address the severe shortage of rental housing in Honolulu and revitalize the central business district.

Repositionings

We often strategically purchase properties with large vacancies or expected near-term lease roll-over and use our knowledge of the property and submarket to reposition the property for the optimal use and tenant mix. The work we undertake to reposition a building typically takes months or even years, and could involve a range of improvements from a complete structural renovation to a targeted remodeling of selected spaces. We generally select a property for repositioning at the time we purchase it, although repositioning efforts can also occur at properties that we already own. During the repositioning, the affected property may display depressed rental revenue and occupancy levels which impacts our results and, therefore, comparisons of our performance from period to period.

Rental Rate Trends - Total Portfolio

Office Rental Rates

The table below presents the average annual rental rate per leased square foot and the annualized lease transaction costs per leased square foot for leases executed in our total office portfolio:

	Year Ended December 31,				
	2018	2017	2016	2015	2014
Average straight-line rental rate ⁽¹⁾⁽²⁾	\$48.77	\$44.48	\$43.21	\$42.65	\$35.93
Annualized lease transaction costs ⁽³⁾	\$5.80	\$5.68	\$5.74	\$4.77	\$4.66

- (1) Because straight-line rent takes into account the full economic value of each lease, including rent concessions and escalations, we believe that it may provide a better comparison than ending cash rents, which include the impact of the annual escalations over the entire term of the lease. However, care should be taken in any comparison, as the averages are often significantly affected from period to period by factors such as the buildings, submarkets, and types of space and terms involved in the leases executed during the respective reporting period.
- (2) Reflects the weighted average straight-line Annualized Rent.
- (3) Reflects the weighted average leasing commissions and tenant improvement allowances divided by the weighted average number of years for the leases. Excludes leases substantially negotiated by the seller in the case of acquired properties and leases for tenants relocated due to repositioning projects.

Office Rent Roll

The table below presents the rent roll for new and renewed leases per leased square foot executed in our total office portfolio during the year ended December 31, 2018:

Rent Roll ⁽¹⁾⁽²⁾	Starting Cash Rent	Straight-line Rent	Expiring Cash Rent
Leases signed during the period	\$46.44	\$48.77	N/A
Prior leases for the same space	\$35.19	\$37.11	\$40.87
Percentage change	32.0%	31.4%	13.6% ⁽³⁾

- (1) Represents the average initial stabilized cash and straight-line rents on new and renewal leases signed during the quarter compared to the prior lease on the same space, excluding Short-Term Leases, leases where the prior lease was terminated more than a year before signing of the new lease, and leases in acquired buildings where we believe the information about the prior agreement is incomplete or where we believe base rent reflects other off-market inducements to the tenant that are not reflected in the prior lease document.
- (2) Our office rent roll can fluctuate from period to period as a result of changes in our submarkets, buildings and term of the expiring leases, making these metrics difficult to predict.
- (3) The percentage change for expiring cash rent represents the comparison between the starting cash rent on leases executed during the respective period and the expiring cash rent on the prior leases for the same space.

Multifamily Rental Rates

The table below presents the average annual rental rate per leased unit for new tenants:

	Year Ended December 31,				
	2018	2017	2016	2015	2014
Average annual rental rate - new tenants ⁽¹⁾	\$ 27,542	\$ 28,501	\$ 28,435	\$ 27,936	\$ 28,870

- (1) These average rental rates are not directly comparable from year to year because of changes in the properties and units included. In particular, in each of 2018 and 2016, we significantly expanded the number of units in our portfolio in Honolulu, where the rental rates are lower than the average in our portfolio.

Multifamily Rent Roll

During 2018, average rent on leases to new tenants was 0.5% lower for the same unit at the time it became vacant.

Occupancy Rates - Total Portfolio

The tables below present the occupancy rates for our total office portfolio and multifamily portfolio:

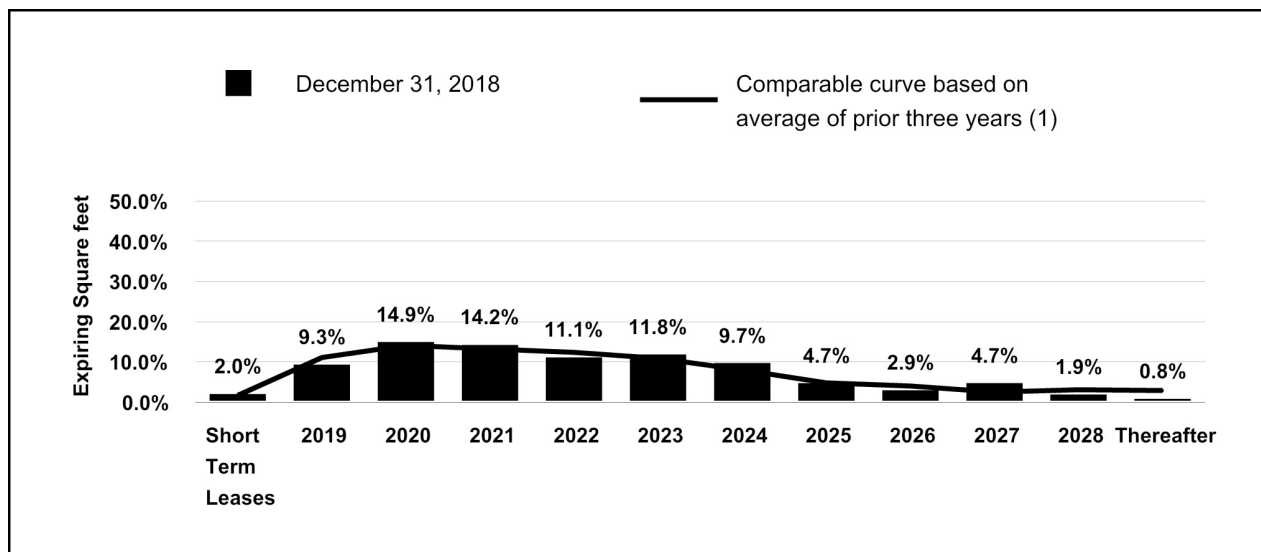
Occupancy Rates ⁽¹⁾ as of:	December 31,				
	2018	2017	2016	2015	2014
Office portfolio	90.3%	89.8%	90.4%	91.2%	90.5%
Multifamily portfolio ⁽²⁾	97.0%	96.4%	97.9%	98.0%	98.2%

Average Occupancy Rates ⁽¹⁾⁽³⁾ :	Year Ended December 31,				
	2018	2017	2016	2015	2014
Office portfolio	89.4%	89.5%	90.6%	90.9%	90.0%
Multifamily portfolio ⁽²⁾	96.6%	97.2%	97.6%	98.2%	98.5%

- (1) Occupancy rates include the impact of property acquisitions, most of whose occupancy rates at the time of acquisition were below that of our existing portfolio.
- (2) The occupancy rate for our multifamily portfolio was impacted during 2018 by the new units that we are leasing at our Moanalua Hillside Apartments development in Honolulu - see "Financings, Developments and Repositionings".
- (3) Average occupancy rates are calculated by averaging the occupancy rates at the end of each of the quarters in the period and at the end of the quarter immediately prior to the start of the period.

Office Lease Expirations

As of December 31, 2018, assuming non-exercise of renewal options and early termination rights, we expect to see expiring square footage in our total office portfolio as follows:



- (1) Average of the percentage of leases at December 31, 2015, 2016, and 2017 with the same remaining duration as the leases for the labeled year had at December 31, 2018. Acquisitions are included in the prior year average commencing in the quarter after the acquisition.

Results of Operations

Comparison of 2018 to 2017

	2018	2017	Favorable (Unfavorable)	Percentage	Commentary
	(In thousands)				
Revenues					
Office rental revenue and tenant recoveries	\$ 661,147	\$ 606,852	\$ 54,295	8.9 %	The increase was due to increase in rental revenues and tenant recoveries of \$27.2 million from properties that we acquired in 2017 and an increase in rental revenues and tenant recoveries of \$27.1 million from properties that we owned throughout both periods. The increase from properties that we owned throughout both periods was primarily due to (i) an increase in rental rates, partially offset by a decrease in occupancy and (ii) an increase in tenant recoveries due to an increase in recoverable operating costs.
Office parking and other income	\$ 116,784	\$ 108,694	\$ 8,090	7.4 %	The increase was due to parking and other income of \$5.8 million from properties that we owned throughout both periods and an increase of \$2.3 million from properties that we acquired in 2017. The increase in parking and other income from properties that we owned throughout both periods primarily reflects an increase in parking rates, partially offset by a decrease in occupancy and an increase in ground rent income.
Multifamily revenue	\$ 103,385	\$ 96,506	\$ 6,879	7.1 %	The increase was primarily due to an increase in rental revenues of \$6.4 million, of which \$3.4 million was due to an increase in revenues from new apartments at our Moanalua development and \$3.0 million was due to increases in revenues from properties that we owned throughout both periods. The increase from the properties that we owned throughout both periods was due to an increase in rental rates for in-place leases, partially offset by a decrease in occupancy.
Operating expenses					
Office rental expenses	\$ 252,751	\$ 233,633	\$ (19,118)	(8.2)%	The increase was due to rental expenses of \$10.9 million from properties that we owned throughout both periods and an increase of \$8.2 million from properties that we acquired during 2017. The increase from properties that we owned throughout both periods was primarily due to an increase in scheduled services expenses, utility expenses, personnel expenses, repairs and maintenance and real estate taxes.
Multifamily rental expenses	\$ 28,116	\$ 24,401	\$ (3,715)	(15.2)%	The increase was primarily due to an increase of \$2.9 million from properties that we owned throughout both periods and an increase of \$0.8 million from new apartments at our Moanalua development. The increase from the properties that we owned throughout both periods was primarily due to personnel expenses, utility expenses, real estate taxes and scheduled services expenses.

	2018	2017	Favorable (Unfavorable)	Percentage	Commentary
	(In thousands)				
General and administrative	\$ 38,641	\$ 36,234	\$ (2,407)	(6.6)%	The increase was primarily due to an increase in personnel expenses, partially offset by a decrease in payroll tax expense due to options that were exercised in the comparable period.
Depreciation and amortization	\$ 309,864	\$ 276,761	\$ (33,103)	(12.0)%	The increase was due to an increase in depreciation and amortization of \$18.4 million from properties that we acquired during 2017, an increase of \$1.2 million from new apartments at our Moanalua development, and an increase of \$13.5 million from properties that we owned throughout both periods. The increase from properties that we owned throughout both periods was primarily due to accelerated depreciation related to our office property repositionings.
<u>Non-Operating Income and Expenses</u>					
Other income	\$ 11,414	\$ 9,712	\$ 1,702	17.5 %	The increase was primarily due to an increase in interest income due to higher money market interest rates.
Other expenses	\$ (7,472)	\$ (7,037)	\$ (435)	(6.2)%	The increase was primarily due an increase in expenses from the health club that we own and operate, and an increase in acquisition-related expenses related to properties that we did not acquire.
Income, including depreciation, from unconsolidated real estate funds	\$ 6,400	\$ 5,905	\$ 495	8.4 %	The increase was primarily due to an increase in net income for our unconsolidated Funds, which was primarily due to (i) an increase in revenues due to an increase in rental rates and (ii) higher interest income due to higher money market interest rates, partially offset by an increase in interest expense due to higher debt balances and higher interest rates.
Interest expense	\$(133,402)	\$(145,176)	\$ 11,774	8.1 %	The decrease was primarily due to lower debt balances.
Demolition expenses	\$ (272)	\$ —	\$ (272)	100.0 %	The increase reflects expenses to demolish an existing structure to allow our high-rise apartment development in Brentwood, California.

Comparison of 2017 to 2016

	2017	2016	Favorable (Unfavorable)	Percentage	Commentary
	(In thousands)				
Revenues					
Office rental revenues and tenant recoveries.	\$ 606,852	\$ 545,061	\$ 61,791	11.3 %	The increase was due to rental revenues and tenant recoveries of \$49.0 million from properties that we acquired in 2016 and 2017 and an increase in rental revenues and tenant recoveries of \$15.9 million from the properties that we owned throughout both periods, partially offset by a decrease of \$3.1 million in rental revenues from a property that we sold during 2016. The increase from properties that we owned throughout both periods was primarily due to (i) an increase in rental rates, partially offset by a decrease in occupancy and a decrease of \$1.5 million in the accretion from below-market leases and (ii) an increase in tenant recoveries due to an increase in recoverable operating costs .
Office parking and other income	\$ 108,694	\$ 100,572	\$ 8,122	8.1 %	The increase was due to parking and other income of \$5.1 million from properties that we acquired in 2016 and 2017 and an increase of \$3.5 million in parking and other income from properties that we owned throughout both periods, partially offset by a decrease of \$0.5 million in parking and other income from a property that we sold during 2016. The increase in parking and other income from properties that we owned throughout both periods primarily reflects increases in rates, partially offset by a decrease in occupancy.
Multifamily revenue	\$ 96,506	\$ 96,918	\$ (412)	(0.4)%	The decrease was due to a decrease of \$2.8 million in the accretion from below-market leases, partially offset by an increase of \$2.4 million in rental revenues and parking income. The decrease in the accretion from below-market leases was due to the completion in the fourth quarter 2016 of the amortization of below-market lease intangibles recorded at the time of our IPO. The increase in rental revenues and parking income was primarily due to an increase in rental rates.
Operating expenses					
Office rental expenses	\$ 233,633	\$ 214,546	\$ (19,087)	(8.9)%	The increase was due to rental expenses of \$17.3 million from properties that we acquired during 2016 and 2017 and an increase of \$3.2 million from properties that we owned throughout both periods, partially offset by a decrease of \$1.4 million from a property that we sold during 2016. The increase from properties that we owned throughout both periods was primarily due to an increase in personnel expenses, utilities and real estate taxes, partially offset by a decrease in parking expenses.
Multifamily rental expenses	\$ 24,401	\$ 23,317	\$ (1,084)	(4.6)%	The increase was due to a prior year excise tax refund of \$0.5 million in 2016 which offset expenses in that year and increases in scheduled services, personnel expenses and utilities in 2017.

	2017	2016	Favorable (Unfavorable)	Percentage	Commentary
	(In thousands)				
General and administrative	\$ 36,234	\$ 34,957	\$ (1,277)	(3.7)%	The increase was primarily due to an increase in personnel expenses.
Depreciation and amortization	\$ 276,761	\$ 248,914	\$ (27,847)	(11.2)%	The increase was primarily due to depreciation and amortization of \$24.6 million from properties that we acquired during 2016 and 2017 and an increase of \$3.7 million from properties that we owned throughout both periods, partially offset by a decrease of \$0.5 million from a property that we sold during 2016. The increase from the properties that we owned throughout both periods was primarily due to an increase in building improvements, tenant improvements and leasing commissions.
<u>Non-Operating Income and Expenses</u>					
Other income	\$ 9,712	\$ 8,759	\$ 953	10.9 %	The increase was primarily due to an increase in interest income and revenue from the health club that we own and operate.
Other expenses	\$ (7,037)	\$ (9,477)	\$ 2,440	25.7 %	The decrease was primarily due to \$2.8 million of acquisition-related expenses incurred in connection with the acquisition of properties by our consolidated JVs in 2016. We commenced capitalizing acquisition-related expenses in 2017 as a result of a change in accounting policy - see Note 2 to our consolidated financial statements in this Report.
Income, including depreciation, from unconsolidated real estate funds	\$ 5,905	\$ 7,812	\$ (1,907)	(24.4)%	The decrease was primarily due to an increase in interest expense and loan costs for one of our unconsolidated Funds related to a 2017 loan refinancing.
Interest expense	\$(145,176)	\$(146,148)	\$ 972	0.7 %	The decrease was due to a decrease in our Operating Partnership interest expense of \$13.3 million as a result of lower debt balances, partially offset by interest expense of \$12.3 million from debt related to our consolidated JV property acquisitions in 2016 and 2017.
Gains on sales of investments in real estate	\$ —	\$ 14,327	\$ (14,327)	(100.0)%	In 2016 we sold (i) a thirty-percent ownership interest in one of our consolidated JVs to a third party investor and recognized a gain of \$1.1 million, (ii) a thirty-five percent ownership interest in one of our consolidated JVs to a third party investor and recognized a gain of \$0.6 million and (iii) a wholly-owned office property and recognized a gain of \$12.7 million.

Non-GAAP Supplemental Financial Measure: FFO

Usefulness to Investors

We report FFO because it is a widely reported measure of the performance of equity REITs, and is also used by some investors to identify trends in occupancy rates, rental rates and operating costs from year to year, and to compare our performance with other REITs. FFO is a non-GAAP financial measure for which we believe that net income is the most directly comparable GAAP financial measure. FFO has limitations as a measure of our performance because it excludes depreciation and amortization of real estate, and captures neither the changes in the value of our properties that result from use or market conditions, nor the level of capital expenditures, tenant improvements and leasing commissions necessary to maintain the operating performance of our properties, all of which have real economic effect and could materially impact our results from operations. FFO should be considered only as a supplement to net income as a measure of our performance and should not be used as a measure of our liquidity or cash flow, nor is it indicative of funds available to fund our cash needs, including our ability to pay dividends. Other REITs may not calculate FFO in accordance with the NAREIT definition and, accordingly, our FFO may not be comparable to the FFO of other REITs. See "Results of Operations" above for a discussion of the items that impacted our net income.

Comparison of 2018 to 2017

Our FFO increased by 45.0 million, or 12.7%, to \$399.7 million for 2018 compared to \$354.7 million for 2017, which was primarily due to (i) an increase in operating income from our office portfolio due to acquisitions in 2017 and higher rental rates, (ii) an increase in operating income from our multifamily portfolio due to rent from new apartments at our Moanalua development and higher rental rates in existing units in our portfolio, and (iii) a decrease in interest expense due to lower debt balances, partially offset by an increase in general and administrative expenses due to an increase in personnel costs.

Comparison of 2017 to 2016

Our FFO increased by \$29.0 million, or 8.9%, to \$354.7 million for 2017 compared to \$325.7 million for 2016, which was primarily due to (i) an increase in operating income from our office portfolio due to property acquisitions in 2016 and 2017 and increasing rental rates, (ii) a decrease in other expenses as a result of acquisition-related costs we expensed in 2016, while similar costs were capitalized in 2017 as a result of the adoption of an ASU in 2017, and (iii) a decrease in interest expense due to lower debt balances, partially offset by (a) a decrease in the operating income from our multifamily portfolio due to a decrease in the accretion from below-market leases due to the completion in 2016 of the amortization of below-market lease intangibles recorded at the time of our IPO, and an excise tax refund of \$0.5 million that reduced our multifamily operating expenses in 2016, (b) an increase in general and administrative expenses due an increase in personnel costs, and (c) a decrease in the FFO of our Funds due to an increase in interest expense and loan costs related to the refinancing of a loan for one of our Funds during 2017.

Reconciliation to GAAP

The table below reconciles our FFO (the FFO attributable to our common stockholders and noncontrolling interests in our Operating Partnership - which includes our share of our consolidated JVs and our unconsolidated Funds FFO) to net income attributable to common stockholders computed in accordance with GAAP:

(In thousands)	Year Ended December 31,		
	2018	2017	2016
Net income attributable to common stockholders	\$ 116,086	\$ 94,443	\$ 85,397
Depreciation and amortization of real estate assets	309,864	276,761	248,914
Net income attributable to noncontrolling interests	12,526	9,984	10,693
Adjustments attributable to unconsolidated funds ⁽¹⁾	16,702	16,220	16,016
Adjustments attributable to consolidated JVs ⁽²⁾	(55,448)	(42,674)	(20,961)
Gain on sale of investment in real estate	—	—	(14,327)
FFO	\$ 399,730	\$ 354,734	\$ 325,732

(1) Adjusts for our share of our unconsolidated Funds depreciation and amortization of real estate assets.

(2) Adjusts for the net income and depreciation and amortization of real estate assets that is attributable to the noncontrolling interests in our consolidated JVs.

Non-GAAP Supplemental Financial Measure: Same Property NOI

Usefulness to Investors

We report Same Property NOI to facilitate a comparison of our operations between reported periods. Many investors use Same Property NOI to evaluate our operating performance and to compare our operating performance with other REITs, because it can reduce the impact of investing transactions on operating trends. NOI is a non-GAAP financial measure for which we believe that net income is the most directly comparable GAAP financial measure. We report NOI because it is a widely recognized measure of the performance of equity REITs, and is used by some investors to identify trends in occupancy rates, rental rates and operating costs and to compare our operating performance with that of other REITs. NOI has limitations as a measure of our performance because it excludes depreciation and amortization expense, and captures neither the changes in the value of our properties that result from use or market conditions, nor the level of capital expenditures, tenant improvements and leasing commissions necessary to maintain the operating performance of our properties, all of which have real economic effect and could materially impact our results from operations. Other REITs may not calculate Same Property NOI in the same manner. As a result, our Same Property NOI may not be comparable to the Same Property NOI of other REITs. Same Property NOI should be considered only as a supplement to net income as a measure of our performance and should not be used as a measure of our liquidity or cash flow, nor is it indicative of funds available to fund our cash needs, including our ability to pay dividends.

Comparison of 2018 to 2017:

Our 2018 same properties included 47 office properties, aggregating 11.8 million Rentable Square Feet, and 9 multifamily properties with an aggregate 2,640 units:

(In thousands)	2018	2017	Favorable (Unfavorable)	Percentage	Commentary
Office revenues	\$ 502,912	\$ 480,101	\$ 22,811	4.8 %	The increase was primarily due to an increase in rental and parking rates, an increase in tenant recovery revenues reflecting an increase in recoverable operating costs and an increase in ground rent income.
Office expenses	(166,541)	(158,262)	(8,279)	(5.2)%	The increase was primarily due to an increase in scheduled services expenses, utility expenses, personnel expenses, repairs and maintenance and real estate taxes.
Office NOI	336,371	321,839	14,532	4.5 %	
Multifamily revenues	84,587	81,927	2,660	3.2 %	The increase was primarily due to an increase in rental revenues due to an increase in occupancy and rental rates.
Multifamily expenses	(21,508)	(19,969)	(1,539)	(7.7)%	The increase was primarily due to an increase in personnel expenses, scheduled services expenses, utility expenses, repairs and maintenance and real estate taxes.
Multifamily NOI	63,079	61,958	1,121	1.8 %	
Total NOI	\$ 399,450	\$ 383,797	\$ 15,653	4.1 %	

Reconciliation to GAAP

The table below presents a reconciliation of our Same Property NOI to net income attributable to common stockholders:

(In thousands)	2018	2017
Same Property NOI	\$ 399,450	\$ 383,797
Non-comparable office revenues	275,019	235,445
Non-comparable office expenses	(86,210)	(75,371)
Non-comparable multifamily revenues	18,770	14,579
Non-comparable multifamily expenses	(6,580)	(4,432)
NOI	600,449	554,018
General and administrative	(38,641)	(36,234)
Depreciation and amortization	(309,864)	(276,761)
Operating income	251,944	241,023
Other income	11,414	9,712
Other expenses	(7,472)	(7,037)
Income, including depreciation, from unconsolidated real estate funds	6,400	5,905
Interest expense	(133,402)	(145,176)
Demolition expenses	(272)	—
Net income	128,612	104,427
Less: Net income attributable to noncontrolling interests	(12,526)	(9,984)
Net income attributable to common stockholders	<u>\$ 116,086</u>	<u>\$ 94,443</u>

Comparison of 2017 to 2016

Our 2017 same properties included 51 office properties, aggregating 13.0 million rentable square feet, and 9 multifamily properties with an aggregate 2,640 units:

(In thousands)	2017	2016	Favorable (Unfavorable)	Percentage	Commentary
Office revenues	\$ 551,651	\$ 531,734	\$ 19,917	3.7 %	The increase was primarily due to an increase in rental and parking rates, as well as higher tenant recovery revenues reflecting increased recoverable operating costs.
Office expenses	(176,916)	(173,977)	(2,939)	(1.7)%	The increase was primarily due to an increase in personnel expenses, utilities and real estate taxes, partially offset by a decrease in parking expenses.
Office NOI	<u>374,735</u>	<u>357,757</u>	16,978	4.7 %	
Multifamily revenues	81,927	82,328	(401)	(0.5)%	The decrease was primarily due to a decrease of \$2.8 million in the accretion from below-market leases, partially offset by an increase in rental revenues and parking and other income. The decrease in the accretion from below-market leases was due to the completion in 2016 of the amortization of below-market lease intangibles recorded at the time of our IPO. The increase in rental revenues and parking and other income was primarily due to an increase in rental rates.
Multifamily expenses	(19,969)	(19,229)	(740)	(3.8)%	The increase was primarily due to an excise tax refund of \$0.5 million in 2016 which offset other operating expenses.
Multifamily NOI	<u>61,958</u>	<u>63,099</u>	(1,141)	(1.8)%	
Total NOI	<u><u>\$ 436,693</u></u>	<u><u>\$ 420,856</u></u>	\$ 15,837	3.8 %	

Reconciliation to GAAP

The table below presents a reconciliation of our Same Property NOI to net income attributable to common stockholders:

(In thousands)	2017	2016
Same Property NOI	\$ 436,693	\$ 420,856
Non-comparable office revenues	163,895	113,899
Non-comparable office expenses	(56,717)	(40,569)
Non-comparable multifamily revenues	14,579	14,590
Non-comparable multifamily expenses	(4,432)	(4,088)
NOI	554,018	504,688
General and administrative	(36,234)	(34,957)
Depreciation and amortization	(276,761)	(248,914)
Operating income	241,023	220,817
Other income	9,712	8,759
Other expenses	(7,037)	(9,477)
Income, including depreciation, from unconsolidated real estate funds	5,905	7,812
Interest expense	(145,176)	(146,148)
Income before gains	104,427	81,763
Gains on sales of investments in real estate	—	14,327
Net income	104,427	96,090
Less: Net income attributable to noncontrolling interests	(9,984)	(10,693)
Net income attributable to common stockholders	<u>\$ 94,443</u>	<u>\$ 85,397</u>

Liquidity and Capital Resources

Short-term liquidity

Excluding acquisitions, development projects and debt refinancings, we expect to meet our short-term liquidity requirements through cash on hand, cash generated by operations, and our revolving credit facility. See Note 7 to our consolidated financial statements of this Report for more information regarding our revolving credit facility.

Long-term liquidity

Our long-term liquidity needs consist primarily of funds necessary to pay for acquisitions, development projects and debt refinancings. We do not expect to have sufficient funds on hand to cover these long-term cash requirements due to the requirement to distribute a substantial majority of our income on an annual basis imposed by REIT federal tax rules. We plan to meet our long-term liquidity needs through long-term secured non-recourse indebtedness, the issuance of equity securities, including common stock and OP Units, as well as property dispositions and JV transactions. We have an ATM program which would allow us, subject to market conditions, to sell up to \$400 million of shares of common stock as of the date of this Report.

To mitigate the impact of changing interest rates on our cash flows from operations, most of our long-term secured loans carry fixed interest rates, and we generally enter into interest rate swap agreements with respect to our loans with floating interest rates. These swap agreements generally expire between one to two years before the maturity date of the related loan, during which time we can refinance the loan without any interest penalty. See Notes 7 and 9 to our consolidated financial statements in this Report for more information regarding our debt and derivative contracts, respectively.

Contractual obligations as of December 31, 2018

(In thousands)	Payment due by period				
	Total	Less than 1 year	2-3 years	4-5 years	Thereafter
Term loan principal payments ⁽¹⁾	\$ 4,163,982	\$ 145,718	\$ 401,539	\$ 2,536,685	\$ 1,080,040
Ground lease payments ⁽²⁾	49,843	733	1,466	1,466	46,178
Development commitments ⁽³⁾	202,865	89,381	113,484	—	—
Capital expenditures and tenant improvements commitments ⁽⁴⁾	55,340	55,340	—	—	—
Total	\$ 4,472,030	\$ 291,172	\$ 516,489	\$ 2,538,151	\$ 1,126,218

- (1) Reflects the future principal payments due on our secured notes payable and revolving credit facility, excluding any maturity extension options. For more information regarding our debt and the interest rates that determine our periodic interest payments see Note 7 to our consolidated financial statements in this Report.
- (2) Reflects the future minimum ground lease payments. See Note 16 to our consolidated financial statements in this Report.
- (3) See "Financings, Developments and Repositionings" for a discussion of our developments.
- (4) Reflects the aggregate remaining contractual commitment for capital expenditure projects and repositionings, as well as tenant improvements. See "Financings, Developments and Repositionings" for a discussion of our repositionings.

Off-Balance Sheet Arrangements

Unconsolidated Funds Debt

Our unconsolidated Funds have their own secured non-recourse debt, and we have made certain environmental and other limited indemnities and guarantees covering customary non-recourse carve-outs related to those loans. We have also guaranteed the related swaps. Our Funds have agreed to indemnify us for any amounts that we would be required to pay under these agreements. As of December 31, 2018, all of the obligations under the respective loans and swap agreements have been performed in accordance with the terms of those agreements. For information regarding our Funds and Funds' debt, see Notes 5 and 17, respectively, to our consolidated financial statements in this Report.

Cash Flows

Comparison of 2018 to 2017

	2018	2017	Increase (Decrease)	Percentage
	(In thousands)			
Cash flows provided by operating activities ⁽¹⁾	\$ 432,982	\$ 402,697	\$ 30,285	7.5 %
Cash flows used in investing activities ⁽²⁾	\$ (249,551)	\$ (669,595)	\$ (420,044)	(62.7)%
Cash flows (used in) provided by financing activities ⁽³⁾	\$ (213,849)	\$ 330,616	\$ (544,465)	(164.7)%

- (1) Our cash flows provided by operating activities are primarily dependent upon the occupancy and rental rates of our portfolio, the collectability of rent and recoveries from our tenants, and the level of our operating expenses and general and administrative costs, and interest expense. The increase was primarily due to (i) an increase in operating income from our office portfolio due to acquisitions in 2017 and higher rental rates, (ii) an increase in operating income from our multifamily portfolio due to rents from new apartments at our Moanalua development and higher rental rates from existing units, and (iii) a decrease in interest expense due to lower debt balances.
- (2) Our cash flows used in investing activities is generally used to fund property acquisitions, developments and redevelopment projects, and Recurring and non-Recurring Capital Expenditures. The decrease is primarily due to \$537.7 million paid for properties acquired in 2017, partially offset by (i) an increase of \$70.7 million for capital expenditures for improvements to real estate and (ii) a decrease of \$36.2 million in capital distributions received from our Funds.
- (3) Our cash flows used in financing activities are generally impacted by our borrowings and capital activities, as well as dividends and distributions paid to common stockholders and noncontrolling interests, respectively. The decrease is primarily due to (i) \$593.2 million in proceeds from the issuance of common stock in 2017, (ii) \$284.2 million in contributions from non-controlling interests in 2017, partially offset by (a) an increase of \$299.7 million in net borrowings and (b) a decrease of \$52.6 million in payroll taxes paid related to the exercise of stock options.

Critical Accounting Policies

Our discussion and analysis of our financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with GAAP, which requires us to make estimates of certain items which affect the reported amounts of our assets, liabilities, revenues and expenses. While we believe that our estimates are based upon reasonable assumptions and judgments at the time that they are made, some of our estimates could prove to be incorrect, and those differences could be material. Below is a discussion of our critical accounting policies, which are the policies we believe require the most estimate and judgment. See Note 2 to our consolidated financial statements included in this Report for the summary of our significant accounting policies.

Investment in Real Estate

Acquisitions

We allocate the purchase price, which includes the capitalized transaction costs, of acquired properties to: (i) land, (ii) buildings and improvements, (iii) tenant improvements and identifiable intangible assets such as in-place at-market leases, (iv) acquired above- and below-market ground and tenant leases, and if applicable (v) assumed debt, based upon our estimates of expected future cash flows and other valuation techniques. We estimate the relative fair values of the tangible assets on an “as-if-vacant” basis. The estimated relative fair value of acquired in-place at-market leases are the estimated costs to lease the property to the occupancy level at the date of acquisition, including the fair value of leasing commissions and legal costs. We evaluate the time period over which we expect such occupancy level to be achieved and include an estimate of the net operating costs (primarily real estate taxes, insurance and utilities) incurred during the lease-up period. Above and below-market ground and tenant leases are recorded as an asset or liability based upon the present value (using an interest rate which reflects the risks associated with the leases acquired) of the difference between the contractual amounts to be paid or received pursuant to the in-place ground or tenant leases, respectively, and our estimate of fair market rental rates for the corresponding in-place leases, over the remaining non-cancelable term of the leases. Assumed debt is recorded at fair value based upon the present value of the expected future payments.

These estimates require judgment, involve complex calculations, and the allocations have a direct and material impact on our results of operations because, for example, (i) there would be less depreciation if we allocate more value to land (which is not depreciated), or (ii) if we allocate more value to buildings than to tenant improvements, the depreciation would be recognized over a much longer time period, because buildings are depreciated over a longer time period than tenant improvements.

Cost capitalization

We capitalize development costs, including predevelopment costs, interest, property taxes, insurance and other costs directly related to the development of real estate. Indirect development costs, including salaries and benefits, office rent, and associated costs for those individuals directly responsible for and who spend their time on development activities are also capitalized and allocated to the projects to which they relate. Development costs are capitalized while substantial activities are ongoing to prepare an asset for its intended use. We consider a development project to be substantially complete when the residential units or office space is available for occupancy but no later than one year after cessation of major construction activity. Costs incurred after a project is substantially complete and ready for its intended use, or after development activities have ceased, are expensed as incurred. Costs previously capitalized related to abandoned developments are charged to earnings. Expenditures for repairs and maintenance are expensed as incurred. The capitalization of development costs requires judgment, and can directly and materially impact our results of operations because, for example, (i) if we don't capitalize costs that should be capitalized, then our operating expenses would be overstated during the development period, and the subsequent depreciation of the developed real estate would be understated, or (ii) if we capitalize costs that should not be capitalized, then our operating expenses would be understated during the development period, and the subsequent depreciation of the real estate would be overstated. We capitalized development costs of \$78.7 million, \$66.0 million and \$31.6 million during 2018, 2017 or 2016, respectively.

Impairment of Long-Lived Assets

We assess our investment in real estate and our investment in our Funds for impairment on a periodic basis, and whenever events or changes in circumstances indicate that the carrying value of our investments may not be recoverable. If the undiscounted future cash flows expected to be generated by the asset are less than the carrying value of the asset, and our evaluation indicates that we may be unable to recover the carrying value, then we would record an impairment loss to the extent that the carrying value exceeds the estimated fair value of the asset. Our estimates of future cash flows are based in part upon assumptions regarding future occupancy, rental rates and operating costs, and could differ materially from actual results. We record real estate held for sale at the lower of carrying value or estimated fair value, less costs to sell, and similarly recognize impairment losses if we believe that we cannot recover the carrying value. Our evaluation of market conditions for assets held for sale requires judgment, and our expectations could differ materially from actual results. Impairment losses would reduce our net income and could be material. We did not record any impairment losses for our long-lived assets during 2018, 2017 or 2016.

Revenue Recognition for Tenant Recoveries

Our tenant recovery revenues for recoverable operating expenses are recognized as revenue in the period that the recoverable expenses are incurred. Subsequent to year-end, we perform reconciliations on a lease-by-lease basis and bill or credit each tenant for any differences between the estimated expenses we billed to the tenant and the actual expenses incurred. Estimating tenant recovery revenues requires an in-depth analysis of the complex terms of each underlying lease. Examples of estimates and judgments made when determining the amounts recoverable include:

- estimating the recoverable expenses;
- estimating the impact of changes to expense and occupancy during the year;
- estimating the fixed and variable components of operating expenses for each building;
- conforming recoverable expense pools to those used in the base year for the underlying lease; and
- judging whether an expense or capital expenditure is recoverable pursuant to the terms of the underlying lease.

These estimates require judgment and involve complex calculations. If our estimates prove to be incorrect, then our tenant recovery revenues and net income could be materially and adversely affected in future periods when we perform our reconciliations. The impact of changing our current year tenant recovery billings by 5% would result in a change to our tenant recovery revenues and net income of \$2.4 million, \$2.1 million and \$2.0 million during 2018, 2017 and 2016, respectively.

Allowances for Tenant and Deferred Rent Receivables

Our estimates regarding the adequacy of our allowances for uncollectible tenant and deferred rent receivables requires judgment, including the creditworthiness of specific tenants and general economic trends and conditions. For most of our tenants, our only security is their security deposits or letters of credit, and in some cases we do not require any security deposit or letter of credit. If our allowances are not sufficient to cover the unsecured losses from our tenants who fail to make contractual payments, our revenues and net income could be materially and adversely affected in future periods. As of December 31, 2018, 2017 and 2016, the total of our allowances was \$8.1 million, \$6.5 million and \$7.8 million, respectively. The impact of changing the allowances by 5% would result in a change to our revenues and net income of \$403 thousand, \$323 thousand and \$390 thousand during 2018, 2017 and 2016, respectively.

Stock-Based Compensation

We award stock-based compensation to certain employees and non-employee directors in the form of LTIP Units. We recognize the fair value of the awards over the requisite vesting period, which is based upon service. The fair value of the awards is based upon the market value of our common stock on the grant date and a discount for post-vesting restrictions. Our estimate of the discount for post-vesting restrictions requires judgment. If our estimate of the discount is too high or too low it would result in the fair value of the awards that we make being too low or too high, respectively, which would result in an under- or over-expense of stock-based compensation, respectively, and this under- or over-expensing of stock-based compensation could be material to our net income. Stock-based compensation expense was \$22.3 million, \$18.5 million and \$17.4 million for 2018, 2017 and 2016, respectively. The impact of changing the discount rate by 5% would result in a change to our stock-based compensation expense and net income of \$1.1 million, \$0.9 million and \$0.9 million during 2018, 2017 and 2016, respectively.

Quantitative and Qualitative Disclosures about Market Risk

We use derivative instruments to hedge interest rate risk related to our floating rate borrowings. However, our use of these instruments exposes us to credit risk from the potential inability of our counterparties to perform under the terms of those agreements. We attempt to minimize this credit risk by contracting with a variety of high-quality financial counterparties. See Notes 7 and 9 to our consolidated financial statements in this Report for more information regarding our debt and derivatives. At December 31, 2018, 6.0% of our debt was unhedged floating rate debt. A fifty-basis point change in the one month USD LIBOR interest rate would result in an annual impact to our earnings (through interest expense) of \$1.3 million. We calculate interest sensitivity by multiplying the amount of unhedged floating rate debt by fifty-basis points.

In July 2017, the Financial Conduct Authority (the authority that regulates LIBOR) announced it intends to stop compelling banks to submit rates for the calculation of LIBOR after 2021. The Alternative Reference Rates Committee ("ARRC") has proposed that the Secured Overnight Financing Rate ("SOFR") is the rate that represents best practice as the alternative to USD-LIBOR for use in derivatives and other financial contracts that are currently indexed to USD-LIBOR. ARRC has proposed a paced market transition plan to SOFR from USD-LIBOR and organizations are currently working on industry wide and company specific transition plans as it relates to derivatives and cash markets exposed to USD-LIBOR. Our floating rate borrowings and derivative instruments are indexed to USD-LIBOR and we are monitoring this activity and evaluating the related risks.

Consolidated Financial Statements

Report of Management on Internal Control over Financial Reporting

The management of Douglas Emmett, Inc. is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934.

Our system of internal control is designed to provide reasonable assurance regarding the reliability of financial reporting and preparation of our financial statements for external reporting purposes in accordance with US GAAP. Our management, including the undersigned CEO and CFO, assessed the effectiveness of our internal control over financial reporting as of December 31, 2018. In conducting its assessment, management used the criteria issued by the Committee of Sponsoring Organizations of the Treadway Commission on Internal Control—Integrated Framework (2013 Framework). Based on this assessment, management concluded that, as of December 31, 2018, our internal control over financial reporting was effective based on those criteria.

Management, including our CEO and CFO, does not expect that our disclosure controls and procedures, or our internal controls will prevent all error and fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints and the benefit of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, have been detected.

The effectiveness of our internal control over financial reporting as of December 31, 2018, has been audited by Ernst & Young LLP, the independent registered public accounting firm that audited the consolidated financial statements included in this annual report, as stated in their report appearing on page 30, which expresses an unqualified opinion on the effectiveness of our internal control over financial reporting as of December 31, 2018.

/s/ JORDAN L. KAPLAN

Jordan L. Kaplan
President and CEO

/s/ MONA M. GISLER

Mona M. Gisler
CFO

February 15, 2019

Report of Independent Registered Public Accounting Firm

To the Shareholders and the Board of Directors of Douglas Emmett, Inc.

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Douglas Emmett, Inc. (the “Company”) as of December 31, 2018 and 2017, and the related consolidated statements of operations, comprehensive income, equity and cash flows for each of the three years in the period ended December 31, 2018 and the related notes (collectively referred to as the “consolidated financial statements”). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company at December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2018, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company’s internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 Framework), and our report dated February 15, 2019 expressed an unqualified opinion thereon.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company’s financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Ernst & Young LLP

We have served as the Company's auditor since 1995.

Los Angeles, California

February 15, 2019

Report of Independent Registered Public Accounting Firm

To the Shareholders and the Board of Directors of Douglas Emmett, Inc.

Opinion on Internal Control over Financial Reporting

We have audited Douglas Emmett, Inc.'s internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). In our opinion, Douglas Emmett, Inc. (the Company) maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated balance sheets of Douglas Emmett, Inc. as of December 31, 2018 and 2017 and the related consolidated statements of operations, comprehensive income, equity and cash flows for each of the three years in the period ended December 31, 2018, and the related notes and our report dated February 15, 2019 expressed an unqualified opinion thereon.

Basis for Opinion

The Company's management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Report of Management on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects.

Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control Over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Ernst & Young LLP

Los Angeles, California

February 15, 2019

Douglas Emmett, Inc.
Consolidated Balance Sheets
(In thousands, except share data)

	<u>December 31, 2018</u>	<u>December 31, 2017</u>
Assets		
Investment in real estate:		
Land	\$ 1,065,099	\$ 1,062,345
Buildings and improvements	7,995,203	7,886,201
Tenant improvements and lease intangibles	840,653	756,190
Property under development	129,753	124,472
Investment in real estate, gross	<u>10,030,708</u>	<u>9,829,208</u>
Less: accumulated depreciation and amortization	(2,246,887)	(2,012,752)
Investment in real estate, net	<u>7,783,821</u>	<u>7,816,456</u>
Cash and cash equivalents	146,227	176,645
Tenant receivables, net	4,371	2,980
Deferred rent receivables, net	124,834	106,021
Acquired lease intangible assets, net	3,251	4,293
Interest rate contract assets	73,414	60,069
Investment in unconsolidated real estate funds	111,032	107,735
Other assets	14,759	18,442
Total Assets	<u><u>\$ 8,261,709</u></u>	<u><u>\$ 8,292,641</u></u>
Liabilities		
Secured notes payable and revolving credit facility, net	\$ 4,134,030	\$ 4,117,390
Interest payable, accounts payable and deferred revenue	130,154	103,947
Security deposits	50,733	50,414
Acquired lease intangible liabilities, net	52,569	75,635
Interest rate contract liabilities	1,530	807
Dividends payable	44,263	42,399
Total liabilities	<u>4,413,279</u>	<u>4,390,592</u>
Equity		
Douglas Emmett, Inc. stockholders' equity:		
Common Stock, \$0.01 par value, 750,000,000 authorized, 170,214,809 and 169,564,927 outstanding at December 31, 2018 and December 31, 2017, respectively	1,702	1,696
Additional paid-in capital	3,282,316	3,272,539
Accumulated other comprehensive income	53,944	43,099
Accumulated deficit	(935,630)	(879,810)
Total Douglas Emmett, Inc. stockholders' equity	<u>2,402,332</u>	<u>2,437,524</u>
Noncontrolling interests	1,446,098	1,464,525
Total equity	<u>3,848,430</u>	<u>3,902,049</u>
Total Liabilities and Equity	<u><u>\$ 8,261,709</u></u>	<u><u>\$ 8,292,641</u></u>

See accompanying notes to the consolidated financial statements.

Douglas Emmett, Inc.
Consolidated Statements of Operations
(In thousands, except per share data)

	Year Ended December 31,		
	2018	2017	2016
Revenues			
Office rental			
Rental revenues and tenant recoveries	\$ 661,147	\$ 606,852	\$ 545,061
Parking and other income	116,784	108,694	100,572
Total office revenues	<u>777,931</u>	<u>715,546</u>	<u>645,633</u>
Multifamily rental			
Rental revenues	95,423	89,039	89,996
Parking and other income	7,962	7,467	6,922
Total multifamily revenues	<u>103,385</u>	<u>96,506</u>	<u>96,918</u>
Total revenues	<u>881,316</u>	<u>812,052</u>	<u>742,551</u>
Operating Expenses			
Office expenses	252,751	233,633	214,546
Multifamily expenses	28,116	24,401	23,317
General and administrative	38,641	36,234	34,957
Depreciation and amortization	309,864	276,761	248,914
Total operating expenses	<u>629,372</u>	<u>571,029</u>	<u>521,734</u>
Operating income	251,944	241,023	220,817
Other income	11,414	9,712	8,759
Other expenses	(7,472)	(7,037)	(9,477)
Income, including depreciation, from unconsolidated real estate funds	6,400	5,905	7,812
Interest expense	(133,402)	(145,176)	(146,148)
Demolition expenses	(272)	—	—
Income before gains	<u>128,612</u>	<u>104,427</u>	<u>81,763</u>
Gains on sales of investments in real estate	—	—	14,327
Net income	<u>128,612</u>	<u>104,427</u>	<u>96,090</u>
Less: Net income attributable to noncontrolling interests	(12,526)	(9,984)	(10,693)
Net income attributable to common stockholders	<u>\$ 116,086</u>	<u>\$ 94,443</u>	<u>\$ 85,397</u>
Net income attributable to common stockholders per share – basic	\$ 0.68	\$ 0.58	\$ 0.57
Net income attributable to common stockholders per share – diluted	\$ 0.68	\$ 0.58	\$ 0.55

See accompanying notes to the consolidated financial statements.

Douglas Emmett, Inc.
Consolidated Statements of Comprehensive Income
(In thousands)

	Year Ended December 31,		
	2018	2017	2016
Net income	\$ 128,612	\$ 104,427	\$ 96,090
Other comprehensive income: cash flow hedges	15,070	34,290	40,474
Comprehensive income	143,682	138,717	136,564
Less: Comprehensive income attributable to noncontrolling interests	(16,751)	(16,331)	(26,726)
Comprehensive income attributable to common stockholders	\$ 126,931	\$ 122,386	\$ 109,838

See accompanying notes to the consolidated financial statements.

Douglas Emmett, Inc.
Consolidated Statements of Equity
(In thousands, except per share data)

		Year Ended December 31,		
		2018	2017	2016
Shares of Common Stock	Beginning balance	169,565	151,530	146,919
	Conversion of OP Units	629	1,059	1,753
	Issuance of common stock	—	15,687	1,400
	Exercise of stock options	21	1,289	1,458
	Ending balance	170,215	169,565	151,530
Common Stock	Beginning balance	\$ 1,696	\$ 1,515	\$ 1,469
	Conversion of OP Units	6	11	17
	Issuance of common stock	—	157	14
	Exercise of stock options	—	13	15
	Ending balance	\$ 1,702	\$ 1,696	\$ 1,515
Additional Paid-in Capital	Beginning balance	\$ 3,272,539	\$ 2,725,157	\$ 2,706,753
	Conversion of OP Units	10,286	14,231	23,043
	Repurchase of OP Units	(59)	(6,763)	(498)
	Issuance of common stock	—	593,011	49,365
	Taxes paid on exercise of stock options	(450)	(53,097)	(53,506)
	Ending balance	\$ 3,282,316	\$ 3,272,539	\$ 2,725,157
AOCI	Beginning balance	\$ 43,099	\$ 15,156	\$ (9,285)
	Beginning balance adjustment - ASU 2017-12 adoption	211	—	—
	Cash flow hedge fair value adjustments	10,634	27,943	24,441
	Ending balance	\$ 53,944	\$ 43,099	\$ 15,156
Accumulated Deficit	Beginning balance	\$ (879,810)	\$ (820,685)	\$ (772,726)
	Beginning balance adjustment - ASU 2017-12 adoption	(211)	—	—
	Net income attributable to common stockholders	116,086	94,443	85,397
	Dividends	(171,695)	(153,568)	(133,356)
	Ending balance	\$ (935,630)	\$ (879,810)	\$ (820,685)
Noncontrolling Interests	Beginning balance	\$ 1,464,525	\$ 1,092,928	\$ 355,337
	Net income attributable to noncontrolling interests	12,526	9,984	10,693
	Cash flow hedge fair value adjustments	4,225	6,347	16,033
	Contributions	—	284,248	459,752
	Sales of equity interests in consolidated JVs	—	—	291,028
	Distributions	(52,142)	(38,101)	(35,478)
	Issuance of OP Units for acquisition of real estate	—	105,687	—
	Conversion of OP Units	(10,292)	(14,242)	(23,060)
	Repurchase of OP Units with cash	(49)	(3,341)	(328)
	Stock-based compensation	27,305	21,015	18,951
	Ending balance	\$ 1,446,098	\$ 1,464,525	\$ 1,092,928
Total Equity	Beginning balance	\$ 3,902,049	\$ 3,014,071	\$ 2,281,548
	Net income	128,612	104,427	96,090
	Cash flow hedge fair value adjustments	14,859	34,290	40,474
	Issuance of common stock, net	—	593,168	49,379
	Issuance of OP Units for acquisition of real estate	—	105,687	—
	Repurchase of OP Units with cash	(108)	(10,104)	(826)
	Taxes paid on exercise of stock options	(450)	(53,084)	(53,491)
	Contributions	—	284,248	459,752
	Sales of equity interests in consolidated JVs	—	—	291,028
	Dividends	(171,695)	(153,568)	(133,356)
	Distributions	(52,142)	(38,101)	(35,478)
	Stock-based compensation	27,305	21,015	18,951
	Ending balance	\$ 3,848,430	\$ 3,902,049	\$ 3,014,071
	Dividends declared per common share	\$ 1.01	\$ 0.94	\$ 0.89

Douglas Emmett, Inc.
Consolidated Statements of Cash Flows
(In thousands)

	Year Ended December 31,		
	2018	2017	2016
Operating Activities			
Net income	\$ 128,612	\$ 104,427	\$ 96,090
Adjustments to reconcile net income to net cash provided by operating activities:			
Income, including depreciation, from unconsolidated real estate funds	(6,400)	(5,905)	(7,812)
Gains on sales of investments in real estate	—	—	(14,327)
Depreciation and amortization	309,864	276,761	248,914
Net accretion of acquired lease intangibles	(22,025)	(18,006)	(18,198)
Straight-line rent	(18,813)	(12,855)	(13,599)
Increase in the allowance for doubtful accounts	2,154	406	422
Deferred loan costs amortized and written off	8,292	10,834	8,927
Amortization of loan premium	(205)	—	—
Non-cash market value adjustments on interest rate contracts	—	51	(196)
Amortization of stock-based compensation	22,299	18,478	17,448
Operating distributions from unconsolidated real estate funds	6,400	5,905	2,668
Change in working capital components:			
Tenant receivables	(3,545)	(1,221)	(680)
Interest payable, accounts payable and deferred revenue	1,376	24,942	10,712
Security deposits	319	4,424	7,307
Other assets	4,654	(5,544)	1,773
Net cash provided by operating activities	<u>432,982</u>	<u>402,697</u>	<u>339,449</u>
Investing Activities			
Capital expenditures for improvements to real estate	(179,062)	(108,326)	(91,826)
Capital expenditures for developments	(68,459)	(63,018)	(27,720)
Property acquisitions	—	(537,669)	(1,619,759)
Proceeds from sale of investments in real estate, net	—	—	348,203
Loan payments received from related parties	—	—	763
Acquisition of additional interests in unconsolidated real estate funds	(9,379)	(4,142)	—
Capital distributions from unconsolidated real estate funds	7,349	43,560	24,170
Net cash used in investing activities	<u>(249,551)</u>	<u>(669,595)</u>	<u>(1,366,169)</u>
Financing Activities			
Proceeds from borrowings	667,000	1,410,500	2,109,500
Repayment of borrowings	(655,326)	(1,698,544)	(1,335,580)
Loan cost payments	(2,992)	(11,442)	(24,586)
Contributions from noncontrolling interests in consolidated JVs	—	284,248	459,752
Distributions paid to noncontrolling interests	(52,142)	(38,101)	(35,478)
Dividends paid to common stockholders	(169,831)	(146,026)	(130,821)
Taxes paid on exercise of stock options	(450)	(53,084)	(53,491)
Repurchase of OP Units	(108)	(10,104)	(826)
Proceeds from issuance of common stock, net	—	593,169	49,379
Net cash (used in) provided by financing activities and restricted cash	<u>(213,849)</u>	<u>330,616</u>	<u>1,037,849</u>
(Decrease) increase in cash and cash equivalents	(30,418)	63,718	11,129
Cash and cash equivalents and restricted cash - beginning balance	176,766	113,048	101,919
Cash and cash equivalents and restricted cash - ending balance	<u>\$ 146,348</u>	<u>\$ 176,766</u>	<u>\$ 113,048</u>

Douglas Emmett, Inc.
Consolidated Statements of Cash Flows
(In thousands)

Supplemental Cash Flows Information

	Year Ended December 31,		
	2018	2017	2016
Operating Activities			
Cash paid for interest, net of capitalized interest	\$ 124,487	\$ 135,824	\$ 137,884
Capitalized interest paid	\$ 3,520	\$ 2,745	\$ 1,193
Non-cash Investing Transactions			
Accrual for real estate and development capital expenditures	\$ 24,702	\$ 3,776	\$ 7,182
Capitalized stock-based compensation for improvements to real estate and developments	\$ 5,006	\$ 2,537	\$ 1,503
Removal of fully depreciated and amortized tenant improvements and lease intangibles	\$ 75,729	\$ 53,687	\$ 146,739
Removal of fully amortized acquired lease intangible assets	\$ 1,582	\$ 414	\$ 1,306
Removal of fully accreted acquired lease intangible liabilities	\$ 15,431	\$ 5,057	\$ 56,278
Issuance of OP Units for acquisition of real estate	\$ —	\$ 105,687	\$ —
Application of deposit to acquisition of real estate	\$ —	\$ —	\$ 75,000
Non-cash Financing Transactions			
Gain recorded in AOCI - Adoption of ASU 2017-12 - consolidated derivatives	\$ 211	\$ —	\$ —
Gain recorded in AOCI - consolidated derivatives	\$ 22,723	\$ 16,512	\$ 14,192
Gain recorded in AOCI - unconsolidated Funds' derivatives (our share)	\$ 3,052	\$ 3,275	\$ 8
Assumption of term loan for acquisition of real estate	\$ —	\$ 36,460	\$ —
Dividends declared	\$ 171,695	\$ 153,568	\$ 133,356
Common stock issued in exchange for OP Units	\$ 10,292	\$ 14,242	\$ 23,060

See accompanying notes to the consolidated financial statements.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements

1. Overview

Organization and Business Description

Douglas Emmett, Inc. is a fully integrated, self-administered and self-managed REIT. We are one of the largest owners and operators of high-quality office and multifamily properties in Los Angeles County, California and Honolulu, Hawaii. Through our interest in our Operating Partnership and its subsidiaries, consolidated JVs and unconsolidated Funds, we focus on owning, acquiring, developing and managing a significant market share of top-tier office properties and premier multifamily communities in neighborhoods that possess significant supply constraints, high-end executive housing and key lifestyle amenities. The terms "us," "we" and "our" as used in the financial statements refer to Douglas Emmett, Inc. and its subsidiaries on a consolidated basis.

At December 31, 2018, our Consolidated Portfolio consisted of (i) a 16.6 million square foot office portfolio, (ii) 3,595 multifamily apartment units and (iii) fee interests in two parcels of land from which we receive rent under ground leases. We also manage and own equity interests in unconsolidated Funds which, at December 31, 2018, owned an additional 1.8 million square feet of office space. We manage our unconsolidated Funds alongside our Consolidated Portfolio, and we therefore present the statistics for our office portfolio on a Total Portfolio basis. As of December 31, 2018, our portfolio (not including two parcels of land from which we receive rent under ground leases), consisted of the following office and multifamily properties (both of which include ancillary retail space):

	Consolidated Portfolio	Total Portfolio
<u>Office</u>		
Wholly-owned properties	53	53
Consolidated JV properties	10	10
Unconsolidated Fund properties	—	8
	63	71
<u>Multifamily</u>		
Wholly-owned properties	10	10
Total	73	81

Basis of Presentation

The accompanying financial statements are the consolidated financial statements of Douglas Emmett, Inc. and its subsidiaries, including our Operating Partnership and our consolidated JVs. All significant intercompany balances and transactions have been eliminated in our consolidated financial statements. Our Operating Partnership and consolidated JVs are VIEs of which we are the primary beneficiary. As of December 31, 2018, the total consolidated assets, liabilities and equity of the VIEs was \$8.26 billion (of which \$7.78 billion related to investment in real estate), \$4.41 billion and \$3.85 billion (of which \$1.45 billion related to noncontrolling interests), respectively.

During the current reporting period, we reported our office rental revenues and tenant recoveries on a combined basis as Rental revenues and tenant recoveries in our consolidated statements of operations and we reclassified the comparable periods to conform to the current period presentation.

The accompanying financial statements have been prepared pursuant to the rules and regulations of the SEC in conformity with US GAAP as established by the FASB in the ASC. The accompanying financial statements include, in our opinion, all adjustments, consisting of normal recurring adjustments, necessary to present fairly the financial information set forth therein. Any reference to the number or class of properties, square footage, per square footage amounts, apartment units and geography, are unaudited and outside the scope of our independent registered public accounting firm's audit of our financial statements in accordance with the standards of the PCAOB.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make certain estimates that affect the reported amounts in the consolidated financial statements and accompanying notes. Actual results could differ materially from those estimates.

Investment in Real Estate

Acquisitions

We account for property acquisitions as asset acquisitions, and include the acquired properties results of operations in our results of operations from the respective acquisition date. We allocate the purchase price, which includes the capitalized transaction costs, to: (i) land, (ii) buildings and improvements, (iii) tenant improvements and identifiable intangible assets such as in-place at-market leases, (iv) acquired above- and below-market ground and tenant leases (including for renewal options), and if applicable (v) assumed debt, based upon our estimates of expected future cash flows and other valuation techniques. Our estimates are based upon expected future cash flows and other valuation techniques. We estimate the relative fair values of the tangible assets on an “as-if-vacant” basis. The estimated relative fair value of acquired in-place at-market leases are the estimated costs to lease the property to the occupancy level at the date of acquisition, including the fair value of leasing commissions and legal costs. We evaluate the time period over which we expect such occupancy level to be achieved and include an estimate of the net operating costs (primarily real estate taxes, insurance and utilities) incurred during the lease-up period. Above- and below-market ground and tenant leases are recorded as an asset or liability based on the present value (using an interest rate which reflects the risks associated with the leases acquired) of the difference between the contractual amounts to be paid or received pursuant to the in-place ground or tenant leases, respectively, and our estimate of the fair market rental rates for the corresponding in-place leases, over the remaining non-cancelable term of the lease. Assumed debt is recorded at fair value based upon the present value of the expected future payments. See Note 3 for our property acquisition disclosures.

Depreciation

Buildings and improvements are depreciated on a straight-line basis using an estimated life of forty years for buildings and fifteen years for improvements, and are carried on our balance sheet, offset by the related accumulated depreciation and any impairment charges, until they are sold. Tenant improvements are depreciated on a straight-line basis over the life of the related lease, with any remaining balance depreciated in the period of any early lease termination. Acquired in-place leases are amortized on a straight line basis over the weighted average remaining term of the acquired in-place leases, and are carried on our balance sheet, offset by the related accumulated amortization, until the related building is either sold or impaired. Lease intangibles are amortized on a straight-line basis over the related lease term, with any remaining balance amortized in the period of any early lease termination. Acquired above- and below-market tenant leases are amortized/accreted on a straight line basis over the life of the related lease and recorded as either an increase (for below-market leases) or a decrease (for above-market leases) to rental revenue. Acquired above- and below-market ground leases, from which we earn ground rent income, are amortized/accreted on a straight line basis over the life of the related lease and recorded either as an increase (for below-market leases) or a decrease (for above-market leases) to rental revenue. Acquired above- and below-market ground leases, for which we incur ground rent expense, are accreted/ amortized over the life of the related lease and recorded either as an increase (for below-market leases) or a decrease (for above-market leases) to expense. We accelerate depreciation for affected assets when we renovate our buildings or existing buildings are impacted by new developments. When assets are sold or retired, their cost and related accumulated depreciation or amortization are removed from our balance sheet with the resulting gains or losses, if any, reflected in our results of operations for the respective period.

Real Estate Held for Sale

Properties are classified as held for sale in our consolidated balance sheets when they meet certain requirements, including the approval of the sale of the property, the marketing of the property for sale, and our expectation that the sale will likely occur within the next 12 months. Properties classified as held for sale are carried at the lower of their carrying value or fair value less costs to sell, and we also cease to depreciate the property. As of December 31, 2018 and 2017, we did not have any properties held for sale.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

Dispositions

Recognition of gains or losses from sales of investments in real estate requires that we meet certain revenue recognition criteria and transfer control of the real estate to the buyer. The gain or loss recorded is measured as the difference between the sales price, less costs to sell, and the carrying value of the real estate when we sell it. See Note 3 for our property disposition disclosures.

Cost capitalization

Costs incurred during the period of construction of real estate are capitalized. Cost capitalization of development and redevelopment activities begins during the predevelopment period, which we define as the activities that are necessary to begin the development of the property. We cease capitalization upon substantial completion of the project, but no later than one year from cessation of major construction activity. We also cease capitalization when activities necessary to prepare the property for its intended use have been suspended. Capitalized costs are included in Property under development in our consolidated balance sheets. Once major construction activity has ceased and the development or redevelopment property is in the lease-up phase, the capitalized costs are transferred to (i) Land, (ii) Building and improvements and (iii) Tenant improvements and lease intangibles on our consolidated balance sheets as the historical cost of the property. Demolition expenses and repairs and maintenance are recorded as expense when incurred. During 2018, 2017 and 2016, we capitalized \$78.7 million, \$66.0 million and \$31.6 million of costs related to our developments, respectively, which included \$3.5 million, \$2.7 million and \$1.2 million of capitalized interest, respectively.

Investment in Unconsolidated Real Estate Funds

We manage and hold equity interests in three Funds: Fund X, Partnership X and the Opportunity Fund. As of December 31, 2018, we held direct and indirect equity interests of 71.3% of Fund X, 24.5% of Partnership X and 6.2% of the Opportunity Fund. We account for our investments in the Funds using the equity method because we have significant influence but not control over the Funds, and our Funds do not qualify as VIEs. Our investment balance includes our share of the net assets of the combined Funds, acquisition basis difference, additional basis for capital raising costs, our share of our Funds' accumulated other comprehensive income (loss) related to our Funds' derivatives, and notes receivable from our Funds. As of December 31, 2018 and 2017, the total basis difference was \$2.2 million and \$2.9 million, respectively. See Note 5 for our Fund disclosures.

Impairment of Long-Lived Assets

We periodically assess whether there has been any impairment in the carrying value of our properties and whenever events or changes in circumstances indicate that the carrying value of a property may not be recoverable. An impairment charge would be recorded if events or changes in circumstances indicate that a decline in the fair value below the carrying value has occurred and the decline is other-than-temporary. Recoverability of the carrying value of our properties is measured by a comparison of the carrying value to the undiscounted future cash flows expected to be generated by the property. If the carrying value exceeds the estimated undiscounted future cash flows, an impairment loss is recorded equal to the difference between the property's carrying value and its fair value based on the estimated discounted future cash flows. We also perform a similar periodic assessment for our investments in our Funds. Based upon such periodic assessments, no impairments occurred during 2018, 2017 or 2016.

Cash and Cash Equivalents

We consider short-term investments with maturities of three months or less when purchased to be cash equivalents.

Revenue Recognition

Rental revenues and tenant recoveries from tenant leases are included in Rental revenues and tenant recoveries in the consolidated statements of operations. All of our tenant leases are classified as operating leases. For lease terms exceeding one year, rental income is recognized on a straight-line basis over the lease term. Deferred rent receivables represent rental revenue recognized on a straight-line basis in excess of billed rents. If a lease is canceled then the deferred rent is recognized over the new remaining lease term. We recognized straight line rent of \$18.8 million, \$12.9 million and \$13.6 million during 2018, 2017 and 2016, respectively. Rental revenue from month-to-month leases or leases with no scheduled rent increases or other adjustments is recognized on a monthly basis when earned.

Lease termination fees, which are included in Rental revenues and tenant recoveries in the consolidated statements of operations, are recognized on a straight line basis over the new remaining lease term when the related lease is canceled. We recognized lease termination revenue of \$1.6 million, \$2.1 million and \$2.4 million during 2018, 2017 and 2016, respectively.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

Tenant improvements constructed, and owned by us, and reimbursed by tenants are recorded as our assets, and the related revenue, which are included in Rental revenues and tenant recoveries in the consolidated statements of operations, is recognized over the related lease term. We recognized revenue for leasehold improvements of \$3.5 million, \$2.6 million and \$2.6 million during 2018, 2017 and 2016, respectively.

Estimated tenant recoveries for real estate taxes, common area maintenance and other recoverable operating expenses, which are included in Rental revenues and tenant recoveries in the consolidated statements of operations, are recognized as revenue on a gross basis in the period that the recoverable expenses are incurred. Subsequent to year-end, we perform reconciliations on a lease-by-lease basis and bill or credit each tenant for any differences between the estimated expenses we billed to the tenant and the actual expenses incurred.

Office parking revenues, which are included in office Parking and other income in our consolidated statements of operations, are within the scope of Topic 606 (Revenue from Contracts with Customers), which we adopted in the first quarter of 2018 on a prospective basis. See "Adopted ASUs" further below. The lease contracts generally make a specified number of parking spaces available to the tenant, and we bill and recognize parking revenues on a monthly basis in accordance with the lease agreements generally using the monthly parking rates in effect at the time of billing. Office parking revenues were \$102.5 million, \$96.2 million and \$88.8 million for the years ended December 31, 2018, 2017 and 2016, respectively. Office parking receivables were \$1.1 million and \$1.0 million as of December 31, 2018 and 2017, respectively, and are included in Tenant receivables in our consolidated balance sheets.

Allowances for Tenant Receivables and Deferred Rent Receivables

We present our tenant receivables and deferred rent receivables net of allowances on our consolidated balance sheets. Tenant receivables consist primarily of amounts due for contractual lease payments and reimbursements of common area maintenance expenses, property taxes, and other costs recoverable from tenants. Deferred rent receivables represent the amount by which the cumulative straight-line rental revenue recorded to date exceeds the cumulative cash rents billed to date under the lease agreement. We consider many factors when evaluating the level of allowances necessary, including evaluations of individual tenant receivables, historical loss activity, current economic conditions and other relevant factors. We generally obtain letters of credit or security deposits from our tenants. The table below presents our allowances and security obtained from our tenants:

(In thousands)	December 31, 2018	December 31, 2017
Allowance for tenant receivables	\$ 5,215	\$ 3,062
Allowance for deferred rent receivables	\$ 2,849	\$ 3,405
Letters of credit from our tenants	\$ 27,749	\$ 25,212
Cash security deposits from our tenants	\$ 50,733	\$ 50,414

The table below presents the impact of the changes in our allowances on our results of operations:

(In thousands)	Year Ended December 31,		
	2018	2017	2016
Tenant receivables allowance - decrease in net income	\$ (2,154)	\$ (406)	\$ (422)
Deferred rent receivables allowance - increase in net income	\$ 556	\$ 1,739	\$ 898

Insurance Recoveries

Insurance recoveries related to property damage are recorded as other income when payment is either received or receipt is determined to be probable.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

Interest Income

Interest income from our short-term money market fund investments is recognized on an accrual basis. Interest income is included in other income in the consolidated statements of operations.

Loan Costs

Loan costs incurred directly with the issuance of secured notes payable and revolving credit facilities are deferred and amortized to interest expense over the respective loan or credit facility term. Any unamortized amounts are written off upon early repayment of the secured notes payable, and the related cost and accumulated amortization are removed from our balance sheet.

To the extent that a refinancing is considered an exchange of debt with the same lender, we account for loan costs based upon whether the old debt is determined to be modified or extinguished for accounting purposes. If the old debt is determined to be modified then we (i) continue to defer and amortize any unamortized deferred loan costs associated with the old debt at the time of the modification over the new term of the modified debt, (ii) defer and amortize the lender costs incurred in connection with the modification over the new term of the modified debt, and (iii) expense all other costs associated with the modification. If the old debt is determined to be extinguished then we (i) write off any unamortized deferred loan costs associated with the extinguished debt at the time of the extinguishment and remove the related cost and accumulated amortization from our balance sheet, (ii) expense all lender costs associated with the extinguishment, and (iii) defer and amortize all other costs incurred directly in connection with the extinguishment over the term of the new debt.

In circumstances where we modify or exchange our revolving credit facility with the same lender, we account for the loan costs based upon whether the borrowing capacity of the new arrangement is (a) equal to or greater than the borrowing capacity of the old arrangement, or (b) less than the borrowing capacity of the old arrangement (borrowing capacity is defined as the product of the remaining term and the maximum available credit). If the borrowing capacity of the new arrangement is greater than or equal to the borrowing capacity of the old arrangement, then we (i) continue to defer and amortize the unamortized deferred loan costs from the old arrangement over the term of the new arrangement and (ii) defer all lender and other costs incurred directly in connection with the new arrangement over the term of the new arrangement. If the borrowing capacity of the new arrangement is less than the borrowing capacity of the old arrangement, then we (i) write off any unamortized deferred loan costs at the time of the transaction related to the old arrangement in proportion to the decrease in the borrowing capacity of the old arrangement and (ii) defer all lender and other costs incurred directly in connection with the new arrangement over the term of the new arrangement.

Deferred loan costs are presented on the balance sheet as a deduction from the carrying amount of our secured notes payable and revolving credit facility. All loan costs expensed and deferred loan costs amortized are included in interest expense in our consolidated statements of operations. See Note 7 for our loan cost disclosures.

Debt Discounts and Premiums

Debt discounts and premiums related to recording debt assumed in connection with property acquisitions at fair value are generally amortized and accreted, respectively, on a straight-line basis over the remaining term of the related loan, which approximates the effective interest method. The amortization/accretion is included in interest expense in our consolidated statements of operations.

Derivative Contracts

We make use of interest rate swap and cap contracts to manage the risk associated with changes in interest rates on our floating-rate debt. When we enter into a floating-rate term loan, we generally enter into an interest rate swap agreement for the equivalent principal amount, for a period covering the majority of the loan term, which effectively converts our floating-rate debt to a fixed-rate basis during that time. In limited instances, we also make use of interest rate caps to limit our exposure to interest rate increases on our floating-rate debt. We do not speculate in derivatives and we do not make use of any other derivative instruments.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

We adopted ASU No. 2017-12 on a prospective basis in the first quarter of 2018 - see "Adopted ASUs" further below. When entering into derivative agreements, we generally elect to designate them as cash flow hedges for accounting purposes. Changes in fair value of hedging instruments designated as cash flow hedges are recorded in accumulated other comprehensive income (loss) (AOCI), which is a component of equity outside of earnings. For our Funds' hedging instruments designated as cash flow hedges, we record our share of the changes in fair value of the hedging instrument in AOCI. Amounts recorded in AOCI related to our designated hedges are reclassified to interest expense as interest payments are made on the hedged floating rate debt. Amounts reported in AOCI related to our Funds' hedges are reclassified to income, including depreciation, from unconsolidated real estate funds, as interest payments are made by our Funds on their hedged floating rate debt. Changes in fair value of hedging instruments not designated as cash flow hedges are recorded as interest expense.

We present our derivatives on the balance sheet at fair value on a gross basis. Our share of the fair value of our Funds' derivatives is included in our investment in unconsolidated real estate funds on our consolidated balance sheet. See Note 9 for our derivative disclosures.

Stock-Based Compensation

We account for stock-based compensation, including stock options and LTIP Units, using the fair value method of accounting. The estimated fair value of stock options and LTIP Units is amortized over the vesting period, which is based upon service. See Note 12 for our stock-based compensation disclosures.

EPS

We calculate basic EPS by dividing the net income attributable to common stockholders for the period by the weighted average number of common shares outstanding during the respective period. We calculate diluted EPS by dividing the net income attributable to common stockholders for the period by the weighted average number of common shares and dilutive instruments outstanding during the respective period using the treasury stock method. Unvested LTIP Units contain non-forfeitable rights to dividends and we account for them as participating securities and include them in the computation of basic and diluted EPS using the two-class method. See Note 11 for our EPS disclosures.

Segment Information

Segment information is prepared on the same basis that our management reviews information for operational decision-making purposes. We operate two business segments: the acquisition, development, ownership and management of office real estate, and the acquisition, development, ownership and management of multifamily real estate. The services for our office segment include primarily rental of office space and other tenant services, including parking and storage space rental. The services for our multifamily segment include primarily rental of apartments and other tenant services, including parking and storage space rental. See Note 14 for our segment disclosures.

Income Taxes

We have elected to be taxed as a REIT under the Code, commencing with our initial taxable year ended December 31, 2006. To qualify as a REIT, we are required (among other things) to distribute at least 90% of our REIT taxable income to our stockholders and meet various other requirements imposed by the Code relating to matters such as operating results, asset holdings, distribution levels and diversity of stock ownership. Provided that we qualify for taxation as a REIT, we are generally not subject to corporate-level income tax on the earnings distributed currently to our stockholders that we derive from our REIT qualifying activities. If we fail to qualify as a REIT in any taxable year, and are unable to avail ourselves of certain savings provisions set forth in the Code, all of our taxable income would be subject to federal income tax at regular corporate rates, including any applicable alternative minimum tax for taxable years prior to 2018. We have elected to treat several of our subsidiaries as TRSs, which generally may engage in any business, including the provision of customary or non-customary services to our tenants. A TRS is treated as a regular corporation and is subject to federal income tax and applicable state income and franchise taxes at regular corporate rates. Our TRSs did not have significant tax provisions or deferred income tax items for 2018, 2017 or 2016. Our subsidiaries (other than our TRS), including our Operating Partnership, are partnerships, disregarded entities, QRSs or REITs, as applicable, for federal income tax purposes. Under applicable federal and state income tax rules, the allocated share of net income or loss from disregarded entities or flow-through entities is reportable in the income tax returns of the respective owners. Accordingly, no income tax provision is included in our consolidated financial statements for these entities.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

New Accounting Pronouncements

Changes to GAAP are implemented by the FASB in the form of ASUs. We consider the applicability and impact of all ASUs. Other than the ASUs discussed below, the FASB has not issued any other ASUs during 2018 that we expect to be applicable and have a material impact on our financial statements.

Adopted ASUs

During 2018 we adopted the ASUs listed below:

Revenue from Contracts with Customers

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers" (Topic 606), which provides guidance for the accounting of revenue from contracts with customers, and supersedes Topic 605, "Revenue Recognition", and most industry-specific guidance throughout the industry topics of the Codification. In March 2016, the FASB issued ASU No. 2016-08, "Principal versus Agent Considerations (Reporting Revenue Gross versus Net)", which amends Topic 606 and clarifies the guidance for principal versus agent considerations. In April 2016, the FASB issued ASU No. 2016-10, "Identifying Performance Obligations and Licensing" which amends Topic 606 and provides guidance for identifying performance obligations and licensing. In May 2016, the FASB issued ASU No. 2016-12, "Narrow-Scope Improvements and Practical Expedients" which amends Topic 606 and provides guidance for a variety of revenue recognition related topics. In February 2017, the FASB issued ASU No. 2017-05 "Other Income - Gains and Losses from the Derecognition of Nonfinancial Assets" (Subtopic 610-20), which provides guidance for recognizing gains and losses from the transfer of nonfinancial assets in contracts with non-customers. Sales of real estate are now accounted for under Subtopic 610-20 which focuses on a transfer of control. The amendments in these ASUs were effective in the first quarter of 2018 and were required to be applied on a retrospective basis. We adopted the ASU in the first quarter of 2018 and it did not have a material impact on our financial statements. Most of our revenues are derived from lease contracts with tenants and are not within the scope of the respective ASUs. Although our office parking revenues are within the scope of the respective ASUs, the timing and pattern of revenue recognition was not impacted.

Derivatives and Hedging

In August 2017, the FASB issued ASU No. 2017-12, "Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities". The ASU requires the entire change in the fair value of the hedging instrument included in the assessment of hedge effectiveness be recorded in other comprehensive income. GAAP historically provided special hedge accounting only for the portion of the hedge deemed to be "highly effective" and requires an entity to separately reflect the amount by which the hedging instrument does not offset the hedged item, which is referred to as the "ineffective" amount. The amendments are effective in the first quarter of 2019 and are required to be applied on a prospective basis. We early adopted the ASU in the first quarter of 2018 and it did not have a material impact on our financial statements. The ASU requires the cumulative effect of initially applying the ASU as an adjustment to AOCI with a corresponding adjustment to the opening balance of retained earnings as of the beginning of the fiscal year in which the ASU is adopted. On January 1, 2018, we recorded such an adjustment to AOCI and accumulated deficit of \$211 thousand. See Note 10.

ASUs Not Yet Adopted

Leases

In February 2016, the FASB issued ASU No. 2016-02, "Leases" (Topic 842). The primary difference between Topic 842 and current GAAP is the recognition of lease assets and liabilities on the balance sheet by lessees for leases classified as operating leases under current GAAP. The accounting applied by lessors is largely unchanged from current GAAP, for example, the vast majority of operating leases will remain classified as operating leases, and lessors will continue to recognize lease income for those leases on a straight-line basis over the lease term. Topic 842 requires separation of the lease from the non-lease components (for example, maintenance services or other activities that transfer a good or service to the customer) in a contract. Only the lease components should be accounted for in accordance with Topic 842. The consideration in the contract is allocated to the lease and non-lease components on a relative standalone selling price basis and the non-lease component would be accounted for in accordance with ASC 606 ("Revenue from Contracts with Customers"). In July 2018, the FASB issued ASU No. 2018-11 which includes an optional practical expedient for lessors to elect, by class of underlying asset, to not separate the lease from the non-lease components if certain criteria are met. Based on our preliminary assessment, we expect that operating leases for which we are the lessor will qualify for the single component presentation, and we therefore expect to elect adoption of this practical expedient.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

Topic 842 defines initial direct costs of a lease (which we have historically capitalized) as costs that would not have been incurred had the lease not been executed. Costs to negotiate a lease that would have been incurred regardless of whether the lease was executed, such as employee salaries, are not considered to be initial direct costs, and may not be capitalized. We capitalized \$7.9 million of leasing costs during the year ended December 31, 2018 that would not qualify as initial direct costs and would be expensed under Topic 842. The expensing of those costs, adjusted for amortization expense, would have reduced net income attributable to common stockholders by \$6.0 million for the year ended December 31, 2018.

We pay rent under a ground lease which expires on December 31, 2086. See Note 16 for more information regarding this ground lease. We currently account for the lease as an operating lease. We expect to recognize a right-of-use asset and lease liability for this ground lease in the first quarter of 2019 when we adopt the ASU. We do not expect the change in accounting for the ground lease to have a material impact on our financial position or results of operations.

The treatment of our revenues could be impacted by Topic 842, however, we do not expect any impact to be material to our financial statements.

In December 2018, the FASB issued ASU 2018-20, an update to ASC Topic 842, *Leases*, which provides guidance on accounting for sales and other similar taxes collected from lessees, certain lessor costs, and recognition of variable payments for contracts with lease and nonlease components. We do not expect the ASU to have a material impact on our financial statements.

The ASUs are effective in the first quarter of 2019 and are required to be adopted using either a) a modified retrospective approach which results in a cumulative adjustment to the opening balance of retained earnings (accumulated deficit) on January 1, 2017, and restatement of the amounts presented prior to January 1, 2019 for leases that existed or were entered into after January 1, 2017, the beginning of the earliest comparative period presented in the 2019 consolidated financial statements, or b) a modified retrospective transition method which results in a cumulative adjustment to the opening balance of retained earnings (accumulated deficit) on January 1, 2019 for leases that existed or were entered into prior to January 1, 2019, the effective date of the ASU. All leases entered into on or after January 1, 2019 would be accounted for as prescribed by ASC 842. ASC 842 provides a practical expedient package that allows entities to not (a) reassess whether any expired or existing contracts are considered or contain leases; (b) reassess the lease classification for any expired or existing leases; and (c) reassess initial direct costs for any existing leases. The Company plans to elect the modified retrospective transition method for adoption on January 1, 2019 and expects to elect the use of the practical expedient package described above. We plan to adopt the ASUs in the first quarter of 2019.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

3. Investment in Real Estate

We account for our property acquisitions as asset acquisitions. Prior to January 1, 2017, we accounted for our property acquisitions as business combinations. The acquired properties results of operations are included in our results of operations from the respective acquisition dates.

2018 Acquisitions

During 2018, we did not purchase any properties.

2017 Acquisitions

During 2017, (i) a consolidated JV that we manage and in which we own an equity interest acquired three Class A office properties (1299 Ocean Avenue, 429 Santa Monica Boulevard and 9665 Wilshire Boulevard), for which investors contributed \$284.0 million directly to the JV, and (ii) we acquired one wholly-owned Class A office property (9401 Wilshire Boulevard). The table below summarizes the purchase price allocations for the acquisitions. The contract and purchase prices differ due to prorations and similar matters.

(In thousands)	1299 Ocean	429 Santa Monica	9665 Wilshire	9401 Wilshire ⁽¹⁾
Submarket	Santa Monica	Santa Monica	Beverly Hills	Beverly Hills
Acquisition date	April 25	April 25	July 20	December 20
Contract price	\$ 275,800	\$ 77,000	\$ 177,000	\$ 143,647
Building square footage	206	87	171	146
Investment in real estate:				
Land	\$ 22,748	\$ 4,949	\$ 5,568	\$ 6,740
Buildings and improvements	260,188	69,286	175,960	144,467
Tenant improvements and lease intangibles	5,010	3,248	1,112	7,843
Acquired above- and below-market leases, net	(10,683)	(722)	(4,339)	(11,559)
Assumed debt ⁽²⁾	—	—	—	(36,460)
Net assets and liabilities acquired	<u>\$ 277,263</u>	<u>\$ 76,761</u>	<u>\$ 178,301</u>	<u>\$ 111,031</u>

(1) We issued OP Units to the seller in connection with the acquisition of 9401 Wilshire. See Note 10 for more information.

(2) We assumed a loan from the seller in connection with the acquisition of 9401 Wilshire. At the date of acquisition, the loan had a fair value of \$36.5 million and a principal balance of \$32.3 million. See Note 7 for more information.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

2016 Acquisitions

Westwood Portfolio Acquisition

On February 29, 2016 (Acquisition Date), a consolidated JV which we manage and in which we own an equity interest acquired four Class A office properties located in Westwood, California (Westwood Portfolio) for a contract price of \$1.34 billion. As of the Acquisition Date, we had contributed sixty-percent of the equity to the JV, which was subsequently reduced to thirty-percent on May 31, 2016 (Sell Down Date) when we sold half of our ownership interest to a third party investor. The table below summarizes our purchase accounting and funding sources for the acquisition. The contract and purchase price differ due to prorrations and similar matters.

(in thousands)	Actual at Closing ⁽¹⁾	Pro Forma Sell Down Adjustments ⁽²⁾	Pro Forma
Building square footage	1,725		1,725
Use of funds:			
Land	\$ 94,996		\$ 94,996
Buildings and improvements	1,236,786		1,236,786
Tenant improvements and lease intangibles	50,439		50,439
Acquired above- and below-market leases, net ⁽³⁾	(49,708)		(49,708)
Net assets and liabilities acquired	<u>\$ 1,332,513</u>		<u>\$ 1,332,513</u>
Source of funds:			
Cash on hand ⁽⁴⁾	\$ 153,745	\$ —	\$ 153,745
Credit facility ⁽⁵⁾	290,000	(240,000)	50,000
Non-recourse term loan, net ⁽⁶⁾	568,768	—	568,768
Noncontrolling interests	320,000	240,000	560,000
Total source of funds	<u>\$ 1,332,513</u>	<u>\$ —</u>	<u>\$ 1,332,513</u>

- (1) Reflects the purchase of the Westwood Portfolio on the Acquisition Date when we contributed sixty-percent of the equity to the consolidated JV.
- (2) Reflects our sale of thirty-percent of the equity in the JV on the Sell Down Date, presented as of the Acquisition Date, treated as in-substance real estate, which reduced our ownership interest in the JV to thirty-percent. We sold the interest for the \$240.0 million we contributed plus an additional \$1.1 million to compensate us for the cost of holding the investment. We recognized a gain on the sale of \$1.1 million. We used the proceeds from the sale to pay down the balance owed on our revolving credit facility.
- (3) As of the Acquisition Date, the weighted average remaining life of the acquired above- and below-market leases was approximately 4.4 years.
- (4) Cash paid included a \$75.0 million deposit, \$67.5 million paid at closing, and \$11.2 million spent on loan costs in connection with securing the \$580.0 million term loan.
- (5) Reflects borrowings using our credit facility, which bears interest at LIBOR + 1.40%. See Note 7 for information regarding our credit facility.
- (6) Reflects 100% (not our pro rata share) of a \$580.0 million interest-only non-recourse loan, net of deferred loan costs of \$11.2 million incurred to secure the loan. The loan has a seven-year term and is secured by the Westwood Portfolio. Interest on the loan is floating at LIBOR + 1.40%, which has been effectively fixed at 2.37% per annum for five years through interest rate swaps. See Note 7 for information regarding this loan.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

The table below presents the revenues and net income attributable to common stockholders from the Westwood Portfolio included in the consolidated statement of operations from the Acquisition Date:

(in thousands)	Year Ended December 31,		
	2018	2017	2016
Total office revenues	\$ 102,398	\$ 96,106	\$ 80,464
Net income attributable to common stockholders ⁽¹⁾	\$ 6,163	\$ 6,346	\$ 2,998

(1) Excluding transaction costs, net income attributable to common stockholders was \$6.2 million, \$6.3 million and \$5.0 million for the years ended December 31, 2018, 2017 and 2016, respectively.

The table below presents the historical results of Douglas Emmett, Inc. and the Westwood Portfolio on a combined basis as if the acquisition was completed on January 1, 2016, based on our thirty-percent ownership interest and includes adjustments that give effect to events that are (i) directly attributable to the acquisition, (ii) expected to have a continuing impact on us, and (iii) are factually supportable. The pro forma reflects the hypothetical impact of the acquisition on us and does not purport to represent what our results of operations would have been had the acquisition occurred on January 1, 2016, or project the results of operations for any future period. The information does not reflect cost savings or operating synergies that may result from the acquisition or the costs to achieve any such potential cost savings or operating synergies. Transaction costs related to the acquisition have been excluded.

(in thousands, except per share information)	Year Ended December 31,	
	2016	
Pro forma revenues	\$	755,878
Pro forma net income attributable to common stockholders	\$	84,319
Pro forma net income attributable to common stockholders per share – basic	\$	0.56
Pro forma net income attributable to common stockholders per share – diluted	\$	0.55

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

Other 2016 Acquisitions

During 2016, a consolidated JV which we manage and in which we own an equity interest acquired two Class A office properties. As of July 21, 2016, we had contributed fifty-five percent of the equity to the JV, which was reduced to twenty-percent when we sold thirty-five percent to a third party investor for \$51.6 million, which included \$194 thousand to compensate us for the cost of holding the investment. We recognized a gain of \$587 thousand on the sale, which is included in Gains on sales of investments in real estate in our consolidated statements of operations. In addition to purchasing a thirty-five percent interest from us, investors contributed \$139.8 million to the JV. Including the effect of the sale of our interest, investors now hold an aggregate of eighty-percent of the capital interests in the JV. As part of the acquisitions, the JV borrowed a \$146.0 million under a three year, interest only, non-recourse loan bearing interest at LIBOR + 1.55%. The loan was secured by the acquired properties. The loan was refinanced in 2017. See Note 7. The table below summarizes the purchase accounting for the acquisitions. The contract and purchase prices differ due to prorations and similar matters.

(in thousands)	<u>12100 Wilshire</u>	<u>233 Wilshire</u>
Submarket	Brentwood	Santa Monica
Acquisition date	July 21	September 27
Contract price	\$ 225,000	\$ 139,500
Building square footage	365	129
Investment in real estate:		
Land	\$ 20,164	\$ 9,263
Buildings and improvements	199,698	126,938
Tenant improvements and lease intangibles	9,057	3,488
Acquired above- and below-market leases, net	(4,523)	(1,838)
Net assets and liabilities acquired	<u>\$ 224,396</u>	<u>\$ 137,851</u>

2016 Disposition

During 2016, we sold a 168,000 square foot Class A office property located in Sherman Oaks, California with a carrying value of \$42.8 million for a contract price of \$56.7 million, and we incurred transaction costs of \$1.2 million resulting in a net gain of \$12.7 million. The gain is included in Gains on sales of investments in real estate in our consolidated statements of operations.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

4. Acquired Lease Intangibles

Summary of our Acquired Lease Intangibles

(In thousands)	December 31, 2018	December 31, 2017
Above-market tenant leases	\$ 5,595	\$ 7,177
Above-market tenant leases - accumulated amortization	(3,289)	(3,846)
Above-market ground lease where we are the lessor	1,152	1,152
Above-market ground lease - accumulated amortization	(207)	(190)
Acquired lease intangible assets, net	<u>\$ 3,251</u>	<u>\$ 4,293</u>
Below-market tenant leases	\$ 112,175	\$ 127,606
Below-market tenant leases - accumulated accretion	(63,013)	(55,428)
Above-market ground lease where we are the tenant	4,017	4,017
Above-market ground lease - accumulated accretion	(610)	(560)
Acquired lease intangible liabilities, net	<u>\$ 52,569</u>	<u>\$ 75,635</u>

Impact on the Consolidated Statements of Operations

The table below summarizes the net amortization/accretion related to our above- and below-market leases:

(In thousands)	Year Ended December 31,		
	2018	2017	2016
Net accretion of above- and below-market tenant lease assets and liabilities ⁽¹⁾	\$ 21,992	\$ 17,973	\$ 18,165
Amortization of an above-market ground lease ⁽²⁾	(17)	(17)	(17)
Accretion of an above-market ground lease liability ⁽³⁾	50	50	50
Total	<u>\$ 22,025</u>	<u>\$ 18,006</u>	<u>\$ 18,198</u>

- (1) Recorded as a net increase to office and multifamily rental revenues.
(2) Recorded as a decrease to office parking and other income.
(3) Recorded as a decrease to office expense.

The table below presents the future net accretion related to our above- and below-market leases at December 31, 2018. The above-market ground lease liability presented in the tables above will be offset against a right of use ground lease asset on January 1, 2019 when we adopt ASU No. 2016-02 - see Note 2, and there is therefore no future accretion for that lease reflected in the table below.

Year ending December 31:	Net increase to revenues
	(In thousands)
2019	\$ 15,521
2020	12,516
2021	6,813
2022	4,157
2023	2,542
Thereafter	4,362
Total	<u>\$ 45,911</u>

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

5. Investments in Unconsolidated Real Estate Funds

Description of our Funds

We manage and own equity interests in three unconsolidated Funds, the Opportunity Fund, Fund X and Partnership X, through which we and investors own eight office properties totaling 1.8 million square feet. During the third quarter of 2018 we purchased an additional 1.9% interest in Fund X. We purchased a 3.7% interest in the Opportunity Fund during the second quarter of 2017 and 2.5% during the fourth quarter of 2017. The Opportunity Fund's only investment is a 13.1% interest in Fund X. At December 31, 2018, we held direct and indirect equity interests of 6.2% in the Opportunity Fund, 71.3% of Fund X and 24.5% of Partnership X. Our Funds pay us fees and reimburse us for certain expenses related to property management and other services we provide. We also receive distributions based on invested capital and on any profits that exceed certain specified cash returns to the investors. The table below presents cash distributions received from our Funds:

(In thousands)	Year Ended December 31,		
	2018	2017	2016
Operating distributions received	\$ 6,400	\$ 5,905	\$ 2,668
Capital distributions received	7,349	43,560	24,170
Total distributions received	<u>\$ 13,749</u>	<u>\$ 49,465</u>	<u>\$ 26,838</u>

Summarized Financial Information for our Funds

The tables below present selected financial information for the Funds on a combined basis. The amounts presented reflect 100% (not our pro-rata share) of amounts related to the Funds, and are based upon historical acquired book value:

(In thousands)	December 31, 2018	December 31, 2017
Total assets	\$ 694,713	\$ 704,186
Total liabilities	\$ 525,483	\$ 523,767
Total equity	\$ 169,230	\$ 180,419

(In thousands)	Year Ended December 31,		
	2018	2017	2016
Total revenues	\$ 79,590	\$ 75,896	\$ 73,171
Operating income	\$ 22,959	\$ 20,640	\$ 19,477
Net income	\$ 6,260	\$ 5,085	\$ 8,213

6. Other Assets

(In thousands)	December 31, 2018	December 31, 2017
Restricted cash	\$ 121	\$ 121
Prepaid expenses	7,830	9,235
Other indefinite-lived intangibles	1,988	1,988
Furniture, fixtures and equipment, net	1,101	1,155
Other	3,719	5,943
Total other assets	<u>\$ 14,759</u>	<u>\$ 18,442</u>

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

7. Secured Notes Payable and Revolving Credit Facility, Net

Description	Maturity Date ⁽¹⁾	Principal Balance as of December 31, 2018	Principal Balance as of December 31, 2017	Variable Interest Rate	Fixed Interest Rate ⁽²⁾	Swap Maturity Date
(In thousands)						
Wholly Owned Subsidiaries						
Term loan ⁽³⁾	—	\$ —	\$ 146,974	—	—	—
Term loan ⁽³⁾	—	—	280,721	—	—	—
Fannie Mae loan	10/1/2019	145,000	145,000	LIBOR + 1.25%	N/A	N/A
Term loan ⁽⁴⁾	4/15/2022	340,000	340,000	LIBOR + 1.40%	2.77%	4/1/2020
Term loan ⁽⁴⁾	7/27/2022	180,000	180,000	LIBOR + 1.45%	3.06%	7/1/2020
Term loan ⁽⁴⁾	11/1/2022	400,000	400,000	LIBOR + 1.35%	2.64%	11/1/2020
Term loan ⁽⁴⁾	6/23/2023	360,000	360,000	LIBOR + 1.55%	2.57%	7/1/2021
Term loan ⁽⁴⁾	12/23/2023	220,000	220,000	LIBOR + 1.70%	3.62%	12/23/2021
Term loan ⁽⁴⁾	1/1/2024	300,000	300,000	LIBOR + 1.55%	3.46%	1/1/2022
Term loan ⁽⁴⁾	3/3/2025	335,000	—	LIBOR + 1.30%	3.84%	3/1/2023
Fannie Mae loan ⁽⁴⁾	4/1/2025	102,400	102,400	LIBOR + 1.25%	2.84%	3/1/2020
Fannie Mae loan ⁽⁴⁾	12/1/2025	115,000	115,000	LIBOR + 1.25%	2.76%	12/1/2020
Fannie Mae loan ⁽⁴⁾	6/1/2027	550,000	550,000	LIBOR + 1.37%	3.16%	6/1/2022
Term loan ⁽⁵⁾	6/1/2038	31,582	32,213	N/A	4.55%	N/A
Revolving credit facility ⁽⁶⁾	8/21/2020	105,000	—	LIBOR + 1.40%	N/A	N/A
Total Wholly Owned Subsidiary Debt		3,183,982	3,172,308			
Consolidated JVs						
Term loan ⁽⁴⁾	2/28/2023	580,000	580,000	LIBOR + 1.40%	2.37%	3/1/2021
Term loan ⁽⁴⁾	12/19/2024	400,000	400,000	LIBOR + 1.30%	3.47%	1/1/2023
Total Consolidated Debt ⁽⁷⁾		4,163,982	4,152,308			
Unamortized loan premium, net		3,986	4,191			
Unamortized deferred loan costs, net		(33,938)	(39,109)			
Total Consolidated Debt, net		\$ 4,134,030	\$ 4,117,390			

Except as noted below, each loan (including our revolving credit facility) is non-recourse and secured by one or more separate collateral pools consisting of one or more properties, and requires monthly payments of interest only with the outstanding principal due upon maturity.

- (1) Maturity dates include the effect of extension options.
- (2) Includes the effect of interest rate swaps and excludes the effect of prepaid loan fees. See Note 9 for details of our interest rate swaps. See below for details of our loan costs.
- (3) At December 31, 2018, these loans have been paid off.
- (4) Loan agreement includes a zero-percent LIBOR floor. The corresponding swaps do not include such a floor.
- (5) Requires monthly payments of principal and interest. Principal amortization is based upon a 30-year amortization schedule.
- (6) \$400.0 million revolving credit facility. Unused commitment fees range from 0.15% to 0.20%.
- (7) See Note 13 for our fair value disclosures.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

Debt Statistics

The following table summarizes our fixed and floating rate debt:

(In thousands)	Principal Balance as of December 31, 2018	Principal Balance as of December 31, 2017
Aggregate swapped to fixed rate loans	\$ 3,882,400	\$ 3,547,400
Aggregate fixed rate loans	31,582	459,908
Aggregate floating rate loans	250,000	145,000
Total Debt	<u>\$ 4,163,982</u>	<u>\$ 4,152,308</u>

The following table summarizes certain debt statistics:

Statistics for consolidated loans with interest fixed under the terms of the loan or a swap	
Principal balance (in billions)	\$3.91
Weighted average remaining life (including extension options)	5.4 years
Weighted average remaining fixed interest period	2.6 years
Weighted average annual interest rate	3.07%

Future Principal Payments

At December 31, 2018, the minimum future principal payments due on our secured notes payable and revolving credit facility were as follows:

Year ending December 31:	Excluding Maturity Extension Options	Including Maturity Extension Options ⁽¹⁾
(In thousands)		
2019	\$ 145,718	\$ 145,718
2020	400,752	105,752
2021	787	787
2022	1,040,823	920,823
2023	1,495,862	1,160,862
Thereafter	1,080,040	1,830,040
Total future principal payments	<u>\$ 4,163,982</u>	<u>\$ 4,163,982</u>

(1) Our loan agreements generally require that we meet certain minimum financial thresholds to be able to extend the loan maturity.

Loan Costs

Deferred loan costs are net of accumulated amortization of \$24.2 million and \$18.0 million at December 31, 2018 and December 31, 2017, respectively. The table below presents loan costs, which are included in interest expense in our consolidated statements of operations:

(In thousands)	Year Ended December 31,		
	2018	2017	2016
Loan costs expensed	\$ 418	\$ 2,359	\$ 1,441
Deferred loan cost amortization	7,874	9,033	7,608
Total	<u>\$ 8,292</u>	<u>\$ 11,392</u>	<u>\$ 9,049</u>

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

8. Interest Payable, Accounts Payable and Deferred Revenue

(In thousands)	December 31, 2018	December 31, 2017
Interest payable	\$ 10,657	\$ 9,829
Accounts payable and accrued liabilities	75,111	62,741
Deferred revenue	44,386	31,377
Total interest payable, accounts payable and deferred revenue	<u>\$ 130,154</u>	<u>\$ 103,947</u>

9. Derivative Contracts

Derivative Summary

As of December 31, 2018, all of our interest rate swaps, which include the interest rate swaps of our consolidated JVs and our unconsolidated Funds, were designated as cash flow hedges:

	Number of Interest Rate Swaps	Notional (In thousands)
Consolidated derivatives ⁽¹⁾⁽³⁾	27	\$ 3,882,400
Unconsolidated Funds' derivatives ⁽²⁾⁽³⁾	4	\$ 510,000

- (1) The notional amount reflects 100%, not our pro-rata share, of our consolidated JVs' derivatives.
(2) The notional amount reflects 100%, not our pro-rata share, of our unconsolidated Funds' derivatives.
(3) See Note 13 for our derivative fair value disclosures.

Credit-risk-related Contingent Features

We have agreements with each of our interest rate swap counterparties that contain a provision under which we could also be declared in default on our derivative obligations if we default on the underlying indebtedness that we are hedging. As of December 31, 2018, there have been no events of default with respect to our interest rate swaps or our consolidated JVs' or unconsolidated Funds' interest rate swaps. We do not post collateral for our interest rate swap contract liabilities. The fair value of our interest rate swap contract liabilities, including accrued interest and excluding credit risk adjustments, were as follows:

(In thousands)	December 31, 2018	December 31, 2017
Consolidated derivatives ⁽¹⁾	\$ 1,681	\$ 915
Unconsolidated Funds' derivatives ⁽²⁾	\$ —	\$ —

- (1) Includes 100%, not our pro-rata share, of our consolidated JVs' derivatives.
(2) Our unconsolidated Funds' did not have any derivatives in a liability position.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

Counterparty Credit Risk

We are subject to credit risk from the counterparties on our interest rate swap contract assets because we do not receive collateral. We seek to minimize that risk by entering into agreements with a variety of high quality counterparties with investment grade ratings. The fair value of our interest rate swap contract assets, including accrued interest and excluding credit risk adjustments, were as follows:

(In thousands)	December 31, 2018		December 31, 2017	
Consolidated derivatives ⁽¹⁾	\$	76,021	\$	60,093
Unconsolidated Funds' derivatives ⁽²⁾	\$	12,576	\$	9,350

(1) Includes 100%, not our pro-rata share, of our consolidated JVs' derivatives.

(2) The amounts reflect 100%, not our pro-rata share, of our unconsolidated Funds' derivatives.

Impact of Hedges on AOCI and the Consolidated Statements of Operations

The table below presents the effect of our derivatives on our AOCI and the consolidated statements of operations:

(In thousands)	Year Ended December 31,		
	2018	2017	2016
Derivatives Designated as Cash Flow Hedges:			
Consolidated derivatives:			
Gain recorded in AOCI - adoption of ASU 2017-12 ⁽¹⁾⁽²⁾	\$ 211	\$ —	\$ —
Gain recorded in AOCI before reclassifications ⁽¹⁾⁽²⁾	\$ 22,723	\$ 16,512	\$ 14,192
(Gain) loss reclassified from AOCI to Interest Expense ⁽¹⁾	\$ (10,103)	\$ 13,976	\$ 25,917
Interest Expense presented in the consolidated statements of operations	\$ (133,402)	\$ (145,176)	\$ (146,148)
(Gain) loss related to ineffectiveness recorded in Interest Expense	\$ —	\$ 51	\$ (196)
Unconsolidated Funds' derivatives (our share)⁽³⁾:			
Gain recorded in AOCI before reclassifications ⁽¹⁾	\$ 3,052	\$ 3,275	\$ 8
(Gain) loss reclassified from AOCI to Income, including depreciation, from unconsolidated real estate funds ⁽¹⁾	\$ (813)	\$ 527	\$ 357
Income, including depreciation, from unconsolidated real estate funds presented in the consolidated statements of operations	\$ 6,400	\$ 5,905	\$ 7,812

(1) See Note 10 for our AOCI reconciliation.

(2) See Note 2 regarding the ASU adoption.

(3) We calculate our share by multiplying the total amount for each Fund by our equity interest in the respective Fund.

Future Reclassifications from AOCI

At December 31, 2018, our estimate of the AOCI related to derivatives designated as cash flow hedges, that will be reclassified to earnings during the next year as interest rate swap payments are made, is as follows:

(In thousands)	
Consolidated derivatives:	
Gains to be reclassified from AOCI to Interest Expense	\$ 36,161
Unconsolidated Funds' derivatives (our share):	
Gains to be reclassified from AOCI to Income, including depreciation, from unconsolidated real estate funds	\$ 2,565

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

10. Equity

Transactions

2018 Transactions

During 2018, we (i) acquired 629 thousand OP Units in exchange for issuing an equal number of shares of our common stock to the holders of the OP Units, (ii) acquired 3 thousand OP Units for \$108 thousand in cash and (iii) issued 21 thousand shares of our common stock for the exercise of 49 thousand stock options on a net settlement basis (net of the exercise price and related taxes).

2017 Transactions

During 2017, we or our Operating Partnership, (i) acquired 1.1 million OP Units in exchange for issuing an equal number of shares of our common stock to the holders of the OP Units, (ii) issued 1.3 million shares of our common stock for the exercise of 3.9 million stock options on a net settlement basis (net of the exercise price and related taxes), (iii) issued 15.7 million shares of our common stock under our ATM program for net proceeds of \$593.3 million, and (iv) issued 2.6 million OP Units valued at \$105.7 million in connection with the acquisition of the 9401 Wilshire office property, of which we subsequently acquired 248 thousand OP Units for \$10.1 million in cash. One of our JVs acquired three office properties, 1299 Ocean Avenue, 429 Santa Monica and 9665 Wilshire, for which investors contributed \$284.0 million directly to the JV.

2016 Transactions

During 2016 we (i) acquired 1.8 million OP Units in exchange for issuing an equal number of shares of our common stock to the holders of OP Units, (ii) acquired 25 thousand OP Units for \$826 thousand in cash, (iii) issued 1.5 million shares of our common stock for the exercise of 7.6 million stock options on a net settlement basis (net of the exercise price and related taxes), (iv) issued 1.4 million shares of our common stock under our ATM program for net proceeds of 49.4 million.

We also created two JVs to acquire various properties: (i) in the JV which acquired the Westwood Portfolio, investors acquired an aggregate of seventy-percent of the capital interests, as a result of contributing \$320 million directly to the JV for a forty-percent interest and acquiring a thirty-percent interest from us for \$241.1 million, (resulting in a gain of \$1.1 million), and (ii) in the second JV, which acquired two office properties, 12100 Wilshire and 233 Wilshire, investors acquired an aggregate of eighty-percent of the capital interests, as a result of contributing \$139.8 million directly to the JV and acquiring a thirty-five-percent interest from us for \$51.6 million (resulting in a gain of \$587 thousand).

Noncontrolling Interests

Our noncontrolling interests consist of interests in our Operating Partnership and consolidated JVs which are not owned by us. Noncontrolling interests in our Operating Partnership consist of OP Units and fully-vested LTIP Units, and represented approximately 14% of our Operating Partnership's total interests as of December 31, 2018 when we and our Operating Partnership had 170.2 million shares of common stock and 28.2 million OP Units and fully-vested LTIP Units outstanding. A share of our common stock, an OP Unit and an LTIP Unit (once vested and booked up) have essentially the same economic characteristics, sharing equally in the distributions from our Operating Partnership. Investors who own OP Units have the right to cause our Operating Partnership to acquire their OP Units for an amount of cash per unit equal to the market value of one share of our common stock at the date of acquisition, or, at our election, exchange their OP Units for shares of our common stock on a one-for-one basis. LTIP Units have been granted to our key employees and non-employee directors as part of their compensation, see Note 12.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

Changes in our Ownership Interest in our Operating Partnership

The table below presents the effect on our equity from net income attributable to common stockholders and changes in our ownership interest in our Operating Partnership:

(In thousands)	Year Ended December 31,		
	2018	2017	2016
Net income attributable to common stockholders	\$ 116,086	\$ 94,443	\$ 85,397
Transfers from noncontrolling interests:			
Exchange of OP Units with noncontrolling interests	10,292	14,242	23,060
Repurchase of OP Units from noncontrolling interests	(59)	(6,764)	(498)
Net transfers from noncontrolling interests	10,233	7,478	22,562
Change from net income attributable to common stockholders and transfers from noncontrolling interests	\$ 126,319	\$ 101,921	\$ 107,959

AOCI Reconciliation⁽¹⁾

The table below presents a reconciliation of our AOCI, which consists solely of adjustments related to derivatives designated as cash flow hedges:

(In thousands)	Year Ended December 31,		
	2018	2017	2016
Beginning balance	\$ 43,099	\$ 15,156	\$ (9,285)
Adoption of ASU 2017-12 - cumulative opening balance adjustment ⁽²⁾	211	—	—
Consolidated derivatives:			
Other comprehensive income before reclassifications	22,723	16,512	14,192
Reclassification of (gains) losses from AOCI to Interest Expense	(10,103)	13,976	25,917
Unconsolidated Funds' derivatives (our share):			
Other comprehensive income before reclassifications	3,052	3,275	8
Reclassification of (gains) losses from AOCI to Income, including depreciation, from unconsolidated real estate funds	(813)	527	357
Net current period OCI	15,070	34,290	40,474
OCI attributable to noncontrolling interests	(4,225)	(6,347)	(16,033)
OCI attributable to common stockholders	10,845	27,943	24,441
Ending balance	\$ 53,944	\$ 43,099	\$ 15,156

(1) See Note 9 for the details of our derivatives and Note 13 for our derivative fair value disclosures.

(2) See Note 2 regarding our adoption of the ASU on January 1, 2018.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

Dividends (unaudited)

Our common stock dividends paid during 2018 are classified for federal income tax purposes as follows:

Record Date	Paid Date	Dividend Per Share	Ordinary Income Percentage	Capital Gain Percentage	Return of Capital Percentage	Amount Qualifying as a Section 199A Dividend
12/29/2017	1/15/2018	\$ 0.25	24.7%	—%	75.3%	24.7%
3/29/2018	4/17/2018	0.25	24.7%	—%	75.3%	24.7%
6/29/2018	7/13/2018	0.25	24.7%	—%	75.3%	24.7%
9/28/2018	10/16/2018	0.25	24.7%	—%	75.3%	24.7%
Total / Weighted Average		\$ 1.00	24.7%	—%	75.3%	24.7%

11. EPS

The table below presents the calculation of basic and diluted EPS:

	Year Ended December 31,		
	2018	2017	2016
Numerator (In thousands):			
Net income attributable to common stockholders	\$ 116,086	\$ 94,443	\$ 85,397
Allocation to participating securities: Unvested LTIP Units	(546)	(626)	(468)
Numerator for basic and diluted net income attributable to common stockholders	<u>\$ 115,540</u>	<u>\$ 93,817</u>	<u>\$ 84,929</u>
Denominator (In thousands):			
Weighted average shares of common stock outstanding - basic	169,893	160,905	149,299
Effect of dilutive securities: Stock options ⁽¹⁾	9	325	3,891
Weighted average shares of common stock and common stock equivalents outstanding - diluted	<u>169,902</u>	<u>161,230</u>	<u>153,190</u>
Basic EPS:			
Net income attributable to common stockholders per share	\$ 0.68	\$ 0.58	\$ 0.57
Diluted EPS:			
Net income attributable to common stockholders per share	\$ 0.68	\$ 0.58	\$ 0.55

(1) The following securities were excluded from the calculation of diluted EPS because including them would be anti-dilutive to the calculation:

(In thousands)	Year Ended December 31,		
	2018	2017	2016
OP Units	26,661	24,810	25,110
Vested LTIP Units	813	274	578

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

12. Stock-Based Compensation

2016 Omnibus Stock Incentive Plan

The Douglas Emmett, Inc. 2016 Omnibus Stock Incentive Plan, our stock incentive plan (our "2016 Plan"), permits us to make grants of incentive stock options, non-qualified stock options, stock appreciation rights, deferred stock awards, restricted stock awards, dividend equivalent rights and other stock-based awards. We had an aggregate of 3.4 million shares available for grant as of December 31, 2018. Awards such as LTIP Units, deferred stock and restricted stock, which deliver the full value of the underlying shares, are counted against the Plan limits as two shares. Awards such as stock options and stock appreciation rights are counted as one share. The number of shares reserved under our 2016 Plan is also subject to adjustment in the event of a stock split, stock dividend or other change in our capitalization. Shares of stock underlying any awards that are forfeited, canceled or otherwise terminated (other than by exercise) are added back to the shares of stock available for future issuance under the 2016 Plan. For options exercised, our policy is to issue common stock on a net settlement basis - net of the exercise price and related taxes.

Until it expired in 2016, we made grants under our 2006 Omnibus Stock Incentive Plan (our "2006 Plan"), which was substantially similar to our 2016 Plan. No further awards may be granted under our 2006 Plan, although awards granted under the 2006 Plan in the past and which are still outstanding will continue to be governed by the terms of our 2006 Plan.

Our 2016 and 2006 Plans (the "Plans") are administered by the compensation committee of our board of directors. The compensation committee may interpret our Plans and make all determinations necessary or desirable for the administration of our Plans. The committee has full power and authority to select the participants to whom awards will be granted, to make any combination of awards to participants, to accelerate the exercisability or vesting of any award and to determine the specific terms and conditions of each award, subject to the provisions of our 2016 Plan. All officers, employees, directors and other key personnel (including consultants and prospective employees) are eligible to participate in our 2016 Plan.

We have made certain awards in the form of a separate series of units of limited partnership interests in our Operating Partnership called LTIP Units, which can be granted either as free-standing awards or in tandem with other awards under our 2016 Plan. Our LTIP Units are valued by reference to the value of our common stock at the time of grant, and are subject to such conditions and restrictions as the compensation committee may determine, including continued employment or service, and/or achievement of pre-established performance goals, financial metrics and other objectives. Once vested, LTIP Units can generally be converted to OP Units on a one for one basis, provided our stock price increases by more than a specified hurdle.

Employee Awards

We grant stock-based compensation in the form of LTIP Units as a part of our annual incentive compensation to various employees each year, a portion which vests at the date of grant, and the remainder which vests in three equal annual installments over the three calendar years following the grant date. Compensation expense for LTIP Units which are not vested at the grant date is recognized on a straight-line basis over the requisite service period for each separately vesting portion of the award. We have also made long-term grants in the form of LTIP Units to certain employees, which generally vest in equal annual installments over four to five calendar years following the grant date, and some of these grants include a portion which vests at the date of grant. In aggregate, we granted 898 thousand, 800 thousand and 704 thousand LTIP Units to employees during 2018, 2017 and 2016, respectively.

Non-Employee Director Awards

As annual fees for their services, each of our non-employee directors receives a grant of LTIP Units that vests on a quarterly basis during the year the services are rendered, which is the calendar year following the grant date. We granted 37 thousand, 28 thousand and 35 thousand LTIP Units to our non-employee directors during 2018, 2017 and 2016, respectively.

Compensation Expense

Total stock-based compensation expense, net of capitalized amounts, was \$22.3 million, \$18.5 million and \$17.4 million during 2018, 2017 and 2016, respectively. Certain amounts of stock-based compensation expense are capitalized for employees who provide leasing and construction services. We capitalized \$5.0 million, \$2.5 million, and \$1.5 million during 2018, 2017 and 2016, respectively. At December 31, 2018, the total unrecognized stock-based compensation expense for unvested LTIP Unit awards was \$19.4 million, which will be recognized over a weighted-average term of two years.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

Stock-Based Award Activity

The table below presents our outstanding stock options activity:

Fully Vested Stock Options:	Number of Stock Options (Thousands)	Weighted Average Exercise Price	Weighted Average Remaining Contract Life (Months)	Total Intrinsic Value (Thousands)	Intrinsic Value of Options Exercised (Thousands)
Outstanding at December 31, 2015	11,535	\$ 18.04	23	\$ 151,569	
Exercised	(7,566)	\$ 20.98			\$ 104,108
Outstanding at December 31, 2016	3,969	\$ 12.43	27	\$ 95,770	
Exercised	(3,920)	\$ 12.43			\$ 102,963
Outstanding at December 31, 2017	49	\$ 12.66	16	\$ 1,375	
Exercised	(49)	\$ 12.66			\$ 1,196
Outstanding at December 31, 2018	—				

The table below presents our unvested LTIP Units activity:

Unvested LTIP Units:	Number of Units (Thousands)	Weighted Average Grant Date Fair Value	Grant Date Fair Value (Thousands)
Outstanding at December 31, 2015	1,096	\$ 19.85	
Granted	739	\$ 27.62	\$ 20,420
Vested	(778)	\$ 22.23	\$ 17,293
Forfeited	(17)	\$ 27.77	\$ 473
Outstanding at December 31, 2016	1,040	\$ 23.46	
Granted	828	\$ 29.89	\$ 24,745
Vested	(807)	\$ 25.40	\$ 20,497
Forfeited	(5)	\$ 31.36	\$ 172
Outstanding at December 31, 2017	1,056	\$ 26.98	
Granted	935	\$ 27.01	\$ 25,247
Vested	(1,036)	\$ 25.82	\$ 26,740
Forfeited	(10)	\$ 34.18	\$ 333
Outstanding at December 31, 2018	945	\$ 28.20	

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

13. Fair Value of Financial Instruments

Our estimates of the fair value of financial instruments were determined using available market information and widely used valuation methods. Considerable judgment is necessary to interpret market data and determine an estimated fair value. The use of different market assumptions or valuation methods may have a material effect on the estimated fair values. The FASB fair value framework hierarchy distinguishes between assumptions based on market data obtained from sources independent of the reporting entity, and the reporting entity's own assumptions about market-based inputs. The hierarchy is as follows:

- Level 1 - inputs utilize unadjusted quoted prices in active markets for identical assets or liabilities.
- Level 2 - inputs are observable either directly or indirectly for similar assets and liabilities in active markets.
- Level 3 - inputs are unobservable assumptions generated by the reporting entity

As of December 31, 2018, we did not have any fair value estimates of financial instruments using Level 3 inputs.

Financial instruments disclosed at fair value

Short term financial instruments: The carrying amounts for cash and cash equivalents, tenant receivables, revolving credit line, interest payable, accounts payable, security deposits and dividends payable approximate fair value because of the short-term nature of these instruments.

Secured notes payable: See Note 7 for the details of our secured notes payable. We estimate the fair value of our consolidated secured notes payable by calculating the credit-adjusted present value of the principal and interest payments for each secured note payable. The calculation incorporates observable market interest rates which we consider to be Level 2 inputs, assumes that the loans will be outstanding through maturity, and excludes any maturity extension options. The table below presents the estimated fair value and carrying value of our secured notes payable (excluding our revolving credit facility), the carrying value includes unamortized loan premium and excludes unamortized deferred loan fees:

(In thousands)	December 31, 2018	December 31, 2017
Fair value	\$ 4,087,979	\$ 4,195,489
Carrying value	\$ 4,062,968	\$ 4,156,499

Financial instruments measured at fair value

Derivative instruments: See Note 9 for the details of our derivatives. We present our derivatives on the balance sheet at fair value, on a gross basis, excluding accrued interest. We estimate the fair value of our derivative instruments by calculating the credit-adjusted present value of the expected future cash flows of each derivative. The calculation incorporates the contractual terms of the derivatives, observable market interest rates which we consider to be Level 2 inputs, and credit risk adjustments to reflect the counterparty's as well as our own nonperformance risk. Our derivatives are not subject to master netting arrangements. The table below presents the estimated fair value of our derivatives:

(In thousands)	December 31, 2018	December 31, 2017
Derivative Assets:		
Fair value - consolidated derivatives ⁽¹⁾	\$ 73,414	\$ 60,069
Fair value - unconsolidated Funds' derivatives ⁽²⁾	\$ 12,228	\$ 9,437
Derivative Liabilities:		
Fair value - consolidated derivatives ⁽¹⁾	\$ 1,530	\$ 807
Fair value - unconsolidated Funds' derivatives ⁽²⁾	\$ —	\$ —

- (1) Consolidated derivatives, which include 100%, not our pro-rata share, of our consolidated JVs' derivatives, are included in interest rate contracts in our consolidated balance sheets. The fair values exclude accrued interest which is included in interest payable in the consolidated balance sheet.
- (2) Reflects 100%, not our pro-rata share, of our unconsolidated Funds' derivatives. Our pro-rata share of the amounts related to the unconsolidated Funds' derivatives is included in our Investment in unconsolidated real estate funds in our consolidated balance sheets. See Note 17 regarding our unconsolidated Funds debt and derivatives.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

14. Segment Reporting

Segment information is prepared on the same basis that our management reviews information for operational decision-making purposes. We operate in two business segments: (i) the acquisition, development, ownership and management of office real estate and (ii) the acquisition, development, ownership and management of multifamily real estate. The services for our office segment primarily include rental of office space and other tenant services, including parking and storage space rental. The services for our multifamily segment include rental of apartments and other tenant services, including parking and storage space rental. Asset information by segment is not reported because we do not use this measure to assess performance or make decisions to allocate resources. Therefore, depreciation and amortization expense is not allocated among segments. General and administrative expenses and interest expense are not included in segment profit as our internal reporting addresses these items on a corporate level. The table below presents the operating activity of our reportable segments:

(In thousands)	Year Ended December 31,		
	2018	2017	2016
<u>Office Segment</u>			
Total office revenues	\$ 777,931	\$ 715,546	\$ 645,633
Office expenses	(252,751)	(233,633)	(214,546)
Office segment profit	525,180	481,913	431,087
<u>Multifamily Segment</u>			
Total multifamily revenues	103,385	96,506	96,918
Multifamily expenses	(28,116)	(24,401)	(23,317)
Multifamily segment profit	75,269	72,105	73,601
Total profit from all segments	\$ 600,449	\$ 554,018	\$ 504,688

The table below presents a reconciliation of the total profit from all segments to net income attributable to common stockholders:

(In thousands)	Year Ended December 31,		
	2018	2017	2016
Total profit from all segments	\$ 600,449	\$ 554,018	\$ 504,688
General and administrative	(38,641)	(36,234)	(34,957)
Depreciation and amortization	(309,864)	(276,761)	(248,914)
Other income	11,414	9,712	8,759
Other expenses	(7,472)	(7,037)	(9,477)
Income, including depreciation, from unconsolidated real estate funds	6,400	5,905	7,812
Interest expense	(133,402)	(145,176)	(146,148)
Demolition expenses	(272)	—	—
Income before gains	128,612	104,427	81,763
Gains on sales of investments in real estate	—	—	14,327
Net income	128,612	104,427	96,090
Less: Net income attributable to noncontrolling interests	(12,526)	(9,984)	(10,693)
Net income attributable to common stockholders	\$ 116,086	\$ 94,443	\$ 85,397

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

15. Future Minimum Lease Rental Receipts

We lease space to tenants primarily under non-cancelable operating leases that generally contain provisions for a base rent plus reimbursement of certain operating expenses, and we own fee interests in two parcels of land from which we receive rent under ground leases. The table below presents the future minimum base rentals on our non-cancelable office tenant and ground leases at December 31, 2018:

<u>Year Ending December 31,</u>	<u>(In thousands)</u>
2019	\$ 578,162
2020	531,875
2021	437,528
2022	353,395
2023	269,535
Thereafter	656,926
Total future minimum base rentals ⁽¹⁾	<u>\$ 2,827,421</u>

(1) Does not include (i) residential leases, which typically have a term of one year or less, (ii) holdover rent, (ii) other types of rent such as storage and antenna rent, (iv) tenant reimbursements, (v) straight line rent, (vi) amortization/accretion of acquired above/below-market lease intangibles and (vii) percentage rents. The amounts assume that early termination options held by tenants are not exercised.

16. Future Minimum Lease Rental Payments

We pay rent under a ground lease which expires on December 31, 2086. The rent is fixed at \$733 thousand per year until February 28, 2029, and will then reset to the greater of the existing ground rent or market. We incurred ground rent expense of \$733 thousand during 2018, 2017 and 2016, respectively. The table below, which assumes that the ground rent payments will continue to be \$733 thousand per year after February 28, 2029, presents the future minimum ground lease payments as of December 31, 2018:

<u>Year ending December 31:</u>	<u>(In thousands)</u>
2019	\$ 733
2020	733
2021	733
2022	733
2023	733
Thereafter	46,178
Total future minimum lease payments	<u>\$ 49,843</u>

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

17. Commitments, Contingencies and Guarantees

Legal Proceedings

From time to time, we are party to various lawsuits, claims and other legal proceedings that arise in the ordinary course of our business. Excluding ordinary, routine litigation incidental to our business, we are not currently a party to any legal proceedings that we believe would reasonably be expected to have a materially adverse effect on our business, financial condition or results of operations.

Concentration of Risk

We are subject to credit risk with respect to our tenant receivables and deferred rent receivables related to our tenant leases. Our tenants' ability to honor the terms of their respective leases remains dependent upon economic, regulatory and social factors. We seek to minimize our credit risk from our tenant leases by (i) targeting smaller, more affluent tenants, from a diverse mix of industries, (ii) performing credit evaluations of prospective tenants, and (iii) obtaining security deposits or letters of credit from our tenants. In 2018, 2017 and 2016, no tenant accounted for more than 10% of our total revenues. See Note 2 for the details of our allowances for tenant receivables and deferred rent receivables.

All of our properties, including the properties of our consolidated JVs and unconsolidated Funds, are located in Los Angeles County, California and Honolulu, Hawaii, and we are therefore susceptible to adverse economic and regulatory developments, as well as natural disasters, in those markets.

We are subject to credit risk with respect to our interest rate swap counterparties that we use to manage the risk associated with our floating rate debt. We do not post or receive collateral with respect to our swap transactions. See Note 9 for the details of our interest rate contracts. We seek to minimize our credit risk by entering into agreements with a variety of high quality counterparties with investment grade ratings.

We have significant cash balances invested in a variety of short-term money market funds that are intended to preserve principal value and maintain a high degree of liquidity while providing current income. These investments are not insured against loss of principal and there is no guarantee that our investments in these funds will be redeemable at par value. We also have significant cash balances in bank accounts with high quality financial institutions with investment grade ratings. Interest bearing bank accounts at each U.S. banking institution are insured by the FDIC up to \$250 thousand.

Asset Retirement Obligations

Conditional asset retirement obligations represent a legal obligation to perform an asset retirement activity in which the timing and/or method of settlement is conditional on a future event that may or may not be within our control. A liability for a conditional asset retirement obligation must be recorded if the fair value of the obligation can be reasonably estimated. Environmental site assessments have identified twenty-eight buildings in our Consolidated Portfolio, and four buildings owned by our unconsolidated Funds which contain asbestos, and would have to be removed in compliance with applicable environmental regulations if these properties are demolished or undergo major renovations. As of December 31, 2018, the obligations to remove the asbestos from these properties if they were demolished or undergo major renovations have indeterminable settlement dates, and we are unable to reasonably estimate the fair value of the associated conditional asset retirement obligation. As of December 31, 2018, the obligations to remove the asbestos from properties that are currently undergoing major renovations, or that we plan to renovate in the future, are not material to our financial statements.

Development and Other Contracts

During 2016, we commenced building an additional 491 new apartments at our Moanalua Hillside Apartments in Honolulu, Hawaii. We also invested additional capital to upgrade the existing buildings, improve the parking and landscaping, built a new leasing and management office, and constructed a new fitness facility and two pools. In West Los Angeles, we are building a high-rise apartment building with 376 apartments. As of December 31, 2018, we had an aggregate remaining contractual commitment for these development projects of approximately \$202.9 million. As of December 31, 2018, we had an aggregate remaining contractual commitment for repositionings, capital expenditure projects and tenant improvements of approximately \$55.3 million.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

Guarantees

We have made certain environmental and other limited indemnities and guarantees covering customary non-recourse carve-outs for our unconsolidated Funds' debt. We have also guaranteed the related swaps. Our Funds have agreed to indemnify us for any amounts that we would be required to pay under these agreements. As of December 31, 2018, all of the obligations under the related debt and swap agreements have been performed in accordance with the terms of those agreements. The table below summarizes our Funds' debt as of December 31, 2018. The amounts represent 100% (not our pro-rata share) of the amounts related to our Funds:

Fund ⁽¹⁾	Loan Maturity Date	Principal Balance (In millions)	Variable Interest Rate	Swap Fixed Interest Rate	Swap Maturity Date
Partnership X ⁽²⁾⁽⁴⁾	3/1/2023	\$ 110.0	LIBOR + 1.40%	2.30%	3/1/2021
Fund X ⁽³⁾⁽⁴⁾	7/1/2024	400.0	LIBOR + 1.65%	3.44%	7/1/2022
		<u>\$ 510.0</u>			

- (1) See Note 5 for more information regarding our unconsolidated Funds.
- (2) Floating rate term loan, swapped to fixed, which is secured by two properties and requires monthly payments of interest only, with the outstanding principal due upon maturity. As of December 31, 2018, assuming a zero-percent LIBOR interest rate during the remaining life of the swap, the maximum future payments under the swap agreement were \$2.2 million.
- (3) Floating rate term loan, swapped to fixed, which is secured by six properties and requires monthly payments of interest only, with the outstanding principal due upon maturity. As of December 31, 2018, assuming a zero-percent LIBOR interest rate during the remaining life of the swap, the maximum future payments under the swap agreement were \$25.4 million. Loan agreement includes the requirement to purchase an interest rate cap if one month LIBOR equals or exceeds 3.56% for fourteen consecutive days after the related swap matures.
- (4) Loan agreement includes a zero-percent LIBOR floor. The corresponding swaps do not include such a floor.

Douglas Emmett, Inc.
Notes to Consolidated Financial Statements (continued)

18. Quarterly Financial Information (unaudited)

The tables below present selected quarterly information for 2018 and 2017:

(In thousands, except per share amounts)	Three Months Ended			
	March 31, 2018	June 30, 2018	September 30, 2018	December 31, 2018
Total revenue	\$ 212,247	\$ 219,469	\$ 223,308	\$ 226,292
Net income before noncontrolling interests	\$ 32,631	\$ 37,033	\$ 35,416	\$ 23,532
Net income attributable to common stockholders	\$ 28,206	\$ 31,684	\$ 30,561	\$ 25,635
Net income per common share - basic	\$ 0.17	\$ 0.19	\$ 0.18	\$ 0.15
Net income per common share - diluted	\$ 0.17	\$ 0.19	\$ 0.18	\$ 0.15
Weighted average shares of common stock outstanding - basic	169,601	169,916	169,926	170,121
Weighted average shares of common stock and common stock equivalents outstanding - diluted	169,625	169,926	169,931	170,121

(In thousands, except per share amounts)	Three Months Ended			
	March 31, 2017	June 30, 2017	September 30, 2017	December 31, 2017
Total revenue	\$ 194,481	\$ 199,632	\$ 208,749	\$ 209,190
Net income before noncontrolling interests	\$ 21,780	\$ 22,153	\$ 28,508	\$ 31,986
Net income attributable to common stockholders	\$ 19,049	\$ 20,244	\$ 25,614	\$ 29,536
Net income per common share - basic	\$ 0.12	\$ 0.13	\$ 0.15	\$ 0.17
Net income per common share - diluted	\$ 0.12	\$ 0.13	\$ 0.15	\$ 0.17
Weighted average shares of common stock outstanding - basic	152,490	155,898	165,471	169,521
Weighted average shares of common stock and common stock equivalents outstanding - diluted	153,655	155,952	165,520	169,562

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OUR SENIOR MANAGEMENT

DAN A. EMMETT
Executive Chairman

JORDAN L. KAPLAN
President & Chief Executive Officer

KENNETH M. PANZER
Chief Operating Officer

PETER D. SEYMOUR
Chief Financial Officer

KEVIN A. CRUMMY
Chief Investment Officer

CORPORATE HEADQUARTERS

1299 Ocean Avenue
Suite 1000
Santa Monica, CA 90401
310.255.7700

INVESTOR INFORMATION

***For additional information,
please contact:***

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Vice President – Investor Relations
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Our SEC Filings, including
our latest 10-K and proxy statement, are
available on our website at

www.douglasemmett.com

OUR BOARD OF DIRECTORS

DAN A. EMMETT
Chairman of the Board

JORDAN L. KAPLAN
President & Chief Executive Officer

KENNETH M. PANZER
Chief Operating Officer

CHRISTOPHER H. ANDERSON
Retired Real Estate Executive
and Investor

LESLIE E. BIDER
Vice Chairman - PinnacleCare

DR. DAVID T. FEINBERG
Vice President – Google Health

VIRGINIA A. MCFERRAN
Partner - Optum Ventures

THOMAS E. O'HERN
Chief Executive Officer -
Macerich Company

WILLIAM E. SIMON, JR.
Partner - Massey Quick Simon & Co., LLC

STOCK EXCHANGE

The New York Stock Exchange – NYSE
Ticker Symbol – DEI

LEGAL COUNSEL

Manatt I Phelps I Phillips LLP
Los Angeles, CA

INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Ernst & Young LLP
Los Angeles, CA

SHAREHOLDER ACCOUNT ASSISTANCE

Shareholder records are maintained by
Douglas Emmett's Transfer Agent:

Computershare Investor Services, LLC
312.588.4990

ANNUAL MEETING

1299 Ocean Avenue
Suite 1000
Santa Monica, CA 90401
May 30, 2019 9:00 a.m. (PDT)

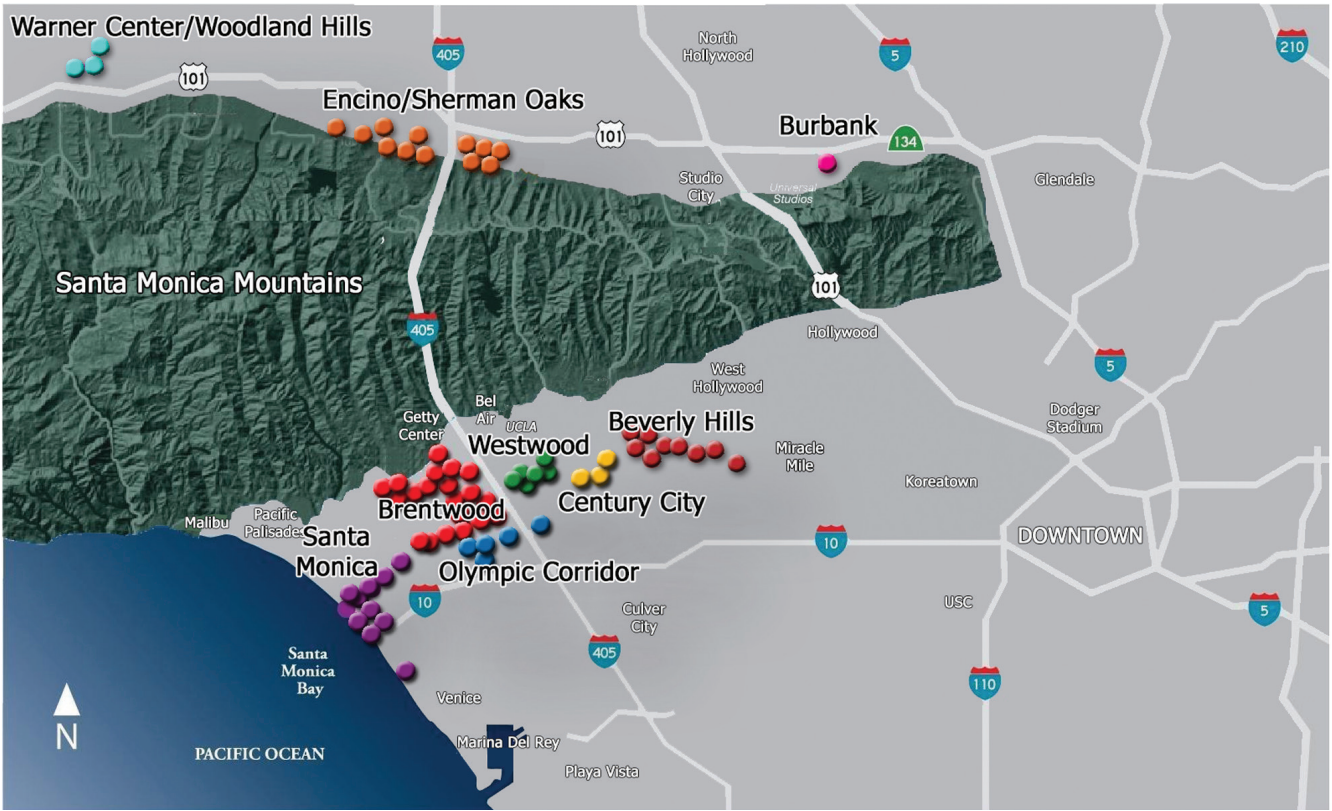


At Douglas Emmett concern for the environment is ingrained in our corporate culture. We are committed to implementing and maintaining financially responsible sustainability programs in our properties. Through the years we have proactively introduced conservation and sustainability measures across our portfolio that have significantly reduced our energy consumption, increased our operational efficiencies and reduced our carbon footprint. We engage our service providers, suppliers, and tenants to join our mission and work with them to pursue opportunities where cost savings and social responsibility merge.

At Douglas Emmett we know that sustainability is a yard stick for both social responsibility and fiscal management. Simply put, thoughtful implementation of sustainable initiatives is good business.

Douglas Emmett

Map of Office and Residential Properties



Los Angeles Submarkets

- Warner Center/Woodland Hills
- Santa Monica
- Beverly Hills
- Westwood
- Burbank
- Century City
- Brentwood
- Encino/Sherman Oaks
- Olympic Corridor



Honolulu Submarket

