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DUKE REALTY CORP

Form 10-Q

May 04, 2018

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q**

(Mark One)

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

For the quarterly period ended March 31, 2018

OR

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

For the transition period from _____ to _____

Commission File Number: 1-9044 (Duke Realty Corporation) 0-20625 (Duke Realty Limited Partnership)

**DUKE REALTY CORPORATION
DUKE REALTY LIMITED PARTNERSHIP**

(Exact Name of Registrant as Specified in Its Charter)

Indiana (Duke Realty Corporation) 35-1740409 (Duke Realty Corporation)
Indiana (Duke Realty Limited Partnership) 35-1898425 (Duke Realty Limited Partnership)
(State or Other Jurisdiction of Incorporation or Organization) (I.R.S. Employer Identification Number)
600 East 96th Street, Suite 100 46240
Indianapolis, Indiana (Address of Principal Executive Offices) (Zip Code)

Registrant's Telephone Number, Including Area Code: (317) 808-6000

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Duke Realty Corporation Yes No **Duke Realty Limited Partnership** Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Duke Realty Corporation Yes No **Duke Realty Limited Partnership** Yes No

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

Duke Realty Corporation:

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company Emerging growth company

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

Duke Realty Limited Partnership:

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company Emerging growth company

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

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

Duke Realty Corporation Yes No **Duke Realty Limited Partnership** Yes No

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

Class	Outstanding Common Shares of Duke Realty Corporation at May 3, 2018
Common Stock 0.01 par value per share	357,030,140

EXPLANATORY NOTE

This report (the "Report") combines the quarterly reports on Form 10-Q for the period ended March 31, 2018 of both Duke Realty Corporation and Duke Realty Limited Partnership. Unless stated otherwise or the context otherwise requires, references to "Duke Realty Corporation" or the "General Partner" mean Duke Realty Corporation and its consolidated subsidiaries, and references to the "Partnership" mean Duke Realty Limited Partnership and its consolidated subsidiaries. The terms the "Company," "we," "us" and "our" refer to the General Partner and the Partnership, collectively, and those entities owned or controlled by the General Partner and/or the Partnership. Duke Realty Corporation is a self-administered and self-managed real estate investment trust ("REIT") and is the sole general partner of the Partnership, owning 99.1% of the common partnership interests of the Partnership ("General Partner Units") as of March 31, 2018. The remaining 0.9% of the common partnership interests ("Limited Partner Units" and, together with the General Partner Units, the "Common Units") are owned by limited partners. As the sole general partner of the Partnership, the General Partner has full, exclusive and complete responsibility and discretion in the day-to-day management and control of the Partnership.

The General Partner and the Partnership are operated as one enterprise. The management of the General Partner consists of the same members as the management of the Partnership. As the sole general partner with control of the Partnership, the General Partner consolidates the Partnership for financial reporting purposes, and the General Partner does not have any significant assets other than its investment in the Partnership. Therefore, the assets and liabilities of the General Partner and the Partnership are substantially the same.

We believe combining the quarterly reports on Form 10-Q of the General Partner and the Partnership into this single report results in the following benefits:

- enhances investors' understanding of the General Partner and the Partnership by enabling investors to view the business as a whole in the same manner as management views and operates the business;
- eliminates duplicative disclosure and provides a more streamlined and readable presentation of information since a substantial portion of the Company's disclosure applies to both the General Partner and the Partnership; and
- creates time and cost efficiencies through the preparation of one combined report instead of two separate reports.

We believe it is important to understand the few differences between the General Partner and the Partnership in the context of how we operate as an interrelated consolidated company. The General Partner's only material asset is its ownership of partnership interests in the Partnership. As a result, the General Partner does not conduct business itself, other than acting as the sole general partner of the Partnership and issuing public equity from time to time. The General Partner does not issue any indebtedness, but does guarantee some of the unsecured debt of the Partnership. The Partnership holds substantially all the assets of the business, directly or indirectly, and holds the ownership interests related to certain of the Company's investments. The Partnership conducts the operations of the business and has no publicly traded equity. Except for net proceeds from equity issuances by the General Partner, which are contributed to the Partnership in exchange for General Partner Units or Preferred Units, the Partnership generates the capital required by the business through its operations, its incurrence of indebtedness and the issuance of Limited Partner Units to third parties.

Noncontrolling interests, shareholders' equity and partners' capital are the main areas of difference between the consolidated financial statements of the General Partner and those of the Partnership. The noncontrolling interests in the Partnership's financial statements include the interests in consolidated investees not wholly owned by the Partnership. The noncontrolling interests in the General Partner's financial statements include the same noncontrolling interests at the Partnership level, as well as the common limited partnership interests in the Partnership, which are accounted for as partners' capital by the Partnership.

In order to highlight the differences between the General Partner and the Partnership, there are separate sections in this report, as applicable, that separately discuss the General Partner and the Partnership, including separate financial statements and separate Exhibit 31 and 32 certifications. In the sections that combine disclosure of the General Partner and the Partnership, this report refers to actions or holdings as being actions or holdings of the collective Company.

**DUKE REALTY CORPORATION/DUKE REALTY LIMITED PARTNERSHIP
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PART I - FINANCIAL INFORMATION**Item 1. Financial Statements****DUKE REALTY CORPORATION AND SUBSIDIARIES****Consolidated Balance Sheets****(in thousands, except per share amounts)**

	March 31, 2018 (Unaudited)	December 31, 2017
ASSETS		
Real estate investments:		
Real estate assets	\$ 6,608,594	\$ 6,593,567
Construction in progress	441,484	401,407
Investments in and advances to unconsolidated joint ventures	121,576	126,487
Undeveloped land	259,842	226,987
	7,431,496	7,348,448
Accumulated depreciation	(1,238,688)	(1,193,905)
Net real estate investments	6,192,808	6,154,543
Real estate investments and other assets held-for-sale	21,740	17,550
Cash and cash equivalents	160,861	67,562
Accounts receivable, net of allowance of \$1,626 and \$1,709	21,939	19,427
Straight-line rent receivable, net of allowance of \$6,104 and \$5,254	97,266	93,005
Receivables on construction contracts, including retentions	16,692	13,480
Deferred leasing and other costs, net of accumulated amortization of \$208,092 and \$209,451	297,103	292,682
Restricted cash held in escrow for like-kind exchange	59,196	116,405
Notes receivable from property sales	386,789	426,657
Other escrow deposits and other assets	173,280	186,885
	\$ 7,427,674	\$ 7,388,196
LIABILITIES AND EQUITY		
Indebtedness:		
Secured debt, net of deferred financing costs of \$529 and \$614	\$ 310,070	\$ 311,349
Unsecured debt, net of deferred financing costs of \$20,000 and \$20,500	2,111,386	2,111,542
Unsecured line of credit	75,000	—
	2,496,456	2,422,891
Liabilities related to real estate investments held-for-sale	1,327	1,163
Construction payables and amounts due subcontractors, including retentions	53,339	54,545
Accrued real estate taxes	71,234	67,374
Accrued interest	27,166	17,911
Other liabilities	152,358	210,825
Tenant security deposits and prepaid rents	44,610	39,109
Total liabilities	2,846,490	2,813,818
Shareholders' equity:		
Common shares (\$0.01 par value); 600,000 shares authorized; 357,025 and 356,361 shares issued and outstanding, respectively	3,570	3,564
Additional paid-in capital	5,204,855	5,205,316
Distributions in excess of net income	(674,920)	(676,036)
Total shareholders' equity	4,533,505	4,532,844

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Noncontrolling interests	47,679	41,534
Total equity	4,581,184	4,574,378
	\$7,427,674	\$ 7,388,196

See accompanying Notes to Consolidated Financial Statements

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DUKE REALTY CORPORATION AND SUBSIDIARIES
Consolidated Statements of Operations and Comprehensive Income
For the three months ended March 31,
(in thousands, except per share amounts)
(Unaudited)

	2018	2017
Revenues:		
Rental and related revenue	\$193,456	\$171,676
General contractor and service fee revenue	41,101	9,399
	234,557	181,075
Expenses:		
Rental expenses	20,396	16,237
Real estate taxes	31,146	26,511
General contractor and other services expenses	40,409	7,624
Depreciation and amortization	77,529	62,023
	169,480	112,395
Other operating activities:		
Equity in earnings of unconsolidated joint ventures	8,287	4,749
Gain on sale of properties	44,886	37,046
Gain on land sales	2,949	1,505
Other operating expenses	(786)	(738)
Impairment charges	—	(859)
General and administrative expenses	(21,023)	(19,232)
	34,313	22,471
Operating income	99,390	91,151
Other income (expenses):		
Interest and other income, net	4,463	533
Interest expense	(20,000)	(24,162)
Gain on debt extinguishment	—	25
Income from continuing operations before income taxes	83,853	67,547
Income tax expense	(10,329)	(2,132)
Income from continuing operations	73,524	65,415
Discontinued operations:		
(Loss) income before gain on sales	(8)	5,366
Gain on sale of depreciable properties	132	—
Income from discontinued operations	124	5,366
Net income	73,648	70,781
Net income attributable to noncontrolling interests	(685)	(581)
Net income attributable to common shareholders	\$72,963	\$70,200
Basic net income per common share:		
Continuing operations attributable to common shareholders	\$0.20	\$0.18
Discontinued operations attributable to common shareholders	—	0.02
Total	\$0.20	\$0.20
Diluted net income per common share:		
Continuing operations attributable to common shareholders	\$0.20	\$0.18
Discontinued operations attributable to common shareholders	—	0.02
Total	\$0.20	\$0.20
Weighted average number of common shares outstanding	356,740	355,282
Weighted average number of common shares and potential dilutive securities	360,400	360,700

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Comprehensive income:

Net income	\$73,648	\$70,781
Other comprehensive loss:		
Amortization of interest contracts	—	(256)
Comprehensive income	\$73,648	\$70,525

See accompanying Notes to Consolidated Financial Statements

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DUKE REALTY CORPORATION AND SUBSIDIARIES**Consolidated Statements of Cash Flows****For the three months ended March 31,****(in thousands)****(Unaudited)**

	2018	2017
Cash flows from operating activities:		
Net income	\$73,648	\$70,781
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation of buildings and tenant improvements	63,944	66,172
Amortization of deferred leasing and other costs	13,585	15,385
Amortization of deferred financing costs	1,418	1,316
Straight-line rental income and expense, net	(6,288)	(2,928)
Impairment charges	—	859
Gain on debt extinguishment	—	(25)
Gains on land and depreciated property sales	(47,967)	(38,551)
Third-party construction contracts, net	(367)	714
Other accrued revenues and expenses, net	19,862	(3,733)
Equity in earnings in excess of operating distributions received from unconsolidated joint ventures	(4,673)	(282)
Net cash provided by operating activities	113,162	109,708
Cash flows from investing activities:		
Development of real estate investments	(104,346)	(112,727)
Acquisition of real estate investments and related intangible assets	(22,801)	(114,369)
Acquisition of undeveloped land	(67,256)	(50,436)
Second generation tenant improvements, leasing costs and building improvements	(14,102)	(10,431)
Other deferred leasing costs	(9,798)	(4,398)
Other assets	39,183	(4,186)
Proceeds from land and depreciated property sales, net	131,380	103,120
Capital distributions from unconsolidated joint ventures	9,404	4,858
Capital contributions and advances to unconsolidated joint ventures	—	(297)
Net cash used for investing activities	(38,336)	(188,866)
Cash flows from financing activities:		
Proceeds from issuance of common shares, net	706	786
Payments on unsecured debt	(656)	(616)
Payments on secured indebtedness including principal amortization	(1,345)	(17,539)
Borrowings on line of credit, net	75,000	189,000
Distributions to common shareholders	(71,398)	(67,554)
Distributions to noncontrolling interests	(680)	(640)
Tax payments on stock-based compensation awards	(7,984)	(8,848)
Change in book cash overdrafts	(33,448)	7,115
Deferred financing costs	(285)	(7)
Net cash (used for) provided by financing activities	(40,090)	101,697
Net increase in cash, cash equivalents and restricted cash	34,736	22,539
Cash, cash equivalents and restricted cash at beginning of period	193,627	57,038
Cash, cash equivalents and restricted cash at end of period	\$228,363	\$79,577
Non-cash investing and financing activities:		
Conversion of Limited Partner Units to common shares	\$—	\$1,685
See accompanying Notes to Consolidated Financial Statements		

DUKE REALTY CORPORATION AND SUBSIDIARIES**Consolidated Statement of Changes in Equity****For the three months ended March 31, 2018****(in thousands, except per share data)****(Unaudited)**

	Common Shareholders				Total
	Common Stock	Additional Paid-in Capital	Distributions in Excess of Net Income	Noncontrolling Interests	
Balance at December 31, 2017	\$ 3,564	\$ 5,205,316	\$ (676,036)	\$ 41,534	\$ 4,574,378
Net income	—	—	72,963	685	73,648
Issuance of common shares	—	706	—	—	706
Stock-based compensation plan activity	6	(1,167)	(449)	6,140	4,530
Distributions to common shareholders (\$0.20 per share)	—	—	(71,398)	—	(71,398)
Distributions to noncontrolling interests	—	—	—	(680)	(680)
Balance at March 31, 2018	\$ 3,570	\$ 5,204,855	\$ (674,920)	\$ 47,679	\$ 4,581,184

See accompanying Notes to Consolidated Financial Statements

DUKE REALTY LIMITED PARTNERSHIP AND SUBSIDIARIES**Consolidated Balance Sheets****(in thousands)**

	March 31, 2018	December 31, 2017
	(Unaudited)	
ASSETS		
Real estate investments:		
Real estate assets	\$ 6,608,594	\$ 6,593,567
Construction in progress	441,484	401,407
Investments in and advances to unconsolidated joint ventures	121,576	126,487
Undeveloped land	259,842	226,987
	7,431,496	7,348,448
Accumulated depreciation	(1,238,688)	(1,193,905)
Net real estate investments	6,192,808	6,154,543
Real estate investments and other assets held-for-sale	21,740	17,550
Cash and cash equivalents	160,861	67,562
Accounts receivable, net of allowance of \$1,626 and \$1,709	21,939	19,427
Straight-line rent receivable, net of allowance of \$6,104 and \$5,254	97,266	93,005
Receivables on construction contracts, including retentions	16,692	13,480
Deferred leasing and other costs, net of accumulated amortization of \$208,092 and \$209,451	297,103	292,682
Restricted cash held in escrow for like-kind exchange	59,196	116,405
Notes receivable from property sales	386,789	426,657
Other escrow deposits and other assets	173,280	186,885
	\$ 7,427,674	\$ 7,388,196
LIABILITIES AND EQUITY		
Indebtedness:		
Secured debt, net of deferred financing costs of \$529 and \$614	\$ 310,070	\$ 311,349
Unsecured debt, net of deferred financing costs of \$20,000 and \$20,500	2,111,386	2,111,542
Unsecured line of credit	75,000	—
	2,496,456	2,422,891
Liabilities related to real estate investments held-for-sale	1,327	1,163
Construction payables and amounts due subcontractors, including retentions	53,339	54,545
Accrued real estate taxes	71,234	67,374
Accrued interest	27,166	17,911
Other liabilities	152,358	210,825
Tenant security deposits and prepaid rents	44,610	39,109
Total liabilities	2,846,490	2,813,818
Partners' equity:		
Common equity (357,025 and 356,361 General Partner Units issued and outstanding, respectively)	4,533,505	4,532,844
Limited Partners' common equity (3,402 and 3,283 Limited Partner Units issued and outstanding, respectively)	46,706	40,563
Total partners' equity	4,580,211	4,573,407
Noncontrolling interests	973	971
Total equity	4,581,184	4,574,378
	\$ 7,427,674	\$ 7,388,196

See accompanying Notes to Consolidated Financial Statements

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DUKE REALTY LIMITED PARTNERSHIP AND SUBSIDIARIES
Consolidated Statements of Operations and Comprehensive Income
For the three months ended March 31,
(in thousands, except per unit amounts)
(Unaudited)

	2018	2017
Revenues:		
Rental and related revenue	\$193,456	\$171,676
General contractor and service fee revenue	41,101	9,399
	234,557	181,075
Expenses:		
Rental expenses	20,396	16,237
Real estate taxes	31,146	26,511
General contractor and other services expenses	40,409	7,624
Depreciation and amortization	77,529	62,023
	169,480	112,395
Other operating activities:		
Equity in earnings of unconsolidated joint ventures	8,287	4,749
Gain on sale of properties	44,886	37,046
Gain on land sales	2,949	1,505
Other operating expenses	(786)	(738)
Impairment charges	—	(859)
General and administrative expenses	(21,023)	(19,232)
	34,313	22,471
Operating income	99,390	91,151
Other income (expenses):		
Interest and other income, net	4,463	533
Interest expense	(20,000)	(24,162)
Gain on debt extinguishment	—	25
Income from continuing operations before income taxes	83,853	67,547
Income tax expense	(10,329)	(2,132)
Income from continuing operations	73,524	65,415
Discontinued operations:		
(Loss) income before gain on sales	(8)	5,366
Gain on sale of depreciable properties	132	—
Income from discontinued operations	124	5,366
Net income	73,648	70,781
Net (income) loss attributable to noncontrolling interests	(2)	71
Net income attributable to common unitholders	\$73,646	\$70,852
Basic net income per Common Unit:		
Continuing operations attributable to common unitholders	\$0.20	\$0.18
Discontinued operations attributable to common unitholders	—	0.02
Total	\$0.20	\$0.20
Diluted net income per Common Unit:		
Continuing operations attributable to common unitholders	\$0.20	\$0.18
Discontinued operations attributable to common unitholders	—	0.02
Total	\$0.20	\$0.20
Weighted average number of Common Units outstanding	360,095	358,598
Weighted average number of Common Units and potential dilutive securities	360,400	360,700

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Comprehensive income:

Net income	\$73,648	\$70,781
Other comprehensive loss:		
Amortization of interest contracts	—	(256)
Comprehensive income	\$73,648	\$70,525

See accompanying Notes to Consolidated Financial Statements

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DUKE REALTY LIMITED PARTNERSHIP AND SUBSIDIARIES**Consolidated Statements of Cash Flows****For the three months ended March 31,****(in thousands)****(Unaudited)**

	2018	2017
Cash flows from operating activities:		
Net income	\$ 73,648	\$ 70,781
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation of buildings and tenant improvements	63,944	66,172
Amortization of deferred leasing and other costs	13,585	15,385
Amortization of deferred financing costs	1,418	1,316
Straight-line rental income and expense, net	(6,288)	(2,928)
Impairment charges	—	859
Gain on debt extinguishment	—	(25)
Gains on land and depreciated property sales	(47,967)	(38,551)
Third-party construction contracts, net	(367)	714
Other accrued revenues and expenses, net	19,862	(3,733)
Equity in earnings in excess of operating distributions received from unconsolidated joint ventures	(4,673)	(282)
Net cash provided by operating activities	113,162	109,708
Cash flows from investing activities:		
Development of real estate investments	(104,346)	(112,727)
Acquisition of real estate investments and related intangible assets	(22,801)	(114,369)
Acquisition of undeveloped land	(67,256)	(50,436)
Second generation tenant improvements, leasing costs and building improvements	(14,102)	(10,431)
Other deferred leasing costs	(9,798)	(4,398)
Other assets	39,183	(4,186)
Proceeds from land and depreciated property sales, net	131,380	103,120
Capital distributions from unconsolidated joint ventures	9,404	4,858
Capital contributions and advances to unconsolidated joint ventures	—	(297)
Net cash used for investing activities	(38,336)	(188,866)
Cash flows from financing activities:		
Contributions from the General Partner	706	786
Payments on unsecured debt	(656)	(616)
Payments on secured indebtedness including principal amortization	(1,345)	(17,539)
Borrowings on line of credit, net	75,000	189,000
Distributions to common unitholders	(72,078)	(68,184)
Distributions to noncontrolling interests	—	(10)
Tax payments on stock-based compensation awards	(7,984)	(8,848)
Change in book cash overdrafts	(33,448)	7,115
Deferred financing costs	(285)	(7)
Net cash (used for) provided by financing activities	(40,090)	101,697
Net increase in cash, cash equivalents and restricted cash	34,736	22,539
Cash, cash equivalents and restricted cash at beginning of period	193,627	57,038
Cash, cash equivalents and restricted cash at end of period	\$ 228,363	\$ 79,577
Non-cash investing and financing activities:		
Conversion of Limited Partner Units to common shares of the General Partner	\$—	\$ 1,685
See accompanying Notes to Consolidated Financial Statements		

DUKE REALTY LIMITED PARTNERSHIP AND SUBSIDIARIES**Consolidated Statement of Changes in Equity****For the three months ended March 31, 2018****(in thousands, except per unit data)****(Unaudited)**

	Common Unitholders				Total Equity
	General Partner's Common Equity	Limited Partners' Common Equity	Partners' Equity	Noncontrolling Interests	
Balance at December 31, 2017	\$4,532,844	\$40,563	\$4,573,407	\$ 971	\$4,574,378
Net income	72,963	683	73,646	2	73,648
Capital contribution from the General Partner	706	—	706	—	706
Stock-based compensation plan activity	(1,610)	6,140	4,530	—	4,530
Distributions to common unitholders (\$0.20 per Common Unit)	(71,398)	(680)	(72,078)	—	(72,078)
Balance at March 31, 2018	\$4,533,505	\$46,706	\$4,580,211	\$ 973	\$4,581,184

See accompanying Notes to Consolidated Financial Statements

DUKE REALTY CORPORATION AND DUKE REALTY LIMITED PARTNERSHIP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. General Basis of Presentation

The interim consolidated financial statements included herein have been prepared by the General Partner and the Partnership. The 2017 year-end consolidated balance sheet data included in this Report was derived from the audited financial statements in the combined Annual Report on Form 10-K of the General Partner and the Partnership for the year ended December 31, 2017 (the "2017 Annual Report"), but does not include all disclosures required by accounting principles generally accepted in the United States of America ("GAAP"). The financial statements have been prepared in accordance with GAAP for interim financial information and in accordance with Rule 10-01 of Regulation S-X of the Securities Exchange Act of 1934, as amended. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and revenue and expenses during the reporting period. Our actual results could differ from those estimates and assumptions. These financial statements should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations included herein and the consolidated financial statements and notes thereto included in the 2017 Annual Report.

The General Partner was formed in 1985, and we believe that it qualifies as a REIT under the provisions of the Internal Revenue Code of 1986, as amended (the "Code"). The Partnership was formed on October 4, 1993, when the General Partner contributed all of its properties and related assets and liabilities, together with the net proceeds from an offering of additional shares of its common stock, to the Partnership. Simultaneously, the Partnership completed the acquisition of Duke Associates, a full-service commercial real estate firm operating in the Midwest whose operations began in 1972.

The General Partner is the sole general partner of the Partnership, owning approximately 99.1% of the Common Units at March 31, 2018. The remaining 0.9% of the Common Units are owned by limited partners. As the sole general partner of the Partnership, the General Partner has full, exclusive and complete responsibility and discretion in the day-to-day management and control of the Partnership. The General Partner and the Partnership are operated as one enterprise. The management of the General Partner consists of the same members as the management of the Partnership. As the sole general partner with control of the Partnership, the General Partner consolidates the Partnership for financial reporting purposes, and the General Partner does not have any significant assets other than its investment in the Partnership. Therefore, the assets and liabilities of the General Partner and the Partnership are substantially the same.

Limited partners have the right to redeem their Limited Partner Units, subject to certain restrictions. Pursuant to the Fifth Amended and Restated Agreement of Limited Partnership, as amended (the "Partnership Agreement"), the General Partner is obligated to redeem the Limited Partner Units in shares of its common stock, unless it determines in its reasonable discretion that the issuance of shares of its common stock could cause it to fail to qualify as a REIT. Each Limited Partner Unit shall be redeemed for one share of the General Partner's common stock, or, in the event that the issuance of shares could cause the General Partner to fail to qualify as a REIT, cash equal to the fair market value of one share of the General Partner's common stock at the time of redemption, in each case, subject to certain adjustments described in the Partnership Agreement. The Limited Partner Units are not required, per the terms of the Partnership Agreement, to be redeemed in registered shares of the General Partner.

As of March 31, 2018, we owned and operated a portfolio primarily consisting of industrial properties and provided real estate services to third-party owners. Substantially all of our Rental Operations (see Note 9) are conducted through the Partnership. We conduct our Service Operations (see Note 9) through Duke Realty Services, LLC, Duke Realty Services Limited Partnership and Duke Construction Limited Partnership ("DCLP"), which are consolidated entities that are 100% owned by a combination of the General Partner and the Partnership. DCLP is owned through a taxable REIT subsidiary. The consolidated financial statements include our accounts and the accounts of our majority-owned or controlled subsidiaries.

2. New Accounting Pronouncements

Recently Adopted Accounting Pronouncements

Revenue Recognition and De-recognition of Non-Financial Assets

On January 1, 2018, we concurrently adopted Accounting Standards Codification ("ASC") 606, *Revenue from Contracts with Customers* ("ASC 606") and ASC 610-20, *Other Income: Gains and Losses from the De-recognition of Non-financial Assets* ("ASC 610-20") using a modified retrospective ("cumulative effect") method of adoption. ASC 606 has superseded nearly all existing GAAP revenue recognition guidance, although its scope excludes lease contracts which represent our primary source of revenue. The standard's core principle is that a company will recognize revenue when it satisfies performance obligations, by transferring promised goods or services to customers, in an amount that reflects the consideration to which the company expects to be entitled in exchange for fulfilling those performance obligations.

General Contractor and Service Fee Revenue

Beginning with the January 1, 2018 adoption date, general contractor and service fee revenues, as presented on the Consolidated Statements of Operations, are accounted for within the scope of ASC 606. General contractor and service fee revenues are comprised primarily of construction and development related revenues earned from third parties while acting in capacity of a developer, as a general contractor or a construction manager. There are other ancillary streams of revenue included in general contractor and service fee revenues (see Note 9), such as management fees earned from unconsolidated joint ventures, which are not significant. Opening and closing balances of construction receivables are presented separately on the Consolidated Balance Sheets. Over billed construction receivables totaled \$295,000 and \$276,000 at March 31, 2018 and December 31, 2017, respectively. We generally do not have any contract assets associated with our construction arrangements.

Our construction arrangements are typically structured with only one performance obligation, which generally represents either an obligation to construct a new building or to construct fixtures in an existing building, and these single performance obligations are satisfied over time as construction progresses. We recognize revenue as we satisfy such performance obligations using the percentage of completion method, which is an input method allowed under ASC 606. Using this method, profits are recorded based on our estimates of the percentage of completion of individual contracts, commencing when the work performed under the contracts reaches a point where the final costs can be estimated with reasonable accuracy. The percentage of completion estimates are based on a comparison of the contract expenditures incurred to the estimated final costs. We believe the percentage of completion method is a faithful depiction of the transfer of goods and services as changes in job performance and estimated profitability, which result in revisions to costs and income and are recognized in the period in which the revisions are determined, have not historically been significant. We typically receive regular progress payments on the majority of our construction arrangements and such arrangements generally have an original duration of less than one year. As the result of the relatively short duration of our construction arrangements, we have elected to apply the optional disclosure exemptions, included in ASC 606, related to our remaining performance obligations for our in-process construction projects, for which any future variable consideration is not material.

De-Recognition of Non-Financial Assets

ASC 610-20 provides guidance on how entities recognize sales, including partial sales, of non-financial assets (and in-substance non-financial assets) to non-customers. ASC 606 includes guidance governing the sale of non-financial assets with customers, while sales of non-financial assets to non-customers are governed by ASC 610-20. The only difference in the treatment of sales to customers and non-customers is the presentation in the Consolidated Statements of Operations (revenue and expense is reported when the sale is to a customer and net gain or loss is reported when the sale is to a non-customer). Based on the nature of our business, we have concluded that our property sales represent transactions with non-customers. In the typical course of our business, sales of non-financial assets represent only one performance obligation and are recognized when an enforceable contract is in place, collectability is ensured and control is transferred to the buyer.

ASC 610-20 also requires the seller to recognize a full gain or loss in a partial sale of non-financial assets, to the extent control is not retained. Any noncontrolling interest retained by the seller would, accordingly, be measured at fair value. We have primarily disposed of property and land in all cash transactions with no contingencies and no future involvement in the operations, and therefore, the adoption of ASC 610-20 has not significantly impacted the recognition of property and land sales.

There was no cumulative adjustment recognized to beginning retained earnings as of January 1, 2018 as the result of adopting ASC 606 and ASC 610-20.

Restricted Cash

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows: Restricted Cash* ("ASU 2016-18"). ASU 2016-18 requires entities to show the changes in the total of cash, cash equivalents and restricted cash in the statement of cash flows. As a result, entities will no longer present transfers between cash, cash equivalents and restricted cash in the statement of cash flows. We adopted this standard on January 1, 2018, on a retrospective basis, and the adoption did not have a material impact on our consolidated financial statements.

The following table provides a reconciliation of cash, cash equivalents, and restricted cash reported within the Consolidated Balance Sheets that sum to the total of the same such amounts shown in the Consolidated Statements of Cash Flows (in thousands):

	March 31,	December 31,
	2018	2017
Cash and cash equivalents	\$ 160,861	\$ 67,562
Restricted cash held in escrow for like-kind exchange	59,196	116,405
Restricted cash included in other escrow deposits and other assets	8,306	9,660
Total cash, cash equivalents, and restricted cash shown in the Consolidated Statements of Cash Flows	\$ 228,363	\$ 193,627

Restricted cash held in escrow for like-kind exchange on the Consolidated Balance Sheets includes cash received from the property dispositions but restricted only for qualifying like-kind exchange transactions.

Statement of Cash Flows

In August 2016, the FASB issued ASU 2016-15, *Statement of Cash Flows* ("ASU 2016-15"). ASU 2016-15 clarifies how entities should classify certain cash receipts and cash payments on the statement of cash flows and how the predominance principle should be applied when cash receipts and cash payments have aspects of more than one class of cash flows. We adopted this standard on January 1, 2018, on a retrospective basis, and the adoption did not have a material impact on our consolidated financial statements.

New Accounting Pronouncement Not Yet Adopted

Leases

In February 2016, the FASB issued ASU 2016-02, *Leases* ("ASU 2016-02"), which sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract (i.e. lessees and lessors). ASU 2016-02 supersedes existing leasing standards.

For lessors, the accounting under ASU 2016-02 will remain largely unchanged from current GAAP; however ASU 2016-02 requires that lessors expense certain initial direct costs, which are capitalizable under existing leasing standards, as incurred. ASU 2016-02 also specifies that payments for certain lease-related services, which are often included in lease agreements, represent "non-lease" components that will become subject to the guidance in ASC 606, when ASU 2016-02 becomes effective. The FASB recently clarified that only new or modified leases subsequent to adoption of ASU 2016-02 will require different accounting for "non-lease" components under the guidance in ASC 606. Additionally, on March 28, 2018 the FASB tentatively approved amendments to ASU

2016-02 (the "Approved Amendments"), which, if ultimately finalized as an amendment to ASU 2016-02, will allow lessors an optional election to not separate "non-lease" components from the related lease components. This election would be contingent upon certain conditions being met, including a requirement that separating the "non-lease" components would not result in a change in the timing and pattern of the revenue recognition.

ASU 2016-02 requires lessees to apply a dual approach, classifying leases as either finance or operating leases based on the principle of whether or not the lease is effectively a financed purchase of the leased asset by the lessee. This classification will determine whether the lease expense is recognized based on an effective interest method or on a straight-line basis over the term of the lease. A lessee is also required to record a right-of-use asset and a lease liability for all leases with a term of greater than 12 months regardless of classification. ASU 2016-02 will impact the accounting and disclosure requirements for ground leases, and other operating leases, where we are the lessee. ASU 2016-02 will be effective for us on January 1, 2019 under the modified retrospective approach, with early adoption permitted.

A set of practical expedients for implementation, which must be elected as a package and for all leases, may also be elected. These practical expedients include (i) relief from re-assessing whether an expired or existing contract meets the definition of a lease, (ii) relief from re-assessing the classification of expired or existing leases at the adoption date and (iii) allowing previously capitalized initial direct leasing costs to continue to be amortized. In addition to these practical expedients, the Approved Amendments also include an option that would allow lessors to use the effective date of ASU 2016-02 as the date of initial application, without restating comparative periods, and to recognize a cumulative effect adjustment as of the effective date. We are currently assessing the method of adoption and the impact that ASU 2016-02 will have on our consolidated financial statements but have tentatively concluded that we will apply the practical expedients as well as the optional relief provided by the Approved Amendments, should they be finalized.

3. Reclassifications

Certain amounts in the accompanying consolidated financial statements that have been reclassified to conform to the 2018 consolidated financial statement presentation include the change in presentation for properties determined to be discontinued operations (see Note 10).

4. Variable Interest Entities

Partnership

Due to the fact that the Limited Partners do not have kick out rights, or substantive participating rights, the Partnership is a variable interest entity ("VIE"). Because the General Partner holds majority ownership and exercises control over every aspect of the Partnership's operations, the General Partner has been determined as the primary beneficiary and, therefore, consolidates the Partnership.

The assets and liabilities of the General Partner and the Partnership are substantially the same, as the General Partner does not have any significant assets other than its investment in the Partnership. All of the Company's debt is an obligation of the Partnership.

Unconsolidated Joint Ventures

We have equity interests in unconsolidated joint ventures that primarily own and operate rental properties or hold land for development. We consolidate those joint ventures that are considered to be VIEs where we are the primary beneficiary. We analyze our investments in joint ventures to determine if the joint venture is considered a VIE and would require consolidation. We (i) evaluate the sufficiency of the total equity investment at risk, (ii) review the voting rights and decision-making authority of the equity investment holders as a group and whether there are

limited partners (or similar owning entities) that lack substantive participating or kick out rights and (iii) establish whether or not activities within the venture are on behalf of an investor with disproportionately few voting rights in making this VIE determination.

To the extent that we own interests in a VIE and we (i) are the sole entity that has the power to direct the activities of the VIE and (ii) have the obligation or rights to absorb the VIE's losses or receive its benefits, then we would be determined to be the primary beneficiary and would consolidate the VIE. To the extent we own interests in a VIE, then at each reporting period, we re-assess our conclusions as to which, if any, party within the VIE is considered the primary beneficiary. Consolidated joint ventures that are VIEs are not significant in any period presented in these consolidated financial statements.

To the extent that our joint ventures do not qualify as VIEs, they are consolidated if we control them through majority ownership interests or if we are the managing entity (general partner or managing member) and the other partner does not have substantive participating rights. Control is further demonstrated by our ability to unilaterally make significant operating decisions, refinance debt and sell the assets of the joint venture without the consent of the non-managing entity and the inability of the non-managing entity to remove us from our role as the managing entity. Consolidated joint ventures that are not VIEs are not significant in any period presented in these consolidated financial statements.

There were no unconsolidated joint ventures, in which we have any recognized assets or liabilities or have retained any economic exposure to loss at March 31, 2018, that met the criteria to be considered VIEs. Our maximum loss exposure for guarantees of unconsolidated joint venture indebtedness, none of which relate to VIEs, totaled \$102.9 million at March 31, 2018.

5. Acquisitions and Dispositions

Acquisitions and dispositions for the periods presented were completed in accordance with our strategy to reposition our investment concentration among the product types and markets in which we operate and to increase our overall investments in quality industrial projects. With the exception of certain properties that have been sold or classified as held for sale, the results of operations for all acquired properties have been included in continuing operations within our consolidated financial statements since their respective dates of acquisition. Transaction costs related to asset acquisitions are capitalized and transaction costs related to business combinations and dispositions are expensed.

Acquisitions

We acquired two properties during the three months ended March 31, 2018. We determined that these two properties did not meet the definition of a business and, accordingly, we accounted for them as asset acquisitions as opposed to business combinations.

The following table summarizes amounts recognized for each major class of assets and liability (in thousands) for these acquisitions during the three months ended March 31, 2018:

Real estate assets	\$21,537
Lease related intangible assets	1,693
Total acquired assets	23,230
Below market lease liability	367
Fair value of acquired net assets	\$22,863

The leases in the acquired properties had a weighted average remaining life at acquisition of approximately 7.4 years.

Fair Value Measurements

We determine the fair value of the individual components of real estate asset acquisitions primarily through calculating the "as-if vacant" value of a building, using an income approach, which relies significantly upon internally determined assumptions. We have determined that these estimates primarily rely upon level 3 inputs, which are unobservable inputs based on our own assumptions. The most significant assumptions used in calculating the "as-if vacant" value for acquisition activity during the three months ended March 31, 2018 are as follows:

	Low	High
Exit capitalization rate	4.50%	4.50%
Net rental rate per square foot	\$9.12	\$10.20

Capitalized acquisition costs were insignificant and the fair value of the two properties acquired during the three months ended March 31, 2018 was substantially the same as the cost of acquisition.

Dispositions

Dispositions of buildings and undeveloped land generated net cash proceeds of \$131.4 million and \$103.1 million during the three months ended March 31, 2018 and 2017, respectively. The number of buildings sold, as well as their classification between continuing and discontinued operations, is disclosed in Note 10.

6. Indebtedness

All debt is issued directly or indirectly by the Partnership. The General Partner does not have any indebtedness, but does guarantee some of the unsecured debt of the Partnership. The following table summarizes the book value and changes in the fair value of our debt (in thousands):

	Book Value at 12/31/2017	Book Value at 3/31/2018	Fair Value at 12/31/2017	Issuances and Assumptions	Payments/Payoffs	Adjustments to Fair Value	Fair Value at 3/31/2018
Fixed rate secured debt	\$ 309,463	\$ 308,099	\$ 325,753	\$ —	\$ (1,345)	\$ (3,756)	\$ 320,652
Variable rate secured debt	2,500	2,500	2,500	—	—	—	2,500
Unsecured debt	2,132,042	2,131,386	2,190,548	—	(656)	(60,502)	2,129,390
Unsecured line of credit	—	75,000	—	75,000	—	—	75,000
Total	\$ 2,444,005	\$ 2,516,985	\$ 2,518,801	\$ 75,000	\$ (2,001)	\$ (64,258)	\$ 2,527,542
Less: Deferred financing costs	21,114	20,529					
Total indebtedness as reported on the consolidated balance sheets	\$ 2,422,891	\$ 2,496,456					

Secured Debt

Because our fixed rate secured debt is not actively traded in any marketplace, we utilized a discounted cash flow methodology to determine its fair value. Accordingly, we calculated fair value by applying an estimate of the current market rate to discount the debt's remaining contractual cash flows. Our estimate of a current market rate, which is the most significant input in the discounted cash flow calculation, is intended to replicate debt of similar maturity and loan-to-value relationship. The estimated rates ranged from 3.90% to 4.00%, depending on the attributes of the specific loans. The current market rates we utilized were internally estimated; therefore, we have concluded that our determination of fair value for our fixed rate secured debt was primarily based upon level 3 inputs.

During the three months ended March 31, 2018, we repaid one fixed rate secured loan, totaling \$215,000, which had a stated interest rate of 5.55%.

Unsecured Debt

At March 31, 2018, all of our unsecured debt bore interest at fixed rates and primarily consisted of unsecured notes that are publicly traded. We utilized broker estimates in estimating the fair value of our fixed rate unsecured debt. Our unsecured notes are thinly traded and, in certain cases, the broker estimates were not based upon comparable transactions. The broker estimates took into account any recent trades within the same series of our fixed rate unsecured debt, comparisons to recent trades of other series of our fixed rate unsecured debt, trades of fixed rate unsecured debt from companies with profiles similar to ours, as well as overall economic conditions. We reviewed these broker estimates for reasonableness and accuracy, considering whether the estimates were based upon market participant assumptions within the principal and most advantageous market and whether any other observable inputs would be more accurate indicators of fair value than the broker estimates. We concluded that the broker estimates were representative of fair value. We have determined that our estimation of the fair value of our fixed rate unsecured debt was primarily based upon level 3 inputs. The estimated trading values of our fixed rate unsecured debt, depending on the maturity and coupon rates, ranged from 95.00% to 122.00% of face value.

The indentures (and related supplemental indentures) governing our outstanding series of unsecured notes also require us to comply with financial ratios and other covenants regarding our operations. We were in compliance with all such financial covenants at March 31, 2018.

Unsecured Line of Credit

Our unsecured line of credit at March 31, 2018 is described as follows (in thousands):

Description	Borrowing Capacity	Maturity Date	Outstanding Balance at March 31, 2018
Unsecured Line of Credit - Partnership	\$ 1,200,000	January 30, 2022	\$ 75,000

The Partnership's unsecured line of credit has an interest rate on borrowings of LIBOR plus 0.875% (equal to 2.75% for outstanding borrowings at March 31, 2018) and has a maturity date of January 30, 2022, with options to extend until January 30, 2023. Subject to certain conditions, the terms also include an option to increase the facility by up to an additional \$800.0 million, for a total of up to \$2.00 billion. This line of credit provides us with an option to obtain borrowings from financial institutions that participate in the line at rates that may be lower than the stated interest rate, subject to certain restrictions.

This line of credit contains financial covenants that require us to meet certain financial ratios and defined levels of performance, including those related to fixed charge coverage, unsecured interest expense coverage and debt-to-asset value (with asset value being defined in the Partnership's unsecured line of credit agreement). At March 31, 2018, we were in compliance with all financial covenants under this line of credit.

We utilize a discounted cash flow methodology in order to estimate the fair value of outstanding borrowings on our unsecured line of credit. To the extent that credit spreads have changed since the origination of the line of credit, the net present value of the difference between future contractual interest payments and future interest payments based on our estimate of a current market rate would represent the difference between the book value and the fair value. Our estimate of a current market rate is based upon the rate, considering current market conditions and our specific credit profile, at which we estimate we could obtain similar borrowings. As our credit spreads have not changed appreciably, we believe that the contractual interest rate and the current market rate on the line of credit are the same. The current market rate is internally estimated and therefore is primarily based upon a level 3 input.

7. Related Party Transactions

We provide property management, asset management, leasing, construction and other tenant-related services to unconsolidated joint ventures in which we have equity interests. We recorded the corresponding fees based on contractual terms that approximate market rates for these types of services and have eliminated our ownership

percentage of these fees in the consolidated financial statements. The following table summarizes the fees earned from these joint ventures, prior to the elimination of our ownership percentage (in thousands):

	Three Months Ended March 31, 2018		2017
Management fees	\$442	\$811	
Leasing fees	302	434	
Construction and development fees	697	624	

8. Net Income per Common Share or Common Unit

Basic net income per common share or Common Unit is computed by dividing net income attributable to common shareholders or common unitholders, less dividends or distributions on share-based awards expected to vest (referred to as "participating securities" and primarily composed of unvested restricted stock units), by the weighted average number of common shares or Common Units outstanding for the period.

Diluted net income per common share is computed by dividing the sum of net income attributable to common shareholders and the noncontrolling interest in earnings allocable to Limited Partner Units (to the extent the Limited Partner Units are dilutive), less dividends or distributions on participating securities that are anti-dilutive, by the sum of the weighted average number of common shares outstanding and, to the extent they are dilutive, weighted average number of Limited Partner Units outstanding and any potential dilutive securities for the period. Diluted net income per Common Unit is computed by dividing the net income attributable to common unitholders, less dividends or distributions on participating securities that are anti-dilutive, by the sum of the weighted average number of Common Units outstanding and any potential dilutive securities for the period. The following table reconciles the components of basic and diluted net income per common share or Common Unit (in thousands):

	Three Months Ended March 31, 2018		2017
<u>General Partner</u>			
Net income attributable to common shareholders	\$72,963	\$70,200	
Less: dividends on participating securities	(437)	(542)	
Basic net income attributable to common shareholders	72,526	69,658	
Add back dividends on dilutive participating securities	—	305	
Noncontrolling interest in earnings of common unitholders	683	652	
Diluted net income attributable to common shareholders	\$		