

HCP, INC.  
Form 10-Q  
August 01, 2017  
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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 June 30, 2017.

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission file number 001-08895

HCP, INC.  
(Exact name of registrant as specified in its charter)

Maryland 33-0091377  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)  
1920 Main Street, Suite 1200  
Irvine, CA 92614  
(Address of principal executive offices)  
(949) 407-0700  
(Registrant's telephone number, including area code)  
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES NO

Indicate by check mark whether the registrant has submitted electronically 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 such shorter period that the registrant was required to submit and post such files). YES NO

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

|   |                           |
|---|---------------------------|
| Large Accelerated Filer                       | Accelerated Filer         |
| Non-accelerated Filer                         | Smaller Reporting Company |
| (Do not check if a 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

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Exchange Act.

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

At July 28, 2017, there were 468,963,146 shares of the registrant's \$1.00 par value common stock outstanding.

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HCP, Inc.

## CONSOLIDATED BALANCE SHEETS

(In thousands, except share and per share data)

(Unaudited)

|  | June 30,<br>2017 | December 31,<br>2016 |
|--|------------------|----------------------|
| <b>ASSETS</b>  |                  |                      |
| Real Estate:   |                  |                      |
| Buildings and improvements   | \$11,114,139     | \$11,692,654         |
| Development costs and construction in progress   | 444,528          | 400,619              |
| Land   | 1,765,305        | 1,881,487            |
| Accumulated depreciation and amortization  | (2,672,489 )     | (2,648,930 )         |
| Net real estate  | 10,651,483       | 11,325,830           |
| Net investment in direct financing leases  | 711,777          | 752,589              |
| Loans receivable, net  | 393,575          | 807,954              |
| Investments in and advances to unconsolidated joint ventures   | 829,231          | 571,491              |
| Accounts receivable, net of allowance of \$4,104 and \$4,459, respectively   | 36,969           | 45,116               |
| Cash and cash equivalents  | 391,965          | 94,730               |
| Restricted cash  | 61,481           | 42,260               |
| Intangible assets, net   | 414,404          | 479,805              |
| Assets held for sale, net  | —                | 927,866              |
| Other assets, net  | 611,690          | 711,624              |
| Total assets   | \$14,102,575     | \$15,759,265         |
| <b>LIABILITIES AND EQUITY</b>  |                  |                      |
| Bank line of credit  | \$136,311        | \$899,718            |
| Term loans   | 218,832          | 440,062              |
| Senior unsecured notes   | 6,889,045        | 7,133,538            |
| Mortgage debt  | 146,337          | 623,792              |
| Other debt   | 94,801           | 92,385               |
| Intangible liabilities, net  | 51,463           | 58,145               |
| Liabilities of assets held for sale, net   | —                | 3,776                |
| Accounts payable and accrued liabilities   | 389,690          | 417,360              |
| Deferred revenue   | 147,155          | 149,181              |
| Total liabilities  | 8,073,634        | 9,817,957            |
| Commitments and contingencies  |                  |                      |
| Common stock, \$1.00 par value: 750,000,000 shares authorized; 468,879,344 and 468,081,489 shares issued and outstanding, respectively | 468,879          | 468,081              |
| Additional paid-in capital   | 8,216,781        | 8,198,890            |
| Cumulative dividends in excess of earnings   | (2,956,324 )     | (3,089,734 )         |
| Accumulated other comprehensive loss   | (27,289 )        | (29,642 )            |
| Total stockholders' equity   | 5,702,047        | 5,547,595            |
| Joint venture partners   | 149,456          | 214,377              |
| Non-managing member unitholders  | 177,438          | 179,336              |
| Total noncontrolling interests   | 326,894          | 393,713              |
| Total equity   | 6,028,941        | 5,941,308            |
| Total liabilities and equity   | \$14,102,575     | \$15,759,265         |

See accompanying Notes to the Unaudited Consolidated Financial Statements.



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HCP, Inc.

## CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

(Unaudited)

|   | Three Months Ended<br>June 30, |           | Six Months Ended<br>June 30, |           |
|---|--------------------------------|-----------|------------------------------|-----------|
|   | 2017                           | 2016      | 2017                         | 2016      |
| Revenues:   |                                |           |                              |           |
| Rental and related revenues   | \$263,820                      | \$292,168 | \$550,038                    | \$582,548 |
| Tenant recoveries   | 35,259                         | 33,531    | 68,934                       | 64,906    |
| Resident fees and services  | 125,416                        | 164,202   | 265,648                      | 329,965   |
| Income from direct financing leases   | 13,564                         | 15,647    | 27,276                       | 30,557    |
| Interest income   | 20,869                         | 32,787    | 39,200                       | 50,816    |
| Total revenues  | 458,928                        | 538,335   | 951,096                      | 1,058,792 |
| Costs and expenses:   |                                |           |                              |           |
| Interest expense  | 77,788                         | 121,333   | 164,506                      | 243,395   |
| Depreciation and amortization   | 130,751                        | 139,919   | 267,305                      | 279,774   |
| Operating   | 153,163                        | 179,080   | 312,244                      | 355,037   |
| General and administrative  | 21,286                         | 22,779    | 43,764                       | 48,230    |
| Acquisition and pursuit costs   | 867                            | 823       | 1,924                        | 3,298     |
| Impairment  | 56,682                         | —         | 56,682                       | —         |
| Total costs and expenses  | 440,537                        | 463,934   | 846,425                      | 929,734   |
| Other income:   |                                |           |                              |           |
| Gain on sales of real estate, net   | 412                            | 119,614   | 317,670                      | 119,614   |
| Other income, net   | 71                             | 2,340     | 51,279                       | 3,632     |
| Total other income, net   | 483                            | 121,954   | 368,949                      | 123,246   |
| Income before income taxes and equity income (loss) from<br>unconsolidated joint ventures | 18,874                         | 196,355   | 473,620                      | 252,304   |
| Income tax benefit (expense)  | 2,987                          | 2,179     | 9,149                        | (1,525 )  |
| Equity income (loss) from unconsolidated joint ventures                                   | 240                            | (1,067 )  | 3,509                        | (1,975 )  |
| Income from continuing operations   | 22,101                         | 197,467   | 486,278                      | 248,804   |
| Discontinued operations:  |                                |           |                              |           |
| Income before income taxes  | —                              | 107,551   | —                            | 225,293   |
| Income taxes  | —                              | (176 )    | —                            | (49,510 ) |
| Total discontinued operations   | —                              | 107,375   | —                            | 175,783   |
| Net income  | 22,101                         | 304,842   | 486,278                      | 424,587   |
| Noncontrolling interests' share in earnings   | (2,718 )                       | (3,125 )  | (5,750 )                     | (6,751 )  |
| Net income attributable to HCP, Inc.  | 19,383                         | 301,717   | 480,528                      | 417,836   |
| Participating securities' share in earnings   | (100 )                         | (342 )    | (674 )                       | (651 )    |
| Net income applicable to common shares  | \$19,283                       | \$301,375 | \$479,854                    | \$417,185 |
| Basic earnings per common share:  |                                |           |                              |           |
| Continuing operations   | \$0.04                         | \$0.42    | \$1.02                       | \$0.52    |
| Discontinued operations   | —                              | 0.23      | —                            | 0.37      |
| Net income applicable to common shares  | \$0.04                         | \$0.65    | \$1.02                       | \$0.89    |
| Diluted earnings per common share:  |                                |           |                              |           |
| Continuing operations   | \$0.04                         | \$0.42    | \$1.02                       | \$0.52    |
| Discontinued operations   | —                              | 0.22      | —                            | 0.37      |
| Net income applicable to common shares  | \$0.04                         | \$0.64    | \$1.02                       | \$0.89    |
| Weighted average shares used to calculate earnings per common share:                      |                                |           |                              |           |

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|  |         |         |         |         |
|--|---------|---------|---------|---------|
| Basic  | 468,646 | 467,084 | 468,474 | 466,579 |
| Diluted  | 468,839 | 471,425 | 473,366 | 466,777 |
| Dividends declared per common share  | \$0.37  | \$0.575 | \$0.74  | \$1.15  |
| See accompanying Notes to the Unaudited Consolidated Financial Statements. |         |         |         |         |

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HCP, Inc.

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands)

(Unaudited)

|  | Three Months Ended<br>June 30, |           | Six Months Ended<br>June 30, |           |   |
|--|--------------------------------|-----------|------------------------------|-----------|---|
|  | 2017                           | 2016      | 2017                         | 2016      |   |
| Net income   | \$22,101                       | \$304,842 | \$486,278                    | \$424,587 |   |
| Other comprehensive income (loss):   |                                |           |                              |           |   |
| Change in net unrealized (losses) gains on securities                      | (3                             | ) 10      | 6                            | (5        | ) |
| Change in net unrealized gains (losses) on cash flow hedges:               |                                |           |                              |           |   |
| Unrealized (losses) gains  | (6,131                         | ) 1,038   | (6,433                       | ) 348     |   |
| Reclassification adjustment realized in net income                         | (193                           | ) 171     | 20                           | 340       |   |
| Change in Supplemental Executive Retirement Plan obligation                | 74                             | 71        | 148                          | 141       |   |
| Foreign currency translation adjustment                                    | 7,622                          | (355      | ) 8,612                      | (1,092    | ) |
| Total other comprehensive income (loss)                                    | 1,369                          | 935       | 2,353                        | (268      | ) |
| Total comprehensive income   | 23,470                         | 305,777   | 488,631                      | 424,319   |   |
| Total comprehensive income attributable to noncontrolling interests        | (2,718                         | ) (3,125  | ) (5,750                     | ) (6,751  | ) |
| Total comprehensive income attributable to HCP, Inc.                       | \$20,752                       | \$302,652 | \$482,881                    | \$417,568 |   |
| See accompanying Notes to the Unaudited Consolidated Financial Statements. |                                |           |                              |           |   |



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HCP, Inc.

## CONSOLIDATED STATEMENTS OF EQUITY

(In thousands, except per share data)

(Unaudited)

|  | Common Stock |           | Additional<br>Paid-In<br>Capital | Cumulative<br>Dividends<br>In Excess<br>Of Earnings | Accumulated<br>Other<br>Comprehensive<br>Loss | Total<br>Stockholders'<br>Equity | Total<br>Noncontrolling<br>Interests | Total<br>Equity |
|--|--------------|-----------|----------------------------------|---|---|----------------------------------|--------------------------------------|-----------------|
|  | Shares       | Amount    |                                  |   |   |                                  |                                      |                 |
| January 1, 2017                              | 468,081      | \$468,081 | \$8,198,890                      | \$(3,089,734)                                       | \$(29,642 )                                   | \$5,547,595                      | \$393,713                            | \$5,941,308     |
| Net income                                   | —            | —         | —                                | 480,528   | —   | 480,528                          | 5,750                                | 486,278         |
| Other comprehensive income                   | —            | —         | —                                | —   | 2,353   | 2,353                            | —                                    | 2,353           |
| Issuance of common stock, net                | 850          | 850       | 12,443                           | —   | —   | 13,293                           | —                                    | 13,293          |
| Conversion of DownREIT units to common stock | 68           | 68        | 2,003                            | —   | —   | 2,071                            | (2,071 )                             | —               |
| Repurchase of common stock                   | (141 )       | (141 )    | (4,220 )                         | —   | —   | (4,361 )                         | —                                    | (4,361 )        |
| Exercise of stock options                    | 21           | 21        | 573                              | —   | —   | 594                              | —                                    | 594             |
| Amortization of deferred compensation        | —            | —         | 7,092                            | —   | —   | 7,092                            | —                                    | 7,092           |
| Common dividends (\$0.74 per share)          | —            | —         | —                                | (347,118 )  | —   | (347,118 )                       | —                                    | (347,118 )      |
| Distributions to noncontrolling interests    | —            | —         | —                                | —   | —   | —                                | (13,087 )                            | (13,087 )       |
| Issuances of noncontrolling interests        | —            | —         | —                                | —   | —   | —                                | 650                                  | 650             |
| Deconsolidation of noncontrolling interests  | —            | —         | —                                | —   | —   | —                                | (58,061 )                            | (58,061 )       |
| June 30, 2017                                | 468,879      | \$468,879 | \$8,216,781                      | \$(2,956,324)                                       | \$(27,289 )                                   | \$5,702,047                      | \$326,894                            | \$6,028,941     |
|  | Common Stock |           | Additional<br>Paid-In<br>Capital | Cumulative<br>Dividends<br>In Excess<br>Of Earnings | Accumulated<br>Other<br>Comprehensive<br>Loss | Total<br>Stockholders'<br>Equity | Total<br>Noncontrolling<br>Interests | Total<br>Equity |
|  | Shares       | Amount    |                                  |   |   |                                  |                                      |                 |
| January 1, 2016                              | 465,488      | \$465,488 | \$11,647,039                     | \$(2,738,414)                                       | \$(30,470 )                                   | \$9,343,643                      | \$402,674                            | \$9,746,317     |
| Net income                                   | —            | —         | —                                | 417,836   | —   | 417,836                          | 6,751                                | 424,587         |
| Other comprehensive                          | —            | —         | —                                | —   | (268 )  | (268 )                           | —                                    | (268 )          |

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|  |         |           |              |               |             |             |           |             |
|--|---------|-----------|--------------|---------------|-------------|-------------|-----------|-------------|
| income   |         |           |              |               |             |             |           |             |
| Issuance of common stock, net  | 1,715   | 1,715     | 41,357       | —             | —           | 43,072      | —         | 43,072      |
| Conversion of DownREIT units to common stock                               | 120     | 120       | 4,902        | —             | —           | 5,022       | (5,022 )  | —           |
| Repurchase of common stock   | (109 )  | (109 )    | (3,765 )     | —             | —           | (3,874 )    | —         | (3,874 )    |
| Exercise of stock options  | 111     | 111       | 2,741        | —             | —           | 2,852       | —         | 2,852       |
| Amortization of deferred compensation                                      | —       | —         | 9,505        | —             | —           | 9,505       | —         | 9,505       |
| Common dividends (\$1.15 per share)  | —       | —         | —            | (537,061 )    | —           | (537,061 )  | —         | (537,061 )  |
| Distributions to noncontrolling interests                                  | —       | —         | (36 )        | —             | —           | (36 )       | (12,437 ) | (12,473 )   |
| Issuances of noncontrolling interests                                      | —       | —         | —            | —             | —           | —           | 3,225     | 3,225       |
| Deconsolidation of noncontrolling interests                                | —       | —         | (36 )        | 475           | —           | 439         | 67        | 506         |
| June 30, 2016  | 467,325 | \$467,325 | \$11,701,707 | \$(2,857,164) | \$(30,738 ) | \$9,281,130 | \$395,258 | \$9,676,388 |
| See accompanying Notes to the Unaudited Consolidated Financial Statements. |         |           |              |               |             |             |           |             |

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HCP, Inc.

## CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

|   | Six Months Ended<br>June 30, |            |
|---|------------------------------|------------|
|   | 2017                         | 2016       |
| Cash flows from operating activities:   |                              |            |
| Net income  | \$486,278                    | \$424,587  |
| Adjustments to reconcile net income to net cash provided by operating activities:   |                              |            |
| Depreciation and amortization of real estate, in-place lease and other intangibles: |                              |            |
| Continuing operations   | 267,305                      | 279,774    |
| Discontinued operations   | —                            | 2,934      |
| Amortization of deferred compensation   | 7,092                        | 9,505      |
| Amortization of deferred financing costs  | 7,702                        | 10,561     |
| Straight-line rents   | (8,176 )                     | (11,117 )  |
| Equity (income) loss from unconsolidated joint ventures                             | (3,509 )                     | 1,975      |
| Distributions of earnings from unconsolidated joint ventures                        | 18,528                       | 3,202      |
| Gain on sales of real estate, net   | (317,670 )                   | (119,614 ) |
| Allowance for loan losses   | 56,682                       | —          |
| Deferred income tax (benefit) expense   | (12,472 )                    | 49,156     |
| Foreign exchange and other gains, net   | (845 )                       | (91 )      |
| Gain on sale of marketable securities   | (50,895 )                    | —          |
| Other non-cash items  | (1,478 )                     | (1,502 )   |
| Changes in:   |                              |            |
| Accounts receivable, net  | (2,002 )                     | (2,871 )   |
| Other assets, net   | (6,775 )                     | (2,892 )   |
| Accounts payable and accrued liabilities  | (8,176 )                     | 23,305     |
| Net cash provided by operating activities   | 431,589                      | 666,912    |
| Cash flows from investing activities:   |                              |            |
| Acquisitions of real estate   | (26,446 )                    | (94,271 )  |
| Development of real estate  | (157,898 )                   | (204,624 ) |
| Leasing costs and tenant and capital improvements                                   | (48,575 )                    | (41,161 )  |
| Proceeds from sales of real estate, net   | 1,195,860                    | 96,652     |
| Contributions to unconsolidated joint ventures                                      | (21,302 )                    | (10,156 )  |
| Distributions in excess of earnings from unconsolidated joint ventures              | 1,609                        | 6,421      |
| Net proceeds from the RIDEA II transaction (Note 4)                                 | 480,614                      | —          |
| Proceeds from the sales of Four Seasons investments                                 | 135,538                      | —          |
| Principal repayments on direct financing leases, loans receivable and other         | 414,221                      | 205,576    |
| Investments in loans receivable and other   | (18,433 )                    | (122,113 ) |
| Decrease in restricted cash   | 2,398                        | 10,058     |
| Net cash provided by (used in) investing activities                                 | 1,957,586                    | (153,618 ) |
| Cash flows from financing activities:   |                              |            |
| Net (repayments) borrowings under bank line of credit                               | (441,581 )                   | 642,898    |
| Repayments under bank line of credit  | (339,826 )                   | (135,000 ) |
| Repayment of term loans   | (234,459 )                   | —          |
| Repayments of senior unsecured notes  | (250,000 )                   | (500,000 ) |
| Issuance of mortgage and other debt   | 5,395                        | —          |
| Repayments of mortgage and other debt   | (481,667 )                   | (246,387 ) |

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|  |              |            |
|--|--------------|------------|
| Issuance of common stock and exercise of options                           | 13,887       | 45,924     |
| Repurchase of common stock   | (4,361 )     | (3,874 )   |
| Dividends paid on common stock   | (347,118 )   | (537,061 ) |
| Issuance of noncontrolling interests                                       | 650          | 3,225      |
| Distributions to noncontrolling interests                                  | (13,087 )    | (12,473 )  |
| Net cash used in financing activities                                      | (2,092,167 ) | (742,748 ) |
| Effect of foreign exchange on cash and cash equivalents                    | 227          | (596 )     |
| Net increase (decrease) in cash and cash equivalents                       | 297,235      | (230,050 ) |
| Cash and cash equivalents, beginning of period                             | 94,730       | 346,500    |
| Cash and cash equivalents, end of period                                   | \$ 391,965   | \$ 116,450 |
| See accompanying Notes to the Unaudited Consolidated Financial Statements. |              |            |

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HCP, Inc.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1. Business

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

NOTE 2. Summary of Significant Accounting Policies

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Basis of Presentation

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

The consolidated financial statements include the accounts of HCP, Inc., its wholly-owned subsidiaries, joint ventures ("JVs") and variable interest entities ("VIEs") that it controls through voting rights or other means. Intercompany transactions and balances have been eliminated upon consolidation. In the opinion of management, all adjustments (consisting of normal recurring adjustments) necessary to present fairly the Company's financial position, results of operations and cash flows have been included. Operating results for the three and six months ended June 30, 2017 are not necessarily indicative of the results that may be expected for the year ending December 31, 2017. The accompanying unaudited interim financial information should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2016 included in the Company's Annual Report on Form 10-K filed with the U.S. Securities and Exchange Commission ("SEC").

Real Estate

On January 1, 2017 the Company adopted Accounting Standards Update ("ASU") No. 2017-01, Clarifying the Definition of a Business ("ASU 2017-01") which narrows the Financial Accounting Standards Board's ("FASB") definition of a business and provides a framework that gives entities a basis for making reasonable judgments about whether a transaction involves an asset, or a group of assets, or a business. ASU 2017-01 states that when substantially all of the fair value of the gross assets acquired (or disposed of) is concentrated in a single identifiable asset or group of similar identifiable assets, the set is not a business. If this initial test is not met, a set cannot be considered a business unless it includes an acquired input and a substantive process that together significantly contribute to the ability to create outputs. In addition, ASU 2017-01 clarifies the requirements for a set of activities to be considered a business and narrows the definition of an output. This ASU is to be applied prospectively and the Company expects that a majority of its future real estate acquisitions and dispositions will be deemed asset transactions rather than business combinations. As a result, for asset acquisitions the Company will record identifiable assets acquired, liabilities assumed and any associated noncontrolling interests at cost on a relative fair value basis. In addition, for such asset acquisitions, no goodwill will be recognized, third party transaction costs will be capitalized and any associated contingent consideration will be recorded when the contingency is resolved.

Segment Reporting

The Company's reportable segments, based on how it evaluates its business and allocates resources, are as follows: (i) senior housing triple-net, (ii) SHOP, (iii) life science and (iv) medical office.

Prior to the third quarter of 2016, the Company had five reportable segments: (i) senior housing, (ii) post-acute/skilled

nursing, (iii) life science, (iv) medical office and (v) hospital. During the third quarter of 2016, primarily as a result of the planned spin-off of Quality Care Properties, Inc. ("QCP") (NYSE:QCP), the Company revised its operating analysis structure and changed its reportable segments. The Company believes the change to its reportable segments is appropriate and consistent with how its chief operating decision makers review the Company's operating results and determine resource allocations. Accordingly, all prior period segment information has been reclassified to conform to the current period presentation.

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### Reclassifications

Certain amounts in the Company's consolidated financial statements have been reclassified for prior periods to conform to the current period presentation. Certain prior period amounts have been reclassified on consolidated statements of operations for discontinued operations (see Note 4). See Segment Reporting above for additional reclassifications.

### Recent Accounting Pronouncements

In February 2017, the FASB issued ASU No. 2017-05, Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets ("ASU 2017-05"). The amendments in ASU 2017-05 clarify the scope of the FASB's recently established guidance on nonfinancial asset derecognition which applies to the derecognition of all nonfinancial assets and in-substance nonfinancial assets. In addition, ASU 2017-05 clarifies the accounting for partial sales of nonfinancial assets and in-substance nonfinancial assets to align with the new revenue recognition standard (see below). ASU 2017-05 is effective for annual periods beginning after December 15, 2017, including interim periods within, and must be adopted in conjunction with the Revenue ASUs (as defined below). ASU 2017-05 can be adopted using a full retrospective approach or a modified retrospective approach, resulting in a cumulative-effect adjustment to equity as of the beginning of the fiscal year in which the guidance is effective. The Company has not yet elected a transition method and is evaluating the complete impact of the adoption of the Revenue ASUs (see below) on January 1, 2018 to its consolidated financial position, results of operations and disclosures. The Company expects to complete its evaluation of the impacts of the Revenue ASUs during the second half of 2017. In June 2016, the FASB issued ASU No. 2016-13, Measurement of Credit Losses on Financial Instruments ("ASU 2016-13"). ASU 2016-13 is intended to improve financial reporting by requiring timelier recognition of credit losses on loans and other financial instruments held by financial institutions and other organizations. The amendments in ASU 2016-13 eliminate the "probable" initial threshold for recognition of credit losses in current accounting guidance and, instead, reflect an entity's current estimate of all expected credit losses over the life of the financial instrument. Previously, when credit losses were measured under current accounting guidance, an entity generally only considered past events and current conditions in measuring the incurred loss. The amendments in ASU 2016-13 broaden the information that an entity must consider in developing its expected credit loss estimate for assets measured either collectively or individually. The use of forecasted information incorporates more timely information in the estimate of expected credit loss. ASU 2016-13 is effective for fiscal years, and interim periods within, beginning after December 15, 2019. Early adoption is permitted for fiscal years, and interim periods within, beginning after December 15, 2018. A reporting entity is required to apply the amendments in ASU 2016-13 using a modified retrospective approach by recording a cumulative-effect adjustment to equity as of the beginning of the fiscal year of adoption. A prospective transition approach is required for debt securities for which an other-than-temporary impairment had been recognized before the effective date. Upon adoption of ASU 2016-13, the Company is required to reassess its financing receivables, including direct finance leases and loans receivable, and expects that application of ASU 2016-13 may result in the Company recognizing credit losses at an earlier date than would otherwise be recognized under current accounting guidance. The Company is evaluating the impact of the adoption of ASU 2016-13 on January 1, 2020 to its consolidated financial position and results of operations.

Between May 2014 and May 2016, the FASB issued three ASUs changing the requirements for recognizing and reporting revenue (together, herein referred to as the "Revenue ASUs"): (i) ASU No. 2014-09, Revenue from Contracts with Customers ("ASU 2014-09"), (ii) ASU No. 2016-08, Principal versus Agent Considerations (Reporting Revenue Gross versus Net) ("ASU 2016-08") and (iii) ASU No. 2016-12, Narrow-Scope Improvements and Practical Expedients ("ASU 2016-12"). ASU 2014-09 provides guidance for revenue recognition to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2016-08 is intended to improve the operability and understandability of the implementation guidance on principal versus agent considerations. ASU 2016-12 provides practical expedients and improvements on the previously narrow scope of ASU 2014-09. In August 2015, the FASB issued ASU No. 2015-14, Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date ("ASU 2015-14"). ASU 2015-14 defers the effective date of ASU 2014-09 by one year to fiscal years, and interim periods within, beginning after December 15, 2017. All subsequent ASUs related to ASU 2014-09, including ASU 2016-08 and ASU 2016-12,

assumed the deferred effective date enforced by ASU 2015-14. Early adoption of the Revenue ASUs is permitted for annual periods, and interim periods within, beginning after December 15, 2016. A reporting entity may apply the amendments in the Revenue ASUs using either a modified retrospective approach, by recording a cumulative-effect adjustment to equity as of the beginning of the fiscal year of adoption or full retrospective approach.

As the primary source of revenue for the Company is generated through leasing arrangements, which are excluded from the Revenue ASUs (as it relates to the timing and recognition of revenue), the Company expects that it may be impacted in its recognition of non-lease revenue, such as certain resident fees in its RIDEA structures (a portion of which are not generated through leasing arrangements), non-lease components of revenue from lease agreements and its recognition of real estate sale transactions. Under ASU 2014-09, revenue recognition for real estate sales is largely based on the transfer of control versus continuing involvement under current guidance. As a result, the Company generally expects that the new guidance will result in more transactions qualifying as sales of real estate and revenue being recognized at an earlier date than under current accounting guidance. Additionally, upon adoption of the Revenue ASUs in 2018, the Company anticipates that it will be required to separately disclose the components of



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its total revenue between lease revenue accounted for under existing lease guidance and service revenue accounted for under the new Revenue ASUs, including non-lease components such as certain services embedded in base leasing fees. The Company has not yet elected a transition method and is evaluating the complete impact of the adoption of the Revenue ASUs on January 1, 2018 to its consolidated financial position, results of operations and disclosures. The Company expects to complete its evaluation of the impacts of the Revenue ASUs during the second half of 2017. In February 2016, the FASB issued ASU No. 2016-02, Leases (“ASU 2016-02”). ASU 2016-02 amends the current accounting for leases to: (i) require lessees to put most leases on their balance sheets, but continue recognizing expenses on their income statements in a manner similar to requirements under current accounting guidance, (ii) eliminate current real estate specific lease provisions and (iii) modify the classification criteria and accounting for sales-type leases for lessors. ASU 2016-02 is effective for fiscal years, and interim periods within, beginning after December 15, 2018. Early adoption is permitted. The transition method required by ASU 2016-02 varies based on the specific amendment being adopted. As a result of adopting ASU 2016-02, the Company will recognize all of its significant operating leases for which it is the lessee, including corporate office leases and ground leases, on its consolidated balance sheets and will capitalize fewer legal costs related to the drafting and execution of its lease agreements. From a lessor perspective, the Company expects that it will be required to further bifurcate lease agreements to separately recognize and disclose non-lease components that are executory in nature. Lease components will continue to be recognized on a straight-line basis over the lease term and certain non-lease components will be accounted for under the new revenue recognition guidance in ASU 2014-09. The disaggregated disclosure of lease and executory non-lease components (e.g., maintenance) will be required upon the adoption of ASU 2016-02. The Company anticipates that it will elect a practical expedient offered in ASU 2016-02 that allows an entity to not reassess the following upon adoption (must be elected as a group): (i) whether an expired or existing contract contains a lease arrangement, (ii) lease classification related to expired or existing lease arrangements, or (iii) whether costs incurred on expired or existing leases qualify as initial direct costs. The Company does not expect the bifurcation of non-lease components from a lease agreement to significantly impact the existing revenue recognition pattern. The Company is still evaluating the complete impact of the adoption of ASU 2016-02 on January 1, 2019 to its consolidated financial position, results of operations and disclosures.

The following ASUs have been issued, but not yet adopted, and the Company does not expect a material impact to its consolidated financial position, results of operations, cash flows, or disclosures upon adoption:

ASU No. 2017-04, Simplifying the Test for Goodwill Impairment (“ASU 2017-04”). ASU 2017-04 is effective for fiscal years, including interim periods within, beginning after December 15, 2019 (upon the first goodwill impairment test performed during that fiscal year). Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. A reporting entity must apply the amendments in ASU 2017-04 using a prospective approach.

ASU No. 2016-18, Restricted Cash (“ASU 2016-18”). ASU 2016-18 is effective for fiscal years, and interim periods within, beginning after December 15, 2017. Early adoption is permitted. A reporting entity must apply the amendments in ASU 2016-18 using a full retrospective approach.

ASU No. 2016-16, Intra-Entity Transfers of Assets Other Than Inventory (“ASU 2016-16”). ASU 2016-16 is effective for fiscal years, and interim periods within, beginning after December 15, 2017. Early adoption is permitted as of the first interim period presented in any year following issuance. A reporting entity must apply the amendments in ASU 2016-16 using a modified retrospective approach by recording a cumulative-effect adjustment to equity as of the beginning of the fiscal year of adoption.

ASU No. 2016-15, Classification of Certain Cash Receipts and Cash Payments (“ASU 2016-15”). ASU 2016-15 is effective for fiscal years, and interim periods within, beginning after December 15, 2017. Early adoption is permitted. A reporting entity must apply the amendments in ASU 2016-15 using a full retrospective approach.

ASU No. 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities (“ASU 2016-01”). ASU 2016-01 is effective for fiscal years, and interim periods within, beginning after December 15, 2017. Early adoption is permitted only for updates to certain disclosure requirements. A reporting entity is required to apply the amendments in ASU 2016-01 using a modified retrospective approach by recording a cumulative-effect adjustment to equity as of the beginning of the fiscal year of adoption.



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## NOTE 3. Real Estate Property Investments

The following table summarizes the Company's real estate acquisitions for the six months ended June 30, 2017 (in thousands):

| Segment        | Consideration |             | Assets Acquired |             |
|----------------|---------------|-------------|-----------------|-------------|
|                | Cash          |             |                 |             |
|                | Paid/         | Liabilities | Real Estate     | Net         |
|                | Debt          | Assumed     |                 | Intangibles |
|                | Settled       |             |                 |             |
| Life science   | \$26,019      | \$ 155      | \$24,398        | \$ 1,776    |
| Medical office | 427           | 5           | 432             | —           |
|                | \$26,446      | \$ 160      | \$24,830        | \$ 1,776    |

The following table summarizes the Company's real estate acquisitions for the six months ended June 30, 2016 (in thousands):

| Segment                       | Consideration |             | Assets Acquired |             |
|-------------------------------|---------------|-------------|-----------------|-------------|
|                               | Cash          |             |                 |             |
|                               | Paid/         | Liabilities | Real Estate     | Net         |
|                               | Debt          | Assumed     |                 | Intangibles |
|                               | Settled       |             |                 |             |
| Senior housing triple-net     | \$76,362      | \$ 1,200    | \$71,875        | \$ 5,687    |
| Other non-reportable segments | 17,909        | —           | 16,596          | 1,313       |
|                               | \$94,271      | \$ 1,200    | \$88,471        | \$ 7,000    |

## NOTE 4. Discontinued Operations and Dispositions of Real Estate

## Discontinued Operations - Quality Care Properties, Inc.

On October 31, 2016, the Company completed the spin-off (the "Spin-Off") of its subsidiary, QCP. The Spin-Off included 338 properties, primarily comprised of the HCR ManorCare, Inc. ("HCRMC") direct financing lease ("DFL") investments and an equity investment in HCRMC. QCP is an independent, publicly-traded, self-managed and self-administrated REIT.

In connection with the Spin-Off, the Company entered into a Transition Services Agreement ("TSA") with QCP. Per the terms of the TSA, the Company has agreed to provide certain administrative and support services to QCP on a transitional basis for established fees. The TSA will terminate on the expiration of the term of the last service provided under the agreement, which will be on or prior to October 30, 2017. The TSA provides that QCP generally has the right to terminate a transition service upon thirty days notice to the Company. The TSA contains provisions under which the Company will, subject to certain limitations, be obligated to indemnify QCP for losses incurred by QCP resulting from the Company's breach of the TSA.

Summarized financial information for discontinued operations for the three and six months ended June 30, 2016 is as follows (in thousands):

|                                     | Three<br>Months<br>Ended<br>June 30,<br>2016 | Six<br>Months<br>Ended<br>June 30,<br>2016 |
|-------------------------------------|--|--|
| Revenues:                           |  |  |
| Rental and related revenues         | \$6,908                                      | \$13,722                                   |
| Tenant recoveries                   | 399  | 761  |
| Income from direct financing leases | 116,453                                      | 229,511                                    |

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|                               |           |           |
|-------------------------------|-----------|-----------|
| Total revenues                | 123,760   | 243,994   |
| Costs and expenses:           |           |           |
| Depreciation and amortization | (1,467 )  | (2,934 )  |
| Operating                     | (1,045 )  | (2,043 )  |
| General and administrative    | (14 )     | (62 )     |
| Acquisition and pursuit costs | (13,704 ) | (13,704 ) |
| Other income, net             | 21        | 42        |
| Income before income taxes    | 107,551   | 225,293   |
| Income tax expense            | (176 )    | (49,510 ) |
| Total discontinued operations | \$107,375 | \$175,783 |

Table of Contents**HCR ManorCare, Inc.**

Discontinued operations is primarily comprised of QCP's HCRMC DFL investments. During the six months ended June 30, 2016, the Company received cash payments of \$116 million from the HCRMC DFL investments.

No accretion related to its HCRMC DFL investments was recognized in 2016 due to the Company utilizing a cash basis method of accounting beginning January 1, 2016.

The Company's acquisition of the HCRMC DFL investments in 2011 was subject to federal and state built-in gain tax of up to \$2 billion if all the assets were sold within 10 years of the acquisition date. At the time of acquisition, the Company intended to hold the assets for at least 10 years, at which time the assets would no longer be subject to the built-in gain tax. In December 2015, the U.S. Federal Government passed legislation which permanently reduced the holding period, for federal tax purposes, to 5 years, which the Company satisfied in April 2016. This legislation was not extended to certain states, which maintain a 10 year requirement. During the three months ended March 31, 2016, the Company determined that it may sell assets during the next five years and, therefore, recorded a deferred tax liability of \$49 million representing its estimated exposure to state built-in gain tax.

**Dispositions of Real Estate****Held for Sale**

At June 30, 2017, there were no assets classified as held for sale.

At December 31, 2016, 64 senior housing triple-net facilities, four life science facilities and a SHOP facility were classified as held for sale, with an aggregate carrying value of \$928 million, primarily comprised of real estate assets of \$809 million. All facilities held for sale at December 31, 2016 were sold during the first quarter of 2017.

**2017 Dispositions**

In January 2017, the Company sold four life science facilities in Salt Lake City, Utah for \$76 million, resulting in a net gain on sale of \$45 million.

Also in January 2017, the Company completed the contribution of its ownership interest in RIDEA II to an unconsolidated JV owned by HCP and an investor group led by Columbia Pacific Advisors, LLC ("HCP/CPA PropCo" and "HCP/CPA OpCo," together, the "HCP/CPA JV"). In addition, RIDEA II was recapitalized with \$602 million of debt, of which \$360 million was provided by a third-party and \$242 million was provided by HCP. In return for both transaction elements, the Company received combined proceeds of \$480 million from the HCP/CPA JV and \$242 million in note receivables and retained an approximately 40% beneficial interest in RIDEA II (the note receivable and 40% beneficial interest are herein referred to as the "RIDEA II Investments"). This transaction resulted in the Company deconsolidating the net assets of RIDEA II and recognizing a net gain on sale of \$99 million. The RIDEA II Investments are now recognized and accounted for as equity method investments.

In March 2017, the Company sold 64 senior housing triple-net assets, previously under triple-net leases with Brookdale Senior Living Inc. ("Brookdale"), for \$1.125 billion to affiliates of Blackstone Real Estate Partners VIII, L.P., resulting in a net gain on sale of \$170 million.

In April 2017, the Company sold a land parcel in San Diego, California for \$27 million and one life science building in San Diego, California for \$5 million.

**2016 Dispositions**

During the six months ended June 30, 2016, the Company sold five post-acute/skilled nursing facilities and two senior housing triple-net facilities for \$130 million, a life science facility for \$74 million, two medical office buildings for \$19 million and a SHOP facility for \$6 million and recognized total gain on sales of \$120 million.

**NOTE 5. Net Investment in Direct Financing Leases**


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

|   | June 30,<br>2017 | December 31,<br>2016 |
|---|------------------|----------------------|
| Minimum lease payments receivable         | \$1,081,187      | \$1,108,237          |
| Estimated residual value                  | 500,368          | 539,656              |
| Less unearned income                      | (869,778)        | (895,304)            |
| Net investment in direct financing leases | \$711,777        | \$752,589            |

Properties subject to direct financing leases 29 30

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Certain DFLs contain provisions that allow the tenants to elect to purchase the properties during or at the end of the lease terms for the aggregate initial investment amount plus adjustments, if any, as defined in the lease agreements. Certain leases also permit the Company to require the tenants to purchase the properties at the end of the lease terms. In February 2017, the Company sold a hospital within a DFL in Palm Beach Gardens, Florida for \$43 million to the current tenant.

**Direct Financing Lease Internal Ratings**

The following table summarizes the Company's internal ratings for DFLs at June 30, 2017 (dollars in thousands):

| Segment                       | Carrying Amount | Percentage of DFL Portfolio | Internal Ratings |                 |              |
|-------------------------------|-----------------|-----------------------------|------------------|-----------------|--------------|
|                               |                 |                             | Performing DFLs  | Watch List DFLs | Workout DFLs |
| Senior housing triple-net     | \$627,173       | 88%                         | \$268,815        | \$359,586,000   | \$358,358    |
| Other non-reportable segments | 84,604          | 12                          | 84,604           | —               | —            |
|                               | \$711,777       | 100%                        | \$353,419        | \$358,358       | \$ —         |

Beginning September 30, 2013, the Company placed a 14 property senior housing triple-net DFL (the "DFL Watchlist Portfolio") on nonaccrual status and "Watch List" status. The Company determined that the collection of all rental payments was and continues to be no longer reasonably assured; therefore, rental revenue for the DFL Watchlist Portfolio has been recognized on a cash basis. During both the three months ended June 30, 2017 and 2016, the Company recognized DFL income of \$4 million and received cash payments of \$5 million from the DFL Watchlist Portfolio. During the six months ended June 30, 2017 and 2016, the Company recognized DFL income of \$7 million and \$8 million, respectively, and received cash payments of \$9 million and \$10 million, respectively, from the DFL Watchlist Portfolio. The carrying value of the DFL Watchlist Portfolio was \$358 million and \$361 million at June 30, 2017 and December 31, 2016, respectively.

**NOTE 6. Loans Receivable**

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

|  | June 30, 2017       |               |           | December 31, 2016   |               |           |
|--|---------------------|---------------|-----------|---------------------|---------------|-----------|
|  | Real Estate Secured | Other Secured | Total     | Real Estate Secured | Other Secured | Total     |
| Mezzanine <sup>(1)</sup>                             | \$—                 | \$274,799     | \$274,799 | \$—                 | \$615,188     | \$615,188 |
| Other <sup>(2)</sup>                                 | 176,186             | —             | 176,186   | 195,946             | —             | 195,946   |
| Unamortized discounts, fees and costs <sup>(1)</sup> | —                   | (728)         | (728)     | 413                 | (3,593)       | (3,180)   |
| Allowance for loan losses                            | —                   | (56,682)      | (56,682)  | —                   | —             | —         |
|  | \$176,186           | \$217,389     | \$393,575 | \$196,359           | \$611,595     | \$807,954 |

(1) At December 31, 2016, included £282 million (\$348 million) outstanding and £2 million (\$3 million) of associated unamortized discounts, fees and costs, both related to the HC-One Facility.

(2) At June 30, 2017, included £119 million (\$154 million) outstanding primarily related to Maria Mallaband loans.

**Loans Receivable Internal Ratings**

The following table summarizes the Company's internal ratings for loans receivable at June 30, 2017 (dollars in thousands):

| Investment Type     | Carrying Amount | Percentage of Loan Portfolio | Internal Ratings |                  |               |
|---------------------|-----------------|------------------------------|------------------|------------------|---------------|
|                     |                 |                              | Performing Loans | Watch List Loans | Workout Loans |
| Real estate secured | \$176,186       | 45%                          | \$176,186        | \$—              | \$ —          |
| Other secured       | 217,389         | 55                           | 17,389           | 200,000          | —             |
|                     | \$393,575       | 100%                         | \$193,575        | \$200,000        | \$ —          |

**Real Estate Secured Loans**

Four Seasons Health Care. In March 2017, the Company sold its investment in Four Seasons Health Care's ("Four Seasons") senior secured term loan at par plus accrued interest for £29 million (\$35 million).



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### Other Secured Loans

**HC-One Facility.** On June 30, 2017, the Company received £283 million (\$367 million) from the repayment of its HC-One mezzanine loan.

**Tandem Health Care Loan.** On July 31, 2012, the Company closed a mezzanine loan facility to lend up to \$205 million to Tandem Health Care (“Tandem”), as part of the recapitalization of a post-acute/skilled nursing portfolio (the “Tandem Portfolio”). The Company funded \$100 million (the “First Tranche”) at closing and funded an additional \$102 million (the “Second Tranche”) in June 2013. In May 2015, the Company increased and extended the mezzanine loan facility with Tandem to: (i) fund \$50 million (the “Third Tranche”) and \$5 million (the “Fourth Tranche”), which proceeds were used to repay a portion of Tandem’s existing senior and mortgage debt, respectively; (ii) extend its maturity to October 2018; and (iii) extend the prepayment penalty period through January 2017. The tranches (collectively, the “Tandem Mezzanine Loan”) bear interest at fixed annual rates of 12%, 14%, 6% and 6% per annum for the First, Second, Third and Fourth Tranches, respectively. The blended rate for the Tandem Mezzanine Loan is 11.5% per year.

Tandem leases the entire Tandem Portfolio to Consulate Health Care (“Consulate”) under a master lease (the “Tandem and Consulate Lease”). At June 30, 2017, as a result of the Tandem Portfolio’s operating performance, there are outstanding events of default under the Tandem and Consulate Lease (“Events of Default”) due to: (i) Consulate’s failure to meet certain financial covenants under the Tandem and Consulate Lease and (ii) events of default under Consulate’s working capital facility, which, through a cross-default provision, are Events of Default. Starting in April 2017, Consulate failed to pay the full amount of its rent under the Tandem and Consulate Lease which triggered another Event of Default. Through cross-default provisions, these Events of Default are also events of default under the Tandem Mezzanine Loan and Tandem’s senior mortgage debt (each, a “Loan Event of Default”). The Tandem Mezzanine Loan requires Tandem to pay default interest at a rate of 16.5% per year, during periods in which there is an outstanding Loan Event of Default. Tandem did not pay the additional 5% default interest rate spread above the 11.5% and, therefore created a monetary event of default under the Tandem Mezzanine Loan.

Although Tandem continues to remain current on its non-default interest payment obligations under the Tandem Mezzanine Loan, the Company believes that it is probable it will be unable to collect all interest and principal payments, including default interest payments, according to the contractual terms of the Tandem Mezzanine Loan. As the Tandem Mezzanine Loan is deemed collateral-dependent and the carrying amount of the Tandem Mezzanine Loan exceeded the fair value of the underlying collateral at June 30, 2017, as part of its quarterly review process, the Company recorded an impairment charge and related allowance of \$57 million during the three months ended June 30, 2017, reducing the carrying value to \$200 million, which approximates the fair value of the collateral as of June 30, 2017. The decline in fair value of the collateral was driven by a variety of factors, including recent operating results of the underlying real estate assets, as well as market and industry data, that reflect a declining trend in admissions and a continuing shift away from higher-rate Medicare plans in the post-acute/skilled nursing sector. The calculation of the fair value of the collateral was primarily based on an income approach technique and relies on forecasted EBITDAR (defined as earnings before interest, taxes, depreciation and amortization, and rent) and market data, including, but not limited to, sales price per unit/bed, rent coverage ratios, and real estate capitalization rates. All valuation inputs are considered to be Level 2 measurements within the fair value hierarchy.

Beginning in the first quarter of 2017, the Company elected to recognize interest income on a cash basis. During both the three months ended June 30, 2017 and 2016, the Company recognized interest income and received cash payments of \$7 million from Tandem. During both the six months ended June 30, 2017 and 2016, the Company recognized interest income and received cash payments of \$14 million from Tandem.

The Company entered into a forbearance agreement with Tandem on May 1, 2017, pursuant to which it agreed to forbear from exercising remedies, including waiving default interest, with respect to the above-described Loan Events of Default under the Tandem Mezzanine Loan until June 30, 2017, which was subsequently extended to July 31, 2017 with certain modifications.

On July 31, 2017, subsequent to its quarterly review process and the aforementioned impairment, the Company entered into a binding agreement (“Agreement”) with the borrowers to repay the Tandem Mezzanine Loan at a discounted value of \$197 million (the “Repayment Value”). Upon execution of the Agreement, the borrowers posted a

\$2 million non-refundable deposit and secured the right to repay the Tandem Mezzanine Loan by October 25, 2017 (at the Repayment Value). A second non-refundable deposit of \$2 million is required to be posted by August 31, 2017. The borrowers also retain the option to extend the term of the Agreement to December 31, 2017 upon satisfaction of one of the following requirements: (i) posting of an additional \$4 million non-refundable deposit, (ii) providing evidence of a commitment letter(s) for financing to satisfy the full Repayment Value, which is subject to the Company's approval and may be granted or withheld in the Company's sole discretion, or (iii) paying down the principal balance of the Tandem Mezzanine Loan by at least \$50 million. The borrowers are obligated to continue making interest payments based on the \$257 million par value of the Tandem Mezzanine Loan through the repayment date, adjusted for any principal payments received from Tandem. As part of the Agreement, the Company agreed to forbear from exercising remedies, including waiving default interest, with respect to the above-described Loan Events of Default under the Tandem Mezzanine Loan, through December 31, 2017.

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During the third quarter of 2017, the Company expects to record an additional \$3 million impairment charge to write down the carrying value of the Tandem Mezzanine Loan to the Repayment Value and assign the Tandem Mezzanine Loan an internal rating of Workout. The repayment of the Tandem Mezzanine Loan is subject to customary closing conditions and may not occur within the anticipated timeframe or at all.

NOTE 7. Investments in and Advances to Unconsolidated Joint Ventures

The Company owns interests in the following entities that are accounted for under the equity method at June 30, 2017 (dollars in thousands):

| Entity <sup>(1)</sup>                          | Segment                       | Ownership% | Carrying Amount |                   |
|--|-------------------------------|------------|-----------------|-------------------|
|  |                               |            | June 30, 2017   | December 31, 2016 |
| CCRC JV <sup>(2)</sup>                         | SHOP                          | 49         | \$433,507       | \$439,449         |
| RIDEA II                                       | SHOP                          | 40         | 258,505         | —                 |
| HCP Life Science <sup>(3)</sup>                | Life science                  | 50 - 63    | 64,795          | 67,879            |
| MBK JV   | SHOP                          | 50         | 38,806          | 38,909            |
| Medical Office JVs <sup>(4)</sup>              | Medical office                | 20 - 67    | 13,569          | 13,438            |
| Development JVs <sup>(5)</sup>                 | SHOP                          | 50 - 90    | 18,616          | 10,459            |
| K&Y JVs  | Other non-reportable segments | 80         | 1,420           | 1,342             |
| Advances to unconsolidated joint ventures, net |                               |            | 13              | 15                |
|  |                               |            | \$829,231       | \$571,491         |

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

(2) Includes two unconsolidated JVs in a RIDEA structure (CCRC PropCo and CCRC OpCo).

(3) Includes the following unconsolidated partnerships (and the Company's ownership percentage): (i) Torrey Pines Science Center, LP (50%); (ii) Britannia Biotech Gateway, LP (55%); and (iii) LASDK, LP (63%).

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

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

See Note 4 for further information on the deconsolidation of RIDEA II.

NOTE 8. Intangibles

The following tables summarize the Company's intangible lease assets and liabilities (in thousands):

|   | June 30, 2017 | December 31, 2016 |
|---|---------------|-------------------|
| Intangible lease assets                   |               |                   |
| Gross intangible lease assets             | \$818,577     | \$911,697         |
| Accumulated depreciation and amortization | (404,173 )    | (431,892 )        |
| Net intangible lease assets               | \$414,404     | \$479,805         |
| Intangible lease liabilities              |               |                   |
| Gross intangible lease liabilities        | \$143,209     | \$163,924         |
| Accumulated depreciation and amortization | (91,746 )     | (105,779 )        |
| Net intangible lease liabilities          | \$51,463      | \$58,145          |



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## NOTE 9. Other Assets

The following table summarizes the Company's other assets (in thousands):

|   | June 30,<br>2017 | December 31,<br>2016 |
|---|------------------|----------------------|
| Straight-line rent receivables, net of allowance of \$24,737 and \$25,059, respectively | \$320,485        | \$ 311,776           |
| Marketable debt securities, net   | 18,448           | 68,630               |
| Leasing costs and inducements, net  | 91,818           | 156,820              |
| Goodwill  | 47,019           | 42,386               |
| Other   | 133,920          | 132,012              |
| Total other assets, net   | \$611,690        | \$ 711,624           |

## Four Seasons Health Care Senior Notes

In March 2017, pursuant to a shift in the Company's investment strategy, the Company sold its £138.5 million par value Four Seasons senior notes (the "Four Seasons Notes") for £83 million (\$101 million). The disposition of the Four Seasons Notes generated a £42 million (\$51 million) gain on sale, recognized in other income, net, as the sales price was above the previously-impaired carrying value of £41 million (\$50 million).

## NOTE 10. Debt

## Bank Line of Credit and Term Loans

The Company's \$2.0 billion unsecured revolving line of credit facility (the "Facility") matures on March 31, 2018 and contains a committed one-year extension option, at a cost of 30 basis points. Borrowings under the Facility accrue interest at LIBOR plus a margin that depends on the Company's credit ratings. The Company pays a facility fee on the entire revolving commitment that depends on its credit ratings. Based on the Company's credit ratings at June 30, 2017, the margin on the Facility was 1.05% and the facility fee was 0.20%. The Facility also includes a feature that allows the Company to increase the borrowing capacity by an aggregate amount of up to \$500 million, subject to securing additional commitments from existing lenders or new lending institutions. During the six months ended June 30, 2017, the Company had net repayments of \$781 million primarily using proceeds from the RIDEA II joint venture disposition, the sale of its Four Seasons Notes and the repayment of its HC-One Facility. At June 30, 2017, the Company had £105 million (\$136 million) outstanding under the Facility with a weighted average effective interest rate of 1.63%.

On July 30, 2012, the Company entered into a credit agreement with a syndicate of banks for a £137 million unsecured term loan (the "2012 Term Loan"). In March 2017, the Company repaid the 2012 Term Loan.

On June 30, 2017, the Company repaid £51 million of its four-year unsecured term loan entered into in January 2015 (the "2015 Term Loan"). Concurrently, the Company terminated its three-year interest rate swap which fixed the interest of the 2015 Term Loan. Effective June 30, 2017, the 2015 Term Loan accrues interest at a rate of GBP LIBOR plus 1.15%, subject to adjustments based on the Company's credit ratings. At June 30, 2017 the Company had £169 million (\$219 million) outstanding on the 2015 Term Loan.

The Facility and 2015 Term Loan contain certain financial restrictions and other customary requirements, including cross-default provisions to other indebtedness. Among other things, these covenants, using terms defined in the agreements: (i) limit the ratio of Consolidated Total Indebtedness to Consolidated Total Asset Value to 60%; (ii) limit the ratio of Secured Debt to Consolidated Total Asset Value to 30%; (iii) limit the ratio of Unsecured Debt to Consolidated Unencumbered Asset Value to 60%; and (iv) require a minimum Fixed Charge Coverage ratio of 1.5 times. The Facility and Term Loan also require a Minimum Consolidated Tangible Net Worth of \$6.5 billion at June 30, 2017. At June 30, 2017, the Company was in compliance with each of these restrictions and requirements of the Facility and Term Loan.

## Senior Unsecured Notes

At June 30, 2017, the Company had senior unsecured notes outstanding with an aggregate principal balance of \$7.0 billion. The senior unsecured notes contain certain covenants including limitations on debt, maintenance of

unencumbered assets, cross-acceleration provisions and other customary terms. The Company believes it was in compliance with these covenants at June 30, 2017.

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The following table summarizes the Company's senior unsecured notes payoffs for the year ended December 31, 2016 (dollars in thousands):

| Date               | Amount    | Coupon Rate |
|--------------------|-----------|-------------|
| February 1, 2016   | \$500,000 | 3.750%      |
| September 15, 2016 | \$400,000 | 6.300%      |
| November 30, 2016  | \$500,000 | 6.000%      |
| November 30, 2016  | \$600,000 | 6.700%      |

The following table summarizes the Company's senior unsecured note payoffs for the six months ended June 30, 2017 (dollars in thousands):

| Date        | Amount    | Coupon Rate |
|-------------|-----------|-------------|
| May 1, 2017 | \$250,000 | 5.625%      |

There were no senior unsecured notes issuances for the six months ended June 30, 2017 and the year ended December 31, 2016.

**Mortgage Debt**

At June 30, 2017, the Company had \$140 million in aggregate principal of mortgage debt outstanding, which is secured by 16 healthcare facilities (including redevelopment properties) with a carrying value of \$306 million. In March 2017, the Company paid off \$472 million of mortgage debt.

**Debt Maturities**

The following table summarizes the Company's stated debt maturities and scheduled principal repayments at June 30, 2017 (in thousands):

| Year                                     | Bank Line of Credit <sup>(1)</sup> | 2015 Term Loan <sup>(2)</sup> | Senior Unsecured Notes <sup>(3)</sup> | Mortgage Debt <sup>(4)</sup> | Total <sup>(5)</sup> |
|--|------------------------------------|-------------------------------|---------------------------------------|------------------------------|----------------------|
| 2017 (six months)                        | \$—                                | \$ —                          | \$—                                   | \$1,685                      | \$1,685              |
| 2018                                     | 136,311                            | —                             | —                                     | 3,512                        | 139,823              |
| 2019                                     | —                                  | 219,396                       | 450,000                               | 3,700                        | 673,096              |
| 2020                                     | —                                  | —                             | 800,000                               | 3,758                        | 803,758              |
| 2021                                     | —                                  | —                             | 1,200,000                             | 11,117                       | 1,211,117            |
| Thereafter                               | —                                  | —                             | 4,500,000                             | 116,481                      | 4,616,481            |
|  | 136,311                            | 219,396                       | 6,950,000                             | 140,253                      | 7,445,960            |
| (Discounts), premium and debt costs, net | —                                  | (564 )                        | (60,955 )                             | 6,084                        | (55,435 )            |
|  | \$136,311                          | \$ 218,832                    | \$6,889,045                           | \$146,337                    | \$7,390,525          |

(1) Represents £105 million translated into U.S. dollars ("USD").

(2) Represents £169 million translated into USD.

(3) Effective interest rates on the notes ranged from 2.79% to 6.88% with a weighted average effective interest rate of 4.29% and a weighted average maturity of six years.

(4) Interest rates on the mortgage debt ranged from 2.99% to 5.91% with a weighted average effective interest rate of 4.23% and a weighted average maturity of twenty years.

(5) Excludes \$95 million of other debt that have no scheduled maturities.

**Subsequent Event**

In July 2017, the Company repurchased \$500 million of its 5.375% senior notes due 2021 and expects to record approximately \$54 million of loss on debt extinguishment in the third quarter of 2017.

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### NOTE 11. Commitments and Contingencies

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#### Commitments

From October 31, 2016 through June 2017, HCP was the sole lender to QCP of an unsecured revolving credit facility (the “Unsecured Revolving Credit Facility”) which had a total commitment of \$100 million at inception. The Unsecured Revolving Credit Facility was available to be drawn upon by QCP through October 31, 2017 with any drawn amounts due on October 31, 2018. Commitments under the Unsecured Revolving Credit Facility automatically and permanently decreased each calendar month by an amount equal to 50% of QCP's and its restricted subsidiaries' retained cash flow for the prior calendar month. All borrowings under the Unsecured Revolving Credit Facility were subject to the satisfaction of certain conditions, including (i) QCP's senior secured revolving credit facility being unavailable, (ii) the failure of HCRMC to pay rent and (iii) other customary conditions, including the absence of a default and the accuracy of representations and warranties. QCP could only draw on the Unsecured Revolving Credit Facility prior to the one-year anniversary of the completion of the Spin-Off. Borrowings under the Unsecured Revolving Credit Facility would have borne interest at a rate equal to LIBOR, subject to a 1.00% floor, plus an applicable margin of 6.25%. In addition to paying interest on outstanding principal under the Unsecured Revolving Credit Facility, QCP was required to pay a facility fee equal to 0.50% per annum of the unused capacity under the Unsecured Revolving Credit Facility to HCP, payable quarterly. Through June 30, 2017, no amounts were drawn on the Unsecured Revolving Credit Facility and the total commitment has been reduced to zero at June 30, 2017.

#### Legal Proceedings

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

#### Class Action

On May 9, 2016, a purported stockholder of the Company filed a putative class action complaint, *Boynton Beach Firefighters' Pension Fund v. HCP, Inc., et al.*, Case No. 3:16-cv-01106-JJH, in the U.S. District Court for the Northern District of Ohio against the Company, certain of its officers, HCRMC, and certain of its officers, asserting violations of the federal securities laws. The suit asserts claims under sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and alleges that the Company made certain false or misleading statements relating to the value of and risks concerning its investment in HCRMC by allegedly failing to disclose that HCRMC had engaged in billing fraud, as alleged by the U.S. Department of Justice in a pending suit against HCRMC arising from the False Claims Act. The plaintiff in the suit demands compensatory damages (in an unspecified amount), costs and expenses (including attorneys' fees and expert fees), and equitable, injunctive, or other relief as the Court deems just and proper. As the Boynton Beach action is in its early stages and a lead plaintiff has not yet been named, the defendants have not yet responded to the complaint. The Company believes the suit to be without merit and intends to vigorously defend against it.

#### Derivative Actions

On June 16, 2016 and July 5, 2016, purported stockholders of the Company filed two derivative actions, respectively *Subodh v. HCR ManorCare Inc., et al.*, Case No. 30-2016-00858497-CU-PT-CXC and *Stearns v. HCR ManorCare, Inc., et al.*, Case No. 30-2016-00861646-CU-MC-CJC, in the Superior Court of California, County of Orange, against certain of the Company's current and former directors and officers and HCRMC. The Company is named as a nominal defendant. As both derivative actions contained substantially the same allegations, they have been consolidated into a single action. The consolidated action alleges that the defendants engaged in various acts of wrongdoing, including, among other things, breaching fiduciary duties by publicly making false or misleading statements of fact regarding HCRMC's finances and prospects, and failing to maintain adequate internal controls. As the Subodh/Stearns action is in the early stages, defendants have not yet responded to the complaint. On April 18, 2017, the Court approved the parties' stipulation staying the action pending further developments, including in the related securities class action litigation. The Court also adjourned the status conference scheduled for April 27, 2017 to January 10, 2018.



On April 10, 2017, a purported stockholder of the Company filed a derivative action, Weldon v. Martin et al., Case No. 3:17-cv-755, in federal court in the Northern District of Ohio, Western Division, against certain of the Company's current and former directors and officers and HCRMC. The Company is named as a nominal defendant. The Weldon complaint asserts similar claims to those asserted in the California derivative actions. In addition, the complaint asserts a claim under Section 14(a) of the Securities Exchange Act of 1934, alleging that the Company made false statements in its 2016 proxy statement by not disclosing that the Company's performance issues in 2015 were the direct result of billing fraud at HCRMC. On April 18, 2017, the Court re-assigned and transferred this action to the judge presiding over the related federal securities class action. Defendants have not yet been served or responded to the complaint. On July 11, 2017, the court approved a stipulation by the parties to stay the case pending disposition of the motion to dismiss the class action.

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On July 21, 2017, a purported stockholder of the Company filed a derivative action, Kelley v. HCR Manorcare, Inc., et al., Case No. 8:17-cv-01259, in federal court in the Central District of California, against certain of the Company's current and former directors and officers and HCRMC. The Company is named as a nominal defendant. The Kelley complaint asserts similar claims to those asserted in the California and Ohio derivative actions and, like the Ohio action, asserts a claim under Section 14(a) of the Securities Exchange Act of 1934, alleging that the Company made false statements in its 2016 proxy statement by not disclosing that the Company's performance issues in 2015 were the direct result of billing fraud at HCRMC. Defendants have not yet been served or responded to the complaint. The Company is unable to estimate amount of loss or range of reasonable possible losses with respect to matters discussed above at June 30, 2017.

## NOTE 12. Equity

## Accumulated Other Comprehensive Loss

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

|  | June 30,<br>2017 | December 31,<br>2016 |
|--|------------------|----------------------|
| Cumulative foreign currency translation adjustment       | \$(14,205)       | \$(22,817)           |
| Unrealized losses on cash flow hedges, net               | (10,055)         | (3,642)              |
| Supplemental Executive Retirement plan minimum liability | (2,981)          | (3,129)              |
| Unrealized losses on available for sale securities       | (48)             | (54)                 |
| Total other comprehensive loss                           | \$(27,289)       | \$(29,642)           |

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NOTE 13. Segment Disclosures

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The Company evaluates its business and allocates resources based on its reportable business segments: (i) Senior housing triple-net, (ii) SHOP, (iii) life science and (iv) medical office. Under the medical office segment, the Company invests through the acquisition and development of medical office buildings (“MOBs”), which generally require a greater level of property management. Otherwise, the Company primarily invests, through the acquisition and development of real estate, in single tenant and operator properties. The Company has non-reportable segments that are comprised primarily of the Company’s debt investments, hospital properties and U.K. care homes. The accounting policies of the segments are the same as those in Note 2 to the Consolidated Financial Statements in the Company’s 2016 Annual Report on Form 10-K filed with the SEC, as updated by Note 2 herein. During the year ended December 31, 2016, 17 senior housing triple-net facilities were transitioned to a RIDEA structure (reported in the Company’s SHOP segment). During the six months ended June 30, 2017, one senior housing triple-net facility was transitioned to a RIDEA structure. The Company evaluates performance based upon: (i) property net operating income from continuing operations (“NOI”) and (ii) adjusted NOI of the combined consolidated and unconsolidated investments in each segment. NOI is defined as rental and related revenues, including tenant recoveries, resident fees and services, and income from DFLs, less property level operating expenses. Adjusted NOI is calculated as NOI after eliminating the effects of straight-line rents, DFL non-cash interest, amortization of market lease intangibles, non-refundable entrance fees, net of entrance fee amortization and lease termination fees and the impact of deferred community fee income and expense (“Adjustments to NOI”). The Adjustments to NOI and resulting Adjusted NOI for SHOP have been restated for prior periods presented to conform to the current period presentation for the adjustment to exclude the impact of deferred community fee income and expense, resulting in recognition as cash is received and expenses are paid.

Non-segment assets consist primarily of corporate assets, including cash and cash equivalents, restricted cash, accounts receivable, net, marketable equity securities and, if any, real estate held for sale. Interest expense, depreciation and amortization, and non-property specific revenues and expenses are not allocated to individual segments in evaluating the Company’s segment-level performance. See Note 17 for other information regarding concentrations of credit risk.

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

For the three months ended June 30, 2017:

|   | Senior<br>Housing<br>Triple-Net | SHOP       | Life<br>Science | Medical<br>Office | Other<br>Non-reportable | Corporate<br>Non-segment | Total       |
|---|---------------------------------|------------|-----------------|-------------------|-------------------------|--------------------------|-------------|
| Rental revenues <sup>(1)</sup>                    | \$ 78,079                       | \$ 125,416 | \$ 86,730       | \$ 119,164        | \$ 28,670               | \$ —                     | \$ 438,059  |
| HCP share of unconsolidated JV revenues           | —                               | 81,368     | 2,004           | 496               | 417                     | —                        | 84,285      |
| Operating expenses                                | (882 )                          | ( 85,866 ) | ( 18,744 )      | ( 46,581 )        | ( 1,090 )               | —                        | ( 153,163 ) |
| HCP share of unconsolidated JV operating expenses | —                               | ( 65,487 ) | ( 429 )         | ( 146 )           | ( 19 )                  | —                        | ( 66,081 )  |
| NOI   | 77,197                          | 55,431     | 69,561          | 72,933            | 27,978                  | —                        | 303,100     |
| Adjustments to NOI <sup>(2)</sup>                 | (406 )                          | 4,523      | (91 )           | (769 )            | (864 )                  | —                        | 2,393       |
| Adjusted NOI                                      | 76,791                          | 59,954     | 69,470          | 72,164            | 27,114                  | —                        | 305,493     |
| Addback adjustments                               | 406                             | ( 4,523 )  | 91              | 769               | 864                     | —                        | ( 2,393 )   |
| Interest income                                   | —                               | —          | —               | —                 | 20,869                  | —                        | 20,869      |
| Interest expense                                  | (631 )                          | ( 1,166 )  | ( 96 )          | ( 127 )           | ( 1,181 )               | ( 74,587 )               | ( 77,788 )  |
| Depreciation and amortization                     | (25,519 )                       | ( 24,415 ) | ( 31,004 )      | ( 42,488 )        | ( 7,325 )               | —                        | ( 130,751 ) |
| General and administrative                        | —                               | —          | —               | —                 | —                       | ( 21,286 )               | ( 21,286 )  |
| Acquisition and pursuit costs                     | —                               | —          | —               | —                 | —                       | ( 867 )                  | ( 867 )     |
| Impairment  | —                               | —          | —               | —                 | ( 56,682 )              | —                        | ( 56,682 )  |
| Gain (loss) on sales of real estate, net          | (230 )                          | ( 232 )    | 1,280           | ( 406 )           | —                       | —                        | 412         |
| Other income, net                                 | —                               | —          | —               | —                 | —                       | 71                       | 71          |
| Income tax benefit                                | —                               | —          | —               | —                 | —                       | 2,987                    | 2,987       |
| Less: HCP share of unconsolidated JV NOI          | —                               | ( 15,881 ) | ( 1,575 )       | ( 350 )           | ( 398 )                 | —                        | ( 18,204 )  |
| Equity income (loss) from unconsolidated JVs      | —                               | ( 1,065 )  | 763             | 303               | 239                     | —                        | 240         |
| Net income (loss)                                 | \$ 50,817                       | \$ 12,672  | \$ 38,929       | \$ 29,865         | \$ ( 16,500 )           | \$ ( 93,682 )            | \$ 22,101   |

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For the three months ended June 30, 2016:

|  | Senior<br>Housing<br>Triple-Net | SHOP       | Life<br>Science | Medical<br>Office | Other<br>Non-reportable | Corporate<br>Non-segment | Total      |
|--|---------------------------------|------------|-----------------|-------------------|-------------------------|--------------------------|------------|
| Rental revenues <sup>(1)</sup>                       | \$108,841                       | \$164,202  | \$90,201        | \$110,205         | \$32,099                | \$—                      | \$505,548  |
| HCP share of unconsolidated<br>JV revenues           | —                               | 52,855     | 1,898           | 524               | 407                     | —                        | 55,684     |
| Operating expenses                                   | (1,642 )                        | (115,443 ) | (17,961 )       | (43,028 )         | (1,006 )                | —                        | (179,080 ) |
| HCP share of unconsolidated<br>JV operating expenses | —                               | (42,473 )  | (400 )          | (155 )            | (7 )                    | —                        | (43,035 )  |
| NOI  | 107,199                         | 59,141     | 73,738          | 67,546            | 31,493                  | —                        | 339,117    |
| Adjustments to NOI <sup>(2)</sup>                    | (2,022 )                        | 4,248      | (544 )          | (753 )            | (214 )                  | —                        | 715        |
| Adjusted NOI   | 105,177                         | 63,389     | 73,194          | 66,793            | 31,279                  | —                        | 339,832    |
| Addback adjustments                                  | 2,022                           | (4,248 )   | 544             | 753               | 214                     | —                        | (715 )     |
| Interest income                                      | —                               | —          | —               | —                 | 32,787                  | —                        | 32,787     |
| Interest expense                                     | (4,049 )                        | (7,837 )   | (632 )          | (1,625 )          | (2,476 )                | (104,714 )               | (121,333 ) |
| Depreciation and amortization                        | (34,202 )                       | (24,988 )  | (32,077 )       | (40,604 )         | (8,048 )                | —                        | (139,919 ) |
| General and administrative                           | —                               | —          | —               | —                 | —                       | (22,779 )                | (22,779 )  |
| Acquisition and pursuit costs                        | —                               | —          | —               | —                 | —                       | (823 )                   | (823 )     |
| Gain on sales of real estate, net                    | —                               | —          | 29,455          | 8,311             | 81,848                  | —                        | 119,614    |
| Other income, net                                    | —                               | —          | —               | —                 | —                       | 2,340                    | 2,340      |
| Income tax benefit                                   | —                               | —          | —               | —                 | —                       | 2,179                    | 2,179      |
| Less: HCP share of<br>unconsolidated JV NOI          | —                               | (10,382 )  | (1,498 )        | (369 )            | (400 )                  | —                        | (12,649 )  |
| Equity income (loss) from<br>unconsolidated JVs      | —                               | (2,482 )   | 776             | 421               | 218                     | —                        | (1,067 )   |
| Discontinued operations                              | —                               | —          | —               | —                 | —                       | 107,375                  | 107,375    |
| Net income (loss)                                    | \$68,948                        | \$13,452   | \$69,762        | \$33,680          | \$135,422               | \$ (16,422 )             | \$304,842  |

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For the six months ended June 30, 2017:

|  | Senior<br>Housing<br>Triple-Net | SHOP       | Life<br>Science | Medical<br>Office | Other<br>Non-reportable | Corporate<br>Non-segment | Total      |
|--|---------------------------------|------------|-----------------|-------------------|-------------------------|--------------------------|------------|
| Rental revenues <sup>(1)</sup>                       | \$178,112                       | \$265,644  | \$172,050       | \$237,535         | \$ 58,555               | \$—                      | \$911,896  |
| HCP share of unconsolidated<br>JV revenues           | —                               | 157,731    | 3,944           | 985               | 835                     | —                        | 163,495    |
| Operating expenses                                   | (1,993 )                        | (180,405 ) | (36,064 )       | (91,444 )         | (2,338 )                | —                        | (312,244 ) |
| HCP share of unconsolidated<br>JV operating expenses | —                               | (125,014 ) | (800 )          | (288 )            | (38 )                   | —                        | (126,140 ) |
| NOI  | 176,119                         | 117,956    | 139,130         | 146,788           | 57,014                  | —                        | 637,007    |
| Adjustments to NOI <sup>(2)</sup>                    | (2,245 )                        | 7,679      | (345 )          | (1,739 )          | (1,879 )                | —                        | 1,471      |
| Adjusted NOI   | 173,874                         | 125,635    | 138,785         | 145,049           | 55,135                  | —                        | 638,478    |
| Addback adjustments                                  | 2,245                           | (7,679 )   | 345             | 1,739             | 1,879                   | —                        | (1,471 )   |
| Interest income                                      | —                               | —          | —               | —                 | 39,200                  | —                        | 39,200     |
| Interest expense                                     | (1,258 )                        | (6,017 )   | (200 )          | (256 )            | (2,923 )                | (153,852 )               | (164,506 ) |
| Depreciation and amortization                        | (51,930 )                       | (50,773 )  | (64,795 )       | (85,217 )         | (14,590 )               | —                        | (267,305 ) |
| General and administrative                           | —                               | —          | —               | —                 | —                       | (43,764 )                | (43,764 )  |
| Acquisition and pursuit costs                        | —                               | —          | —               | —                 | —                       | (1,924 )                 | (1,924 )   |
| Impairment   | —                               | —          | —               | —                 | (56,682 )               | —                        | (56,682 )  |
| Gain (loss) on sales of real<br>estate, net          | 268,234                         | 134        | 45,913          | (406 )            | 3,795                   | —                        | 317,670    |
| Other income, net                                    | —                               | —          | —               | —                 | —                       | 51,279                   | 51,279     |
| Income tax benefit                                   | —                               | —          | —               | —                 | —                       | 9,149                    | 9,149      |
| Less: HCP share of<br>unconsolidated JV NOI          | —                               | (32,717 )  | (3,144 )        | (697 )            | (797 )                  | —                        | (37,355 )  |
| Equity income from<br>unconsolidated JVs             | —                               | 927        | 1,533           | 572               | 477                     | —                        | 3,509      |
| Net income (loss)                                    | \$391,165                       | \$29,510   | \$118,437       | \$60,784          | \$ 25,494               | \$ (139,112 )            | \$486,278  |

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For the six months ended June 30, 2016:

|   | Senior<br>Housing<br>Triple-Net | SHOP      | Life<br>Science | Medical<br>Office | Other<br>Non-reportable | Corporate<br>Non-segment | Total       |
|---|---------------------------------|-----------|-----------------|-------------------|-------------------------|--------------------------|-------------|
| Rental revenues <sup>(1)</sup>                          | \$215,731                       | \$329,964 | \$179,149       | \$218,228         | \$64,904                | \$—                      | \$1,007,976 |
| HCP share of<br>unconsolidated JV revenues              | —                               | 103,284   | 3,708           | 1,003             | 814                     | —                        | 108,809     |
| Operating expenses                                      | (3,716)                         | (229,446) | (34,704)        | (84,977)          | (2,194)                 | —                        | (355,037)   |
| HCP share of<br>unconsolidated JV operating<br>expenses | —                               | (83,668)  | (774)           | (304)             | (10)                    | —                        | (84,756)    |
| NOI   | 212,015                         | 120,134   | 147,379         | 133,950           | 63,514                  | —                        | 676,992     |
| Adjustments to NOI <sup>(2)</sup>                       | (7,466)                         | 8,642     | (1,217)         | (1,548)           | (785)                   | —                        | (2,374)     |
| Adjusted NOI  | 204,549                         | 128,776   | 146,162         | 132,402           | 62,729                  | —                        | 674,618     |
| Addback adjustments                                     | 7,466                           | (8,642)   | 1,217           | 1,548             | 785                     | —                        | 2,374       |
| Interest income   | —                               | —         | —               | —                 | 50,816                  | —                        | 50,816      |
| Interest expense  | (8,215)                         | (15,690)  | (1,270)         | (3,291)           | (4,805)                 | (210,124)                | (243,395)   |
| Depreciation and<br>amortization                        | (67,707)                        | (51,286)  | (65,674)        | (79,322)          | (15,785)                | —                        | (279,774)   |
| General and administrative                              | —                               | —         | —               | —                 | —                       | (48,230)                 | (48,230)    |
| Acquisition and pursuit<br>costs                        | —                               | —         | —               | —                 | —                       | (3,298)                  | (3,298)     |
| Gain on sales of real estate,<br>net                    | —                               | —         | 29,455          | 8,311             | 81,848                  | —                        | 119,614     |
| Other income, net                                       | —                               | —         | —               | —                 | —                       | 3,632                    | 3,632       |
| Income tax expense                                      | —                               | —         | —               | —                 | —                       | (1,525)                  | (1,525)     |
| Less: HCP share of<br>unconsolidated JV NOI             | —                               | (19,616)  | (2,934)         | (699)             | (804)                   | —                        | (24,053)    |
| Equity income (loss) from<br>unconsolidated JVs         | —                               | (4,960)   | 1,485           | 1,079             | 421                     | —                        | (1,975)     |
| Discontinued operations                                 | —                               | —         | —               | —                 | —                       | 175,783                  | 175,783     |
| Net income (loss)                                       | \$136,093                       | \$28,582  | \$108,441       | \$60,028          | \$175,205               | \$(83,762)               | \$424,587   |

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

Represents straight-line rents, DFL non-cash interest, amortization of market lease intangibles, net, the deferral of (2) community fees, net of amortization, lease termination fees and non-refundable entrance fees as the fees are collected by the Company's CCRC JV, net of CCRC JV entrance fee amortization.

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

| Segment                       | Three Months<br>Ended June 30, |           | Six Months Ended<br>June 30, |             |
|-------------------------------|--------------------------------|-----------|------------------------------|-------------|
|                               | 2017                           | 2016      | 2017                         | 2016        |
| Senior housing triple-net     | \$78,079                       | \$108,841 | \$178,112                    | \$215,731   |
| SHOP                          | 125,416                        | 164,202   | 265,644                      | 329,964     |
| Life science                  | 86,730                         | 90,201    | 172,050                      | 179,149     |
| Medical office                | 119,164                        | 110,205   | 237,535                      | 218,228     |
| Other non-reportable segments | 49,539                         | 64,886    | 97,755                       | 115,720     |
| Total revenues                | \$458,928                      | \$538,335 | \$951,096                    | \$1,058,792 |

See Notes 3 and 4 for significant transactions impacting the Company's segment assets during the periods presented.





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## NOTE 14. Earnings Per Common Share

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

Options to purchase 1 million shares of common stock were excluded from the computation of diluted earnings per share for both the three and six months ended June 30, 2017 and 2016 because they are anti-dilutive.

Additionally, 7 million and 2 million shares, issuable upon conversion of 4 million and 2 million DownREIT units during the three months ended June 30, 2017 and June 30, 2016, were not included because they are anti-dilutive. For the six months ended June 30, 2017 and June 30, 2016, 2 million and 6 million shares, issuable upon conversion of 1 million and 4 million DownREIT units, were not included because they are anti-dilutive.

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

|   | Three Months Ended<br>June 30,<br>2017 |           | Six Months Ended<br>June 30,<br>2016 |           |
|---|--|-----------|--------------------------------------|-----------|
| Numerator   |  |           |                                      |           |
| Net income from continuing operations                         | \$22,101                               | \$197,467 | \$486,278                            | \$248,804 |
| Noncontrolling interests' share in earnings                   | (2,718 )                               | (3,125 )  | (5,750 )                             | (6,751 )  |
| Net income attributable to HCP, Inc.                          | 19,383                                 | 194,342   | 480,528                              | 242,053   |
| Less: Participating securities' share in earnings             | (100 )                                 | (342 )    | (674 )                               | (651 )    |
| Income from continuing operations applicable to common shares | 19,283                                 | 194,000   | 479,854                              | 241,402   |
| Discontinued operations                                       | —                                      | 107,375   | —                                    | 175,783   |
| Net income applicable to common shares                        | \$19,283                               | \$301,375 | \$479,854                            | \$417,185 |
| Numerator - Dilutive  |  |           |                                      |           |
| Net income applicable to common shares                        | \$19,283                               | \$301,375 | \$479,854                            | \$417,185 |
| Add: distributions on dilutive convertible units and other    | —                                      | 2,388     | 3,655                                | —         |
| Dilutive net income available to common shares                | \$19,283                               | \$303,763 | \$483,509                            | \$417,185 |
| Denominator   |  |           |                                      |           |
| Basic weighted average shares outstanding                     | 468,646                                | 467,084   | 468,474                              | 466,579   |
| Dilutive potential common shares - equity awards              | 193                                    | 208       | 195                                  | 198       |
| Dilutive potential common shares - DownREIT conversions       | —                                      | 4,133     | 4,697                                | —         |
| Diluted weighted average common shares                        | 468,839                                | 471,425   | 473,366                              | 466,777   |
| Basic earnings per common share                               |  |           |                                      |           |
| Continuing operations   | \$0.04                                 | \$0.42    | \$1.02                               | \$0.52    |
| Discontinued operations                                       | —                                      | 0.23      | —                                    | 0.37      |
| Net income applicable to common shares                        | \$0.04                                 | \$0.65    | \$1.02                               | \$0.89    |
| Diluted earnings per common share                             |  |           |                                      |           |
| Continuing operations   | \$0.04                                 | \$0.42    | \$1.02                               | \$0.52    |
| Discontinued operations                                       | —                                      | 0.22      | —                                    | 0.37      |
| Net income applicable to common shares                        | \$0.04                                 | \$0.64    | \$1.02                               | \$0.89    |

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## NOTE 15. Supplemental Cash Flow Information

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

|   | Six Months Ended<br>June 30, |            |
|---|------------------------------|------------|
|   | 2017                         | 2016       |
| Supplemental cash flow information:   |                              |            |
| Interest paid, net of capitalized interest  | \$ 163,455                   | \$ 241,585 |
| Income taxes paid   | 10,335                       | 4,433      |
| Capitalized interest  | 7,628                        | 5,734      |
| Supplemental schedule of non-cash investing and financing activities:   |                              |            |
| Accrued construction costs  | 68,618                       | 57,143     |
| Non-cash acquisitions and dispositions settled with receivables and restricted cash held in connection with Section 1031 transactions | 39,991                       | 129,846    |
| Vesting of restricted stock units and conversion of non-managing member units into common stock                                       | 2,451                        | 5,310      |
| Other liabilities assumed with real estate acquisitions   | 160                          | 1,200      |
| Unrealized losses on available-for-sale securities and derivatives designated as cash flow hedges, net                                | (48)                         | ) 343      |

## NOTE 16. Variable Interest Entities

## Unconsolidated Variable Interest Entities

At June 30, 2017, the Company had investments in: (i) five unconsolidated VIE JVs, (ii) 48 properties leased to VIE tenants, (iii) marketable debt securities of one VIE and (iv) two loans to VIE borrowers. The Company has determined that it is not the primary beneficiary of and therefore does not consolidate these VIEs because it does not have the ability to control the activities that most significantly impact their economic performance. Except for the Company's equity interest in the unconsolidated JVs (CCRC OpCo, RIDEA II PropCo, Vintage Park Development JV, Waldwick JV and the LLC investment discussed below), it has no formal involvement in these VIEs beyond its investments. The Company holds a 49% ownership interest in CCRC OpCo, a joint venture entity formed in August 2014 that operates senior housing properties in a RIDEA structure and has been identified as a VIE (see Note 7). The equity members of CCRC OpCo "lack power" because they share certain operating rights with Brookdale, as manager of the CCRCs. The assets of CCRC OpCo primarily consist of the CCRCs that it owns and leases, resident fees receivable, notes receivable, and cash and cash equivalents; its obligations primarily consist of operating lease obligations to CCRC PropCo, debt service payments and capital expenditures for the properties, and accounts payable and expense accruals associated with the cost of its CCRCs' operations. Assets generated by the CCRC operations (primarily rents from CCRC residents) of CCRC OpCo may only be used to settle its contractual obligations (primarily from debt service payments, capital expenditures, and rental costs and operating expenses incurred to manage such facilities). In January 2017, as a result of the partial sale of its interest in RIDEA II, the Company concluded that it should deconsolidate RIDEA II as it is no longer the primary beneficiary of the joint venture. The HCP/CPA JV is the primary beneficiary of both RIDEA II PropCo and RIDEA II OpCo as it controls the significant activities of RIDEA II PropCo and, of the group that controls the significant activities of RIDEA II OpCo, is most closely associated to the entity. Furthermore, control over the HCP/CPA JV is shared between HCP and CPA, and as such, the Company does not consolidate the HCP/CPA JV. Subsequent to the partial sale of its interest in RIDEA II, the Company continues to hold a direct investment in RIDEA II PropCo, which has been identified as a VIE as Brookdale, the non-managing member, does not have any substantive participating rights or kick-out rights over the managing member, HCP/CPA PropCo (see Notes 4 and 7). The assets of RIDEA II PropCo primarily consist of leased properties (net real estate), rents receivable, and cash and cash equivalents; its obligations primarily consist of a combination of third-party and

HCP debt (see Note 4). Assets generated by RIDEA II PropCo (primarily from RIDEA II OpCo lease payments) may only be used to settle its contractual obligations (primarily debt service payments on the third-party and HCP debt). The Company holds an 85% ownership interest in two development joint ventures (Vintage Park Development JV and Waldwick JV) (see Note 7), which have been identified as VIEs as power is shared with a member that does not have a substantive equity investment at risk. The assets of each joint venture primarily consist of an in-progress senior housing facility development project that it owns and cash and cash equivalents; its obligations primarily consist of accounts payable and expense accruals associated

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with the cost of its development obligations. Any assets generated by each joint venture may only be used to settle its respective contractual obligations (primarily development expenses and debt service payments).

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

The Company leases 48 properties to a total of seven tenants that have also been identified as VIEs ("VIE tenants"). These VIE tenants are "thinly capitalized" entities that rely on the operating cash flows generated from the senior housing facilities to pay operating expenses, including the rent obligations under their leases.

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

The Company provided a £105 million (\$131 million at closing) bridge loan to Maria Mallaband Care Group Ltd. ("MMCG") to fund the acquisition of a portfolio of care homes in the U.K. MMCG created a special purpose entity to acquire the portfolio and funded it entirely using the Company's bridge loan. As such, the special purpose entity has been identified as a VIE because it is "thinly capitalized." The Company retains a three-year call option to acquire all the shares of the special purpose entity, which it can only exercise upon the occurrence of certain events.

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

The classification of the related assets and liabilities and the maximum loss exposure as a result of the Company's involvement with these VIEs at June 30, 2017 was as follows (in thousands):

| VIE Type                                      | Asset/Liability Type                                      | Maximum Loss Exposure and Carrying Amount <sup>(1)</sup> |
|---|---|--|
| VIE tenants - DFLs <sup>(2)</sup>             | Net investment in DFLs                                    | \$ 599,561   |
| VIE tenants - operating leases <sup>(2)</sup> | Lease intangibles, net and straight-line rent receivables | 5,952  |
| CCRC OpCo                                     | Investments in unconsolidated joint ventures              | 218,832  |
| RIDEA II PropCo                               | Investments in unconsolidated joint ventures              | 254,137  |
| Development JVs                               | Investments in unconsolidated joint ventures              | 11,653   |
| Loan- Senior Secured                          | Loans Receivable, net                                     | 137,025  |
| Loan- Seller Financing                        | Loans Receivable, net                                     | 10,000   |
| CMBS and LLC investment                       | Marketable debt and cost method investment                | 33,511   |

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

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

At June 30, 2017, the Company had not provided, and is not required to provide, financial support through a liquidity arrangement or otherwise, to its unconsolidated VIEs, including circumstances in which it could be exposed to further losses (e.g., cash shortfalls).

See Notes 4, 6, and 7 for additional descriptions of the nature, purpose and operating activities of the Company's unconsolidated VIEs and interests therein.



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## Consolidated Variable Interest Entities

HCP, Inc.'s consolidated total assets and total liabilities at June 30, 2017 and December 31, 2016 include certain assets of VIEs that can only be used to settle the liabilities of the related VIE. The VIE creditors do not have recourse to HCP, Inc. Total assets at June 30, 2017 and December 31, 2016 include VIE assets as follows (in thousands):

|  | June 30,<br>2017 | December 31,<br>2016 |
|--|------------------|----------------------|
| Assets   |                  |                      |
| Building and Improvements                                    | \$2,796,279      | \$3,522,310          |
| Developments in Process                                      | 17,702           | 31,953               |
| Land   | 222,893          | 327,241              |
| Accumulated Depreciation                                     | (559,789)        | (676,276)            |
| Net Real Estate  | 2,477,085        | 3,205,228            |
| Investments in and advances to unconsolidated joint ventures | 2,573            | 3,641                |
| Accounts Receivable, Net                                     | 12,062           | 19,996               |
| Cash and Cash Equivalents                                    | 45,034           | 35,844               |
| Restricted Cash  | 41,843           | 22,624               |
| Intangible Assets, Net                                       | 133,210          | 169,027              |
| Other Assets, Net  | 53,400           | 69,562               |
| Total Assets   | \$2,765,207      | \$3,525,922          |
| Liabilities  |                  |                      |
| Mortgage Debt  | 45,156           | 520,870              |
| Intangible Liabilities, Net                                  | 8,475            | 8,994                |
| Accounts Payable and Accrued Expenses                        | 100,648          | 120,719              |
| Deferred Revenue   | 18,453           | 23,456               |
| Total Liabilities  | \$172,732        | \$674,039            |

RIDEA I. The Company holds a 90% ownership interest in JV entities formed in September 2011 that own and operate senior housing properties in a RIDEA structure ("RIDEA I"). The Company has historically classified RIDEA I OpCo as a VIE and, as a result of the adoption of ASU No. 2015-02, Amendments to the Consolidation Analysis ("ASU 2015-02"), also classifies RIDEA I PropCo as a VIE due to the non-managing member lacking substantive participation rights in the management of RIDEA I PropCo or kick-out rights over the managing member. The Company consolidates RIDEA I PropCo and RIDEA I OpCo as the primary beneficiary because it has the ability to control the activities that most significantly impact these VIEs' economic performance. The assets of RIDEA I PropCo primarily consist of leased properties (net real estate), rents receivable, and cash and cash equivalents; its obligations primarily consist of notes payable to a non-VIE consolidated subsidiary of the Company. The assets of RIDEA I OpCo primarily consist of leasehold interests in senior housing facilities (operating leases), resident fees receivable, and cash and cash equivalents; its obligations primarily consist of lease payments to RIDEA I PropCo and operating expenses of its senior housing facilities (accounts payable and accrued expenses). Assets generated by the senior housing operations (primarily from senior housing resident rents) of the RIDEA I structure may only be used to settle its contractual obligations (primarily from the rental costs, operating expenses incurred to manage such facilities and debt costs).

RIDEA III. The Company holds a 90% ownership interest in JV entities formed in June 2015 that own and operate senior housing properties in a RIDEA structure. The Company has historically classified RIDEA III OpCo as a VIE and, as a result of the adoption of ASU 2015-02, also classifies RIDEA III PropCo as a VIE due to the non-managing member lacking substantive participation rights in the management of RIDEA III PropCo or kick-out rights over the managing member. The Company consolidates RIDEA III PropCo and RIDEA III OpCo as the primary beneficiary because it has the ability to control the activities that most significantly impact these VIEs' economic performance. The assets of RIDEA III PropCo primarily consist of leased properties (net real estate), rents receivable, and cash and cash equivalents; its obligations primarily consist of a note payable to a non-VIE consolidated subsidiary of the Company. The assets of RIDEA III OpCo primarily consist of leasehold interests in senior housing facilities

(operating leases), resident fees receivable, and cash and cash equivalents; its obligations primarily consist of lease payments to RIDEA III PropCo and operating expenses of its senior housing facilities (accounts payable and accrued expenses). Assets generated by the senior housing operations (primarily from senior housing resident rents) of the RIDEA III structure may only be used to settle its contractual obligations (primarily from the rental costs, operating expenses incurred to manage such facilities and debt costs).

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**HCP Ventures V, LLC.** The Company holds a 51% ownership interest in and is the managing member of a JV entity formed in October 2015 that owns and leases MOB's ("HCP Ventures V"). Upon adoption of ASU 2015-02, the Company classified HCP Ventures V as a VIE due to the non-managing member lacking substantive participation rights in the management of HCP Ventures V or kick-out rights over the managing member. The Company consolidates HCP Ventures V as the primary beneficiary because it has the ability to control the activities that most significantly impact the VIE's economic performance. The assets of HCP Ventures V primarily consist of leased properties (net real estate), rents receivable, and cash and cash equivalents; its obligations primarily consist of capital expenditures for the properties. Assets generated by HCP Ventures V may only be used to settle its contractual obligations (primarily from capital expenditures).

**Vintage Park JV.** The Company holds a 90% ownership interest in a JV entity formed in January 2015 that owns an 85% interest in an unconsolidated development VIE ("Vintage Park JV"). Upon adoption of ASU 2015-02, the Company classified Vintage Park JV as a VIE due to the non-managing member lacking substantive participation rights in the management of the Vintage Park JV or kick-out rights over the managing member. The Company consolidates Vintage Park JV as the primary beneficiary because it has the ability to control the activities that most significantly impact the VIE's economic performance. The assets of Vintage Park JV primarily consist of an investment in the Vintage Park Development JV and cash and cash equivalents; its obligations primarily consist of funding the ongoing development of the Vintage Park Development JV. Assets generated by the Vintage Park JV may only be used to settle its contractual obligations (primarily from the funding of the Vintage Park Development JV).

**DownREITs.** The Company holds a controlling ownership interest in and is the managing member of five DownREITs. Upon adoption of ASU 2015-02, the Company classified the DownREITs as VIEs due to the non-managing members lacking substantive participation rights in the management of the DownREITs or kick-out rights over the managing member. The Company consolidates the DownREITs as the primary beneficiary because it has the ability to control the activities that most significantly impact these VIEs' economic performance. The assets of the DownREITs primarily consist of leased properties (net real estate), rents receivable, and cash and cash equivalents; their obligations primarily consist of debt service payments and capital expenditures for the properties. Assets generated by the DownREITs (primarily from resident rents) may only be used to settle their contractual obligations (primarily from debt service and capital expenditures).

**Other Consolidated Real Estate Partnerships.** The Company holds a controlling ownership interest in and is the general partner (or managing member) of multiple partnerships that own and lease real estate assets (the "Partnerships"). Upon adoption of ASU 2015-02, the Company classified the Partnerships as VIEs due to the limited partners (non-managing members) lacking substantive participation rights in the management of the Partnerships or kick-out rights over the general partner (managing member). The Company consolidates the Partnerships as the primary beneficiary because it has the ability to control the activities that most significantly impact these VIEs' economic performance. The assets of the Partnerships primarily consist of leased properties (net real estate), rents receivable, and cash and cash equivalents; their obligations primarily consist of debt service payments and capital expenditures for the properties. Assets generated by the Partnerships (primarily from resident rents) may only be used to settle their contractual obligations (primarily from debt service and capital expenditures).

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

### NOTE 17. Concentration of Credit Risk

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Concentrations of credit risk arise when one or more tenants, operators or obligors related to the Company's investments are engaged in similar business activities or activities in the same geographic region, or have similar



economic features that would cause their ability to meet contractual obligations, including those to the Company, to be similarly affected by changes in economic conditions. The Company regularly monitors various segments of its portfolio to assess potential concentrations of credit risks. The Company does not have significant foreign operations.

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The following tables provide information regarding the Company's concentrations with respect to certain tenants:

| Tenant                   | Percentage of Gross Assets |      |                           |      | Percentage of Revenues |      |                  |      |                                    |      |                  |      |
|--------------------------|----------------------------|------|---------------------------|------|------------------------|------|------------------|------|------------------------------------|------|------------------|------|
|                          | Total Company              |      | Senior Housing Triple-Net |      | Total Company Revenues |      |                  |      | Senior Housing Triple-Net Revenues |      |                  |      |
|                          |                            |      |                           |      | Three Months Ended     |      | Six Months Ended |      | Three Months Ended                 |      | Six Months Ended |      |
|                          | June 30, 2017              |      | December 31, 2016         |      | June 30, 2017          |      | June 30, 2016    |      | June 30, 2017                      |      | June 30, 2016    |      |
|                          | 2017                       | 2016 | 2017                      | 2016 | 2017                   | 2016 | 2017             | 2016 | 2017                               | 2016 | 2017             | 2016 |
| Brookdale <sup>(1)</sup> | 11%                        | 17%  | 42%                       | 69%  | 8%                     | 12%  | 10%              | 12%  | 47%                                | 58%  | 55%              | 58%  |

(1) Includes revenues from 64 senior housing triple-net facilities that were classified as held for sale at December 31, 2016 and sold in March 2017.

At June 30, 2017 and December 31, 2016, Brookdale managed or operated, in the Company's SHOP segment, approximately 13% and 18%, respectively, of the Company's real estate investments based on gross assets. Because an operator manages the Company's facilities in exchange for the receipt of a management fee, the Company is not directly exposed to the credit risk of its operators in the same manner or to the same extent as its triple-net tenants. At June 30, 2017, Brookdale provided comprehensive facility management and accounting services with respect to 59 of the Company's SHOP facilities and 65 SHOP facilities owned by its unconsolidated joint ventures, for which the Company or joint venture pay annual management fees pursuant to long-term management agreements. Most of the management agreements have terms ranging from 10 to 15 years, with three to four 5-year renewal periods. The base management fees are 4.5% to 5.0% of gross revenues (as defined) generated by the RIDEA facilities. In addition, there are incentive management fees payable to Brookdale if operating results of the RIDEA properties exceed pre-established EBITDAR (as defined) thresholds.

Brookdale is subject to the registration and reporting requirements of the SEC and is required to file with the SEC annual reports containing audited financial information and quarterly reports containing unaudited financial information. The information related to Brookdale contained or referred to in this report has been derived from SEC filings made by Brookdale or other publicly available information, or was provided to the Company by Brookdale, and the Company has not verified this information through an independent investigation or otherwise. The Company has no reason to believe that this information is inaccurate in any material respect, but the Company cannot assure the reader of its accuracy. The Company is providing this data for informational purposes only, and encourages the reader to obtain Brookdale's publicly available filings, which can be found on the SEC's website at [www.sec.gov](http://www.sec.gov).

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

#### NOTE 18. Fair Value Measurements

Financial assets and liabilities measured at fair value on a recurring basis at June 30, 2017 in the consolidated balance sheets are immaterial.

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

|   | June 30, 2017 <sup>(4)</sup> |            | December 31, 2016 <sup>(4)</sup> |            |
|---|------------------------------|------------|----------------------------------|------------|
|   | Carrying Value               | Fair Value | Carrying Value                   | Fair Value |
| Loans receivable, net <sup>(2)</sup>          | \$393,575                    | \$394,438  | \$807,954                        | \$807,505  |
| Marketable debt securities <sup>(2)</sup>     | 18,448                       | 18,448     | 68,630                           | 68,630     |
| Marketable equity securities <sup>(1)</sup>   | 82                           | 82         | 76                               | 76         |
| Warrants <sup>(3)</sup>                       | 61                           | 61         | 19                               | 19         |
| Bank line of credit <sup>(2)</sup>            | 136,311                      | 136,311    | 899,718                          | 899,718    |
| Term loans <sup>(2)</sup>                     | 218,832                      | 218,832    | 440,062                          | 440,062    |
| Senior unsecured notes <sup>(1)</sup>         | 6,889,045                    | 7,267,553  | 7,133,538                        | 7,386,149  |
| Mortgage debt <sup>(2)</sup>                  | 146,337                      | 133,494    | 623,792                          | 609,374    |
| Other debt <sup>(2)</sup>                     | 94,801                       | 94,801     | 92,385                           | 92,385     |
| Interest-rate swap liabilities <sup>(2)</sup> | 3,272                        | 3,272      | 4,857                            | 4,857      |
| Currency swap asset <sup>(2)</sup>            | —                            | —          | 2,920                            | 2,920      |
| Cross currency swap liability <sup>(2)</sup>  | 5,504                        | 5,504      | —                                | —          |

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

Level 2: Fair value based on (i) for marketable debt securities, quoted prices for similar or identical instruments in active or inactive markets, respectively, or (ii) or for loans receivable, net, mortgage debt, and swaps, calculated

(2) utilizing standardized pricing models in which significant inputs or value drivers are observable in active markets.

For bank line of credit, term loans and other debt, the carrying values are a reasonable estimate of fair value because the borrowings are primarily based on market interest rates and the Company's credit rating.

(3) Level 3: Fair value determined based on significant unobservable market inputs using standardized derivative pricing models.

(4) During the six months ended June 30, 2017 and year ended December 31, 2016, there were no material transfers of financial assets or liabilities within the fair value hierarchy.

#### NOTE 19. Derivative Financial Instruments

The following table summarizes the Company's outstanding interest-rate and cross currency swap contracts at June 30, 2017 (dollars and GBP in thousands):

| Date Entered              | Maturity Date | Hedge Designation | Notional  | Pay Rate | Receive Rate   | Fair Value <sup>(1)</sup> |
|---------------------------|---------------|-------------------|-----------|----------|----------------|---------------------------|
| Interest rate:            |               |                   |           |          |                |                           |
| July 2005 <sup>(2)</sup>  | July 2020     | Cash Flow         | \$ 44,100 | 3.82%    | BMA Swap Index | \$ (3,272 )               |
| Cross currency swap:      |               |                   |           |          |                |                           |
|                           |               |                   | £105,000  |          |                |                           |
| April 2017 <sup>(3)</sup> | February 2019 | Net Investment    | /         | 2.584%   | 3.75           | % \$ (5,504 )             |
|                           |               |                   | \$131,400 |          |                |                           |

(1) Derivative assets are recorded in other assets, net and derivative liabilities are recorded in accounts payable and accrued liabilities on the consolidated balance sheets.

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

Represents a cross currency swap to pay 2.584% on £105 million and receive 3.75% on \$131 million through February 1, 2019, with an initial and final exchange of principals at origination and maturity at a rate of 1.251 USD/GBP. Hedges the risk of changes in the USD equivalent value of a portion of the Company's net investment in its consolidated GBP subsidiaries' attributable to changes in the USD/GBP exchange rate.

The Company uses derivative instruments to mitigate the effects of interest rate and foreign currency fluctuations on specific forecasted transactions as well as recognized financial obligations or assets. Utilizing derivative instruments allows the Company to manage the risk of fluctuations in interest and foreign currency rates related to the potential impact these changes could have on future earnings and forecasted cash flows. The Company does not use derivative instruments for speculative or trading purposes. Assuming a one percentage point shift in the underlying interest rate curve, the estimated change in fair value of each of the underlying derivative instruments would not exceed \$3 million. Assuming a one percentage point shift in the underlying foreign currency exchange rates, the estimated change in fair value of each of the underlying derivative instruments would not exceed \$2 million.

At June 30, 2017, £150 million of the Company's GBP-denominated borrowings under the 2015 Term Loan and a £105 million cross currency swap are designated as a hedge of a portion of the Company's net investments in GBP-functional subsidiaries to mitigate its exposure to fluctuations in the GBP to USD exchange rate. For instruments that are designated and qualify as net

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investment hedges, the variability in the foreign currency to USD exchange rate of the instrument is recorded as part of the cumulative translation adjustment component of accumulated other comprehensive income (loss). Accordingly, the remeasurement value of the designated £150 million GBP-denominated borrowings and £105 million cross currency swap due to fluctuations in the GBP to USD exchange rate are reported in accumulated other comprehensive income (loss) as the hedging relationship is considered to be effective. The cumulative balance of the remeasurement value will be reclassified to earnings when the hedged investment is sold or substantially liquidated.

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### Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

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

#### Cautionary Language Regarding Forward-Looking Statements

Statements in this Quarterly Report on Form 10-Q that are not historical factual statements are "forward-looking statements." We intend to have our forward-looking statements covered by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 and include this statement for purposes of complying with those provisions. Forward-looking statements include, among other things, statements regarding our and our officers' intent, belief or expectation as identified by the use of words such as "may," "will," "project," "expect," "believe," "intend," "anticipate," "seek," "forecast," "plan," "potential," "estimate," "could," "would," "should" and other comparable and derivative terms or the negative thereof. Forward-looking statements reflect our current expectations and views about future events and are subject to known and unknown risks and uncertainties that could significantly affect our future financial condition and results of operations. While forward-looking statements reflect our good faith belief and assumptions we believe to be reasonable based upon current information, we can give no assurance that our expectations or forecasts will be attained. As more fully set forth under "Part I, Item 1A. "Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2016, and Part II, Item 1A. "Risk Factors" in our Quarterly Report on Form 10-Q for the fiscal quarter ended March 31, 2017, risks and uncertainties that may cause our actual results to differ materially from the expectations contained in the forward-looking statements include, among other things:

- our reliance on a concentration of a small number of tenants and operators for a significant portion of our revenues, with our concentration in Brookdale Senior Living, Inc. ("Brookdale") increasing as a result of the consummation of the Spin-Off of Quality Care Properties, Inc. ("QCP") on October 31, 2016;
  - the financial condition of our existing and future tenants, operators and borrowers, including potential bankruptcies and downturns in their businesses, and their legal and regulatory proceedings, which results in uncertainties regarding our ability to continue to realize the full benefit of such tenants' and operators' leases and borrowers' loans;
  - the ability of our existing and future tenants, operators and borrowers to conduct their respective businesses in a manner sufficient to maintain or increase their revenues and to generate sufficient income to make rent and loan payments to us and our ability to recover investments made, if applicable, in their operations;
  - competition for tenants and operators, including with respect to new leases and mortgages and the renewal or rollover of existing leases;
  - our concentration in the healthcare property sector, particularly in life sciences, medical office buildings and hospitals, which makes our profitability more vulnerable to a downturn in a specific sector that if we were investing in multiple industries;
  - availability of suitable properties to acquire at favorable prices, the competition for the acquisition and financing of those properties, and the costs of associated property development;
  - our ability to negotiate the same or better terms with new tenants or operators if existing leases are not renewed or we exercise our right to foreclose on loan collateral or replace an existing tenant or operator upon default;
  - the risks associated with our investments in joint ventures and unconsolidated entities, including our lack of sole decision making authority and our reliance on our partners' financial condition and continued cooperation;
  - our ability to achieve the benefits of investments within expected time frames or at all, or within expected cost projections;
  - operational risks associated with third party management contracts, including the additional regulation and liabilities of our RIDEA lease structures;
  - the potential impact on us and our tenants, operators and borrowers from current and future litigation matters, including the possibility of larger than expected litigation costs, adverse results and related developments;
  - the effect on our tenants and operators of legislation and other legal requirements, including the Affordable Care Act and licensure, certification and inspection requirements, as well as laws addressing entitlement programs and related services, including Medicare and Medicaid, which may result in future reductions in reimbursements;
-

changes in federal, state or local laws and regulations, including those affecting the healthcare industry that affect our costs of compliance or increase the costs, or otherwise affect the operations, of our tenants and operators;

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volatility or uncertainty in the capital markets, the availability and cost of capital as impacted by interest rates, changes in our credit ratings, and the value of our common stock, and other conditions that may adversely impact our ability to fund our obligations or consummate transactions, or reduce the earnings from potential transactions; changes in global, national and local economic conditions, and currency exchange rates; our ability to manage our indebtedness level and changes in the terms of such indebtedness; competition for skilled management and other key personnel; and

- our ability to maintain our qualification as a REIT.

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

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

Executive Summary

2017 Transaction Overview

Dividends

Results of Operations

Liquidity and Capital Resources

Off-Balance Sheet Arrangements

Inflation

Non-GAAP Financial Measures Reconciliations

Critical Accounting Policies

Recent Accounting Pronouncements

Executive Summary

HCP, Inc., a Standard & Poor's ("S&P") 500 company, invests primarily in real estate serving the healthcare industry in the United States. We are a Maryland corporation organized in 1985 and qualify as a self-administered REIT. We acquire, develop, lease, manage and dispose of healthcare real estates. At June 30, 2017, our portfolio of investments, including properties in our unconsolidated joint ventures ("JVs"), consisted of interests in 799 properties.

We invest and manage our real estate portfolio for the long-term to maximize the benefit to our stockholders and support the growth of our dividends. The core elements of our strategy are: (i) to acquire, develop, lease, own and manage a diversified portfolio of quality healthcare properties across multiple geographic locations and business segments including senior housing, medical office, and life science, among others; (ii) to align ourselves with leading healthcare companies, operators and service providers, which over the long-term, should result in higher relative rental rates, net operating cash flows and appreciation of property values; (iii) to maintain adequate liquidity with long-term fixed rate debt financing with staggered maturities, which supports the longer-term nature of our investments, while reducing our exposure to interest rate volatility and refinancing risk at any point in the interest rate or credit cycles; and (iv) to continue to manage our balance sheet with a targeted financial leverage of 40% relative to our assets.

We believe that our real estate portfolio holds the potential for increased future cash flows as it is well-maintained and in desirable locations within markets where new supply is generally limited by the lack of available sites and the difficulty of obtaining the necessary licensing, other approvals and/or financing. Our strategy for maximizing the benefits from these opportunities is to: (i) work with new or existing tenants and operators to address their space and capital needs and (ii) provide high-quality property management services in order to motivate tenants to renew, expand or relocate into our properties.

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



While we emphasize healthcare real estate ownership, we may also provide real estate secured financing to, or invest in equity or debt securities of, healthcare operators or other entities engaged in healthcare real estate ownership. We may also acquire all or substantially all of the securities or assets of other REITs, operating companies or similar entities where such investments would

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be consistent with our investment strategies. We may co-invest alongside institutional or development investors through partnerships or limited liability companies.

We monitor, but do not limit, our investments based on the percentage of our total assets that may be invested in any one property type, investment vehicle or geographic location, the number of properties that may be leased to a single tenant or operator, or loans that may be made to a single borrower. In allocating capital, we target opportunities with the most attractive risk/reward profile for our portfolio as a whole. We may take additional measures to mitigate risk, including diversifying our investments (by sector, geography, tenant or operator), structuring transactions as master leases, requiring tenant or operator insurance and indemnifications, and obtaining credit enhancements in the form of guarantees, letters of credit or security deposits.

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

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

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

### 2017 Transaction Overview

#### Acquisition Transactions

In June 2017, we acquired Wateridge, a 124,000 square foot campus in the Sorrento Mesa submarket of San Diego for \$26 million. Upon acquisition, we commenced repositioning one of the buildings into class-A lab space following an office-to-lab conversion strategy.

In July 2017, we acquired a portfolio of three medical office buildings in Texas for \$48 million.

#### Disposition and Loan Repayment Transactions

In January 2017, we sold four life science facilities in Salt Lake City, Utah for \$76 million, resulting in a net gain on sale of \$45 million.

In January 2017, we completed the contribution of our ownership interest in RIDEA II to an unconsolidated JV owned by HCP and an investor group led by Columbia Pacific Advisors, LLC (“the HCP/CPA JV”). In addition, RIDEA II was recapitalized with \$602 million of debt, of which \$360 million was provided by a third-party and \$242 million was provided by HCP. In return, we received \$480 million in cash proceeds from the HCP/CPA JV and \$242 million in note receivables and retained an approximate 40% beneficial interest in RIDEA II (the note receivable and 40% beneficial interest are herein referred to as the “RIDEA II Investments”). This transaction resulted in HCP deconsolidating the net assets of RIDEA II and recognizing a net gain on sale of \$99 million.

In March 2017, we sold 64 senior housing triple-net assets, previously under triple-net leases with Brookdale, for \$1.125 billion to affiliates of Blackstone Real Estate Partners VIII, L.P., resulting in a net gain on sale of \$170 million.

In March 2017, we sold our aggregate £138.5 million par value Four Seasons senior notes (“Four Seasons Notes”) for £83 million (\$101 million). The disposition of the Four Seasons Notes generated a £42 million (\$51 million) gain on sale as the sales price was above the previously-impaired carrying value of £41 million (\$50 million). In addition, we sold our Four Seasons senior secured term loan at par plus accrued interest for £29 million (\$35 million).

In February 2017, we sold a hospital within one of our DFLs in Palm Beach Gardens, Florida for \$43 million to the current tenant.

In April 2017, we sold a land parcel in San Diego, California for \$27 million and one life science building in San Diego, California for \$5 million.

In June 2017, we received £283 million (\$367 million) from the repayment of our HC-One Facility.

### Financing Activities

During the six months ended June 30, 2017, we had net repayments of \$781 million on our revolving line of credit primarily using proceeds from the RIDEA II joint venture disposition, the sale of our Four Seasons Notes and the repayment of our HC-One Facility.

In March 2017, we repaid our £137 million unsecured term loan (the “2012 Term Loan”) and \$472 million of mortgage debt.

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In May 2017, we repaid \$250 million of maturing senior unsecured notes.

In June 2017, we paid down £51 million of our £220 million unsecured term loan (the “2015 Term Loan”).

In July 2017, we repurchased \$500 million of our 5.375% senior notes due 2021 and expect to record approximately \$54 million of loss on debt extinguishment in the third quarter of 2017.

#### Developments and Redevelopments

During the second quarter of 2017 and through July 2017, we added \$116 million of new projects to our development and redevelopment pipelines including:

- Commenced \$22 million of redevelopment projects at two recently-acquired life science assets in the Sorrento Mesa submarket of San Diego.

- Commenced a \$40 million redevelopment of a medical office building located in the University City submarket in Philadelphia near the University of Pennsylvania.

Entered into a joint venture agreement and commenced development on a 111 unit senior housing facility in Otay Ranch, California (San Diego MSA) for \$31 million. Our share of the total construction cost is approximately \$28 million with an estimated completion in the second half of 2018.

In June, commenced development on a 79 unit senior housing facility in Waldwick, New Jersey (New York MSA) for \$31 million. Our share of the total construction costs is approximately \$26 million with an estimated completion in late 2018.

#### Dividends

The following table summarizes our common stock cash dividends declared in 2017:

| Declaration Date | Record Date | Amount<br>Per Share | Dividend<br>Payable Date |
|------------------|-------------|---------------------|--------------------------|
| February 2       | February 15 | \$ 0.37             | March 2                  |
| April 27         | May 8       | 0.37                | May 23                   |
| July 27          | August 7    | 0.37                | August 22                |

#### Results of Operations

We evaluate our business and allocate resources among our reportable business segments: (i) senior housing triple-net; (ii) senior housing operating portfolio (“SHOP”); (iii) life science; and (iv) medical office. Under the medical office segment, we invest through the acquisition and development of medical office buildings (“MOBs”), which generally require a greater level of property management. Otherwise, we primarily invest, through the acquisition and development of real estate, in single tenant and operator properties. We have other non-reportable segments that are comprised primarily of our U.K. care homes, debt investments and hospitals. We evaluate performance based upon (i) property net operating income from continuing operations (“NOI”) and (ii) adjusted NOI (cash NOI) of the combined consolidated and unconsolidated investments in each segment. The accounting policies of the segments are the same as those described in the summary of significant accounting policies in Note 2 of our Annual Report on Form 10-K for the year ended December 31, 2016 filed with the U.S. Securities and Exchange Commission (“SEC”), as updated by Note 2 herein.

#### Non-GAAP Financial Measures

##### Net Operating Income (“NOI”)

NOI and adjusted NOI are non-U.S. generally accepted accounting principles (“GAAP”) supplemental financial measures used to evaluate the operating performance of real estate. We include properties from our consolidated portfolio, as well as our pro-rata share of properties owned by our unconsolidated joint ventures, in our NOI and adjusted NOI. We believe providing this information assists investors and analysts in estimating the economic interest in our total portfolio of real estate. Our pro-rata share information is prepared on a basis consistent with the comparable consolidated amounts, is intended to reflect our proportionate economic interest in the operating results of properties in our portfolio and is calculated by applying our actual ownership percentage for the period. We do not control the unconsolidated joint ventures, and the pro-rata presentations of revenues and expenses included in NOI (see below) do not represent our legal claim to such items. The joint venture members or partners are entitled to profit or loss allocations and distributions of cash flows according to the joint venture agreements, which provide for such allocations generally according to their invested capital.



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

NOI is defined as rental and related revenues, including tenant recoveries, resident fees and services, and income from DFLs, less property level operating expenses; NOI excludes all other financial statement amounts included in net income (loss) as presented in Note 13 to the Consolidated Financial Statements. Management believes NOI provides relevant and useful information because it reflects only income and operating expense items that are incurred at the property level and presents them on an unleveraged basis. Adjusted NOI is calculated as NOI after eliminating the effects of straight-line rents, DFL non-cash interest, amortization of market lease intangibles, non-refundable entrance fees, net of entrance fee amortization and lease termination fees and the impact of deferred community fee income and expense (“Adjustments to NOI”). The Adjustments to NOI and resulting Adjusted NOI for SHOP have been restated for prior periods presented to conform to the current period presentation for the adjustment to exclude the impact of deferred community fee income and expense, resulting in recognition as cash is received and expenses are paid. Adjusted NOI is oftentimes referred to as “cash NOI.” We use NOI and adjusted NOI to make decisions about resource allocations, to assess and compare property level performance, and to evaluate our same property portfolio (“SPP”), as described below. We believe that net income (loss) is the most directly comparable GAAP measure to NOI. NOI should not be viewed as an alternative measure of operating performance to net income (loss) as defined by GAAP since it does not reflect various excluded items. Further, our definition of NOI may not be comparable to the definition used by other REITs or real estate companies, as they may use different methodologies for calculating NOI. For a reconciliation of NOI and Adjusted NOI to net income (loss) by segment, refer to Note 13 to the Consolidated Financial Statements.

Operating expenses generally relate to leased medical office and life science properties and SHOP facilities. We generally recover all or a portion of our leased medical office and life science property expenses through tenant recoveries. We present expenses as operating or general and administrative based on the underlying nature of the expense. Periodically, we review the classification of expenses between categories and make revisions based on changes in the underlying nature of the expenses.

#### Same Property Portfolio

SPP NOI and adjusted NOI information allows us to evaluate the performance of our property portfolio under a consistent population by eliminating changes in the composition of our portfolio of properties. We include properties from our consolidated portfolio, as well as properties owned by our unconsolidated joint ventures in our SPP NOI and adjusted NOI (see NOI above for further discussion regarding our use of pro-rata share information and its limitations). We identify our SPP as stabilized properties that remained in operations and were consistently reported as leased properties or RIDEA properties for the duration of the year-over-year comparison periods presented, excluding assets held for sale. Accordingly, it takes a stabilized property a minimum of 12 months in operations under a consistent reporting structure to be included in our SPP. Newly acquired operating assets are generally considered stabilized at the earlier of lease-up (typically when the tenant(s) control(s) the physical use of at least 80% of the space) or 12 months from the acquisition date. Newly completed developments and redevelopments are considered stabilized at the earlier of lease-up or 24 months from the date the property is placed in service. SPP NOI excludes (i) certain non-property specific operating expenses that are allocated to each operating segment on a consolidated basis and (ii) entrance fees and related activity such as deferred expenses, reserves and management fees related to entrance fees. A property is removed from our SPP when it is classified as held for sale, sold, placed into redevelopment or changes its reporting structure. For a reconciliation of SPP to total portfolio adjusted NOI and other relevant disclosures by segment, refer to our Segment Analysis below.

#### Funds From Operations (“FFO”)

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

FFO, as defined by the National Association of Real Estate Investment Trusts ("NAREIT"), is net income (loss) applicable to common shares (computed in accordance with GAAP), excluding gains or losses from sales of depreciable property, including any current and deferred taxes directly associated with sales of depreciable property, impairments of, or related to, depreciable real estate, plus real estate and other depreciation and amortization, and adjustments to compute our share of FFO and FFO as adjusted (see below) from joint ventures. Adjustments for joint ventures are calculated to reflect our pro-rata share of both our consolidated and unconsolidated joint ventures. We reflect our share of FFO for unconsolidated joint ventures by applying our

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actual ownership percentage for the period to the applicable reconciling items on an entity by entity basis. We reflect our share for consolidated joint ventures in which we do not own 100% of the equity by adjusting our FFO to remove the third party ownership share of the applicable reconciling items based on actual ownership percentage for the applicable periods. Our pro-rata share information is prepared on a basis consistent with the comparable consolidated amounts, is intended to reflect our proportionate economic interest in the operating results of properties in our portfolio and is calculated by applying our actual ownership percentage for the period. We do not control the unconsolidated joint ventures, and the pro-rata presentations of reconciling items included in FFO (see above) do not represent our legal claim to such items. The joint venture members or partners are entitled to profit or loss allocations and distributions of cash flows according to the joint venture agreements, which provide for such allocations generally according to their invested capital. See NOI above for further discussion regarding our use of pro-rata share information and its limitations.

FFO does not represent cash generated from operating activities in accordance with GAAP, is not necessarily indicative of cash available to fund cash needs and should not be considered an alternative to net income (loss). We compute FFO in accordance with the current NAREIT definition; however, other REITs may report FFO differently or have a different interpretation of the current NAREIT definition from ours.

In addition, we present FFO before the impact of non-comparable items including, but not limited to, severance-related charges, litigation costs, preferred stock redemption charges, impairments (recoveries) of non-depreciable assets, prepayment costs (benefits) associated with early retirement or payment of debt, foreign currency remeasurement losses (gains) and transaction-related items ("FFO as adjusted"). Prepayment costs (benefits) associated with early retirement of debt include the write-off of unamortized deferred financing fees, or additional costs, expenses, discounts, make-whole payments, penalties or premiums incurred as a result of early retirement or payment of debt. Transaction-related items include expensed acquisition and pursuit costs and gains/charges incurred as a result of mergers and acquisitions and lease amendment or termination activities. Management believes that FFO as adjusted provides a meaningful supplemental measurement of our FFO run-rate and is frequently used by analysts, investors and other interested parties in the evaluation of our performance as a REIT. At the same time that NAREIT created and defined its FFO measure for the REIT industry, it also recognized that "management of each of its member companies has the responsibility and authority to publish financial information that it regards as useful to the financial community." We believe stockholders, potential investors and financial analysts who review our operating performance are best served by an FFO run-rate earnings measure that includes, in addition to adjustments made to arrive at the NAREIT defined measure of FFO, other adjustments to net income (loss). FFO as adjusted is used by management in analyzing our business and the performance of our properties, and we believe it is important that stockholders, potential investors and financial analysts understand this measure used by management. We use FFO as adjusted to: (i) evaluate our performance in comparison with expected results and results of previous periods, relative to resource allocation decisions, (ii) evaluate the performance of our management, (iii) budget and forecast future results to assist in the allocation of resources, (iv) assess our performance as compared with similar real estate companies and the industry in general and (v) evaluate how a specific potential investment will impact our future results. Other REITs or real estate companies may use different methodologies for calculating an adjusted FFO measure, and accordingly, our FFO as adjusted may not be comparable to those reported by other REITs. For a reconciliation of net income (loss) to FFO and FFO as adjusted and other relevant disclosure, refer to "Non-GAAP Financial Measures Reconciliations" below.



Table of Contents**Funds Available for Distribution (“FAD”)**

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

**Comparison of the Three and Six Months Ended June 30, 2017 to the Three and Six Months Ended June 30, 2016 Overview**

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**Three Months Ended June 30, 2017 and 2016**

The following table summarizes results for the three months ended June 30, 2017 and 2016 (dollars in thousands, except per share data):

| Three Months Ended<br>June 30, 2017 |                      | Three Months Ended<br>June 30, 2016 |                      |              |
|-------------------------------------|----------------------|-------------------------------------|----------------------|--------------|
| Amount                              | Diluted<br>Per Share | Amount                              | Diluted<br>Per Share | Per<br>Share |

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|  |           |         |            |         | Change    |
|--|-----------|---------|------------|---------|-----------|
| Net income applicable to common shares | \$ 19,283 | \$ 0.04 | \$ 301,375 | \$ 0.64 | \$(0.60 ) |
| FFO                                    | 164,650   | 0.35    | 333,218    | 0.71    | (0.36 )   |
| FFO as adjusted                        | 224,770   | 0.48    | 347,876    | 0.74    | (0.26 )   |
| FAD                                    | 200,157   |         | 337,866    |         |           |

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

- a reduction in net income from discontinued operations due to the spinoff of QCP on October 31, 2016;
- a reduction in gains on sales of real estate during the second quarter of 2017 compared to the second quarter of 2016;

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a reduction in resident fees and services, partially offset by a reduction in operating expenses due to the partial sale and deconsolidation of RIDEA II during the first quarter of 2017;  
 a reduction in incremental interest income due to the payoff of two participating development loans during the second quarter of 2016; and

an impairment of our Tandem Health Care Loan in the second quarter of 2017.

The decrease in EPS was partially offset by:

increased NOI from our 2016 acquisitions, annual rent escalations and developments placed in service; and  
 a reduction in interest expense as a result of debt repayments in the second half of 2016 and the second quarter of 2017.

FFO decreased primarily as a result of the aforementioned events impacting EPS, excluding gains on sales of real estate, which is an adjustment to our calculation of FFO.

FFO as adjusted decreased primarily as a result of the aforementioned events impacting FFO, except for the impairment of our Tandem Health Care Loan in the second quarter of 2017 which is excluded from FFO as adjusted.

FAD decreased primarily as a result of the aforementioned events impacting FFO as adjusted and increased leasing costs and tenant capital improvements and lower lease restructure payments.

Six Months Ended June 30, 2017 and 2016

The following table summarizes results for the six months ended June 30, 2017 and 2016 (dollars in thousands, except per share data):

|  | Six Months Ended<br>June 30, 2017 |                      | Six Months Ended<br>June 30, 2016 |                      |                        |
|--|-----------------------------------|----------------------|-----------------------------------|----------------------|------------------------|
|  | Amount                            | Diluted<br>Per Share | Amount                            | Diluted<br>Per Share | Per<br>Share<br>Change |
| Net income applicable to common shares | \$ 479,854                        | \$ 1.02              | \$ 417,185                        | \$ 0.89              | \$ 0.13                |
| FFO                                    | 452,882                           | 0.96                 | 652,483                           | 1.40                 | (0.44 )                |
| FFO as adjusted                        | 464,925                           | 0.99                 | 669,659                           | 1.43                 | (0.44 )                |
| FAD                                    | 418,702                           |                      | 646,906                           |                      |                        |

Earnings per share ("EPS") increased primarily as a result of the following:

increased gains on sales of real estate during the first half of 2017 compared to the first half of 2016;

a gain on sale of our Four Seasons Notes in the first quarter of 2017;

a reduction in interest expense as a result of debt repayments during the second half of 2016 and the second quarter of 2017; and

increased NOI from our 2016 acquisitions, annual rent escalations and developments placed in service.

The increase in EPS was partially offset by the following:

a reduction in net income from discontinued operations due to the spinoff of QCP on October 31, 2016;

a reduction in resident fees and services, partially offset by a reduction in operating expenses due to the partial sale and deconsolidation of RIDEA II during the first quarter of 2017;

a reduction in incremental interest income due to the payoff of two participating development loans during the second quarter of 2016; and

an impairment of our Tandem Health Care Loan in the second quarter of 2017;

FFO decreased primarily as a result of the aforementioned events impacting EPS, excluding gains on sales of real estate, which is an adjustment to our calculation of FFO.

FFO as adjusted decreased primarily as a result of the aforementioned events impacting FFO, except for the gain on sale of our Four Seasons Notes in the first quarter of 2017 offset by the impairment of our Tandem Health Care Loan in the second quarter of 2017 both of which are excluded from FFO as adjusted.

FAD decreased primarily as a result of the aforementioned events impacting FFO as adjusted, increased leasing costs and tenant capital improvements and lower lease restructure payments.



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## Segment Analysis

The tables below provide selected operating information for our SPP and total property portfolio for each of our business segments. Our SPP for the three months ended June 30, 2017 consists of 744 properties representing properties acquired or placed in service and stabilized on or prior to April 1, 2016 and that remained in operation under a consistent reporting structure through June 30, 2017. Our SPP for the six months ended June 30, 2017 consists of 737 properties representing properties acquired or placed in service and stabilized on or prior to January 1, 2016 and that remained in operation under a consistent reporting structure through June 30, 2017. Our total property portfolio consists of 799 and 853 properties at June 30, 2017 and 2016, respectively.

## Senior Housing Triple-Net

The following table summarizes results at and for the three months ended June 30, 2017 and 2016 (dollars in thousands, except per unit data):

|   | SPP                         |          |         | Total Portfolio             |           |            |
|---|-----------------------------|----------|---------|-----------------------------|-----------|------------|
|   | Three Months Ended June 30, |          |         | Three Months Ended June 30, |           |            |
|   | 2017                        | 2016     | Change  | 2017                        | 2016      | Change     |
| Rental revenues <sup>(1)</sup>          | \$78,079                    | \$76,890 | \$1,189 | \$78,079                    | \$108,841 | \$(30,762) |
| Operating expenses                      | (157 )                      | (169 )   | 12      | (882 )                      | (1,642 )  | 760        |
| NOI                                     | 77,922                      | 76,721   | 1,201   | 77,197                      | 107,199   | (30,002 )  |
| Adjustments to NOI                      | (407 )                      | (1,200 ) | 793     | (406 )                      | (2,022 )  | 1,616      |
| Adjusted NOI                            | \$77,515                    | \$75,521 | \$1,994 | 76,791                      | 105,177   | (28,386 )  |
| Non-SPP adjusted NOI                    |                             |          |         | 724                         | (29,656 ) | 30,380     |
| SPP adjusted NOI                        |                             |          |         | \$77,515                    | \$75,521  | \$1,994    |
| Adjusted NOI % change                   |                             |          | 2.6 %   |                             |           |            |
| Property count <sup>(2)</sup>           | 209                         | 209      |         | 209                         | 298       |            |
| Average capacity (units) <sup>(3)</sup> | 20,566                      | 20,567   |         | 20,566                      | 29,153    |            |
| Average annual rent per unit            | \$15,107                    | \$14,721 |         | \$15,107                    | \$14,657  |            |

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

(2) From our 2016 presentation of SPP, we removed 71 senior housing properties from SPP that were sold and 18 senior housing properties that we transitioned to SHOP.

(3) Represents average capacity as reported by the respective tenants or operators for the 12-month period and a quarter in arrears from the periods presented.

SPP adjusted NOI increased primarily as a result of the following:

• annual rent escalations; and

• higher cash rent received from our portfolio of assets leased to Sunrise Senior Living.

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

• senior housing triple-net facilities sold during 2016 and 2017; and

• the transition of 18 senior housing triple-net facilities to a RIDEA structure during the second half of 2016 and first quarter of 2017 (reported in our SHOP segment).

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

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The following table summarizes results at and for the six months ended June 30, 2017 and 2016 (dollars in thousands, except per unit data):

|   | SPP                       |           |         | Total Portfolio           |           |            |
|---|---------------------------|-----------|---------|---------------------------|-----------|------------|
|   | Six Months Ended June 30, |           |         | Six Months Ended June 30, |           |            |
|   | 2017                      | 2016      | Change  | 2017                      | 2016      | Change     |
| Rental revenues <sup>(1)</sup>          | \$152,153                 | \$150,518 | \$1,635 | \$178,112                 | \$215,731 | \$(37,619) |
| Operating expenses                      | (309)                     | (343)     | 34      | (1,993)                   | (3,716)   | 1,723      |
| NOI                                     | 151,844                   | 150,175   | 1,669   | 176,119                   | 212,015   | (35,896)   |
| Adjustments to NOI                      | (1,922)                   | (5,791)   | 3,869   | (2,245)                   | (7,466)   | 5,221      |
| Adjusted NOI                            | \$149,922                 | \$144,384 | \$5,538 | 173,874                   | 204,549   | (30,675)   |
| Non-SPP adjusted NOI                    |                           |           |         | (23,952)                  | (60,165)  | 36,213     |
| SPP adjusted NOI                        |                           |           |         | \$149,922                 | \$144,384 | \$5,538    |
| Adjusted NOI % change                   |                           |           | 3.8     | %                         |           |            |
| Property count <sup>(2)</sup>           | 204                       | 204       |         | 209                       | 298       |            |
| Average capacity (units) <sup>(3)</sup> | 20,167                    | 20,168    |         | 23,481                    | 29,100    |            |
| Average annual rent per unit            | \$14,899                  | \$14,352  |         | \$14,980                  | \$14,314  |            |

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

(2) From our 2016 presentation of SPP, we removed 71 senior housing properties from SPP that were sold and 18 senior housing properties that we transitioned to SHOP.

(3) Represents average capacity as reported by the respective tenants or operators for the 12-month period and a quarter in arrears from the periods presented.

SPP adjusted NOI increased primarily as a result of the following:

• annual rent escalations; and

• higher cash rent received from our portfolio of assets leased to Sunrise Senior Living.

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

• senior housing triple-net facilities sold during 2016 and 2017; and

• the transition of 18 senior housing triple-net facilities to a RIDEA structure during the second half of 2016 and first quarter of 2017 (reported in our SHOP segment).

The decrease to Total Portfolio NOI and adjusted NOI is partially offset by (i) increased non-SPP income from five senior housing triple-net facilities acquired in the first quarter of 2016 and (ii) the aforementioned increases to SPP.

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## Senior Housing Operating Portfolio

The following table summarizes results at and for the three months ended June 30, 2017 and 2016 (dollars in thousands, except per unit data):

|   | SPP                         |           |         | Total Portfolio             |            |            |
|---|-----------------------------|-----------|---------|-----------------------------|------------|------------|
|   | Three Months Ended June 30, |           |         | Three Months Ended June 30, |            |            |
|   | 2017                        | 2016      | Change  | 2017                        | 2016       | Change     |
| Rental revenues <sup>(1)</sup>                    | \$92,187                    | \$91,478  | \$709   | \$125,416                   | \$164,202  | \$(38,786) |
| HCP share of unconsolidated JV revenues           | 77,681                      | 75,464    | 2,217   | 81,368                      | 52,855     | 28,513     |
| Operating expenses                                | (59,759 )                   | (57,945 ) | (1,814) | (85,866 )                   | (115,443 ) | 29,577     |
| HCP share of unconsolidated JV operating expenses | (64,699 )                   | (61,803 ) | (2,896) | (65,487 )                   | (42,473 )  | (23,014 )  |
| NOI   | 45,410                      | 47,194    | (1,784) | 55,431                      | 59,141     | (3,710 )   |
| Adjustments to NOI                                | 143                         | (922 )    | 1,065   | 4,523                       | 4,248      | 275        |
| Adjusted NOI                                      | \$45,553                    | \$46,272  | \$(719) | 59,954                      | 63,389     | (3,435 )   |
| Non-SPP adjusted NOI                              |                             |           |         | (14,401 )                   | (17,117 )  | 2,716      |
| SPP adjusted NOI                                  |                             |           |         | \$45,553                    | \$46,272   | \$(719 )   |
| Adjusted NOI % change                             |                             |           | (1.6 )% |                             |            |            |
| Property count <sup>(2)</sup>                     | 124                         | 124       |         | 153                         | 107        |            |
| Average capacity (units) <sup>(3)</sup>           | 22,334                      | 16,959    |         | 25,484                      | 23,411     |            |
| Average annual rent per unit                      | \$50,592                    | \$49,696  |         | \$52,345                    | \$56,237   |            |

(1) Represents rental and related revenues.

From our past presentation of SPP, we have recast the components of SPP to reflect our retained 40% equity

(2) interest in RIDEA II within HCP share of unconsolidated JV revenues and operating expenses resulting from our deconsolidation of RIDEA II during the first quarter of 2017.

(3) Represents average capacity as reported by the respective tenants or operators for the 12-month period and a quarter in arrears from the periods presented.

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

• higher expense growth and occupancy declines; partially offset by

• increased rates for resident fees and services.

Total Portfolio NOI and adjusted NOI decreased primarily as a result of the aforementioned decreases to SPP and the following impacts to non-SPP:

• decreased non-SPP income from our partial sale of RIDEA II; partially offset by

• non-SPP income for 18 senior housing triple-net assets transitioned to SHOP during the second half of 2016 and first quarter of 2017.

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The following table summarizes results at and for the six months ended June 30, 2017 and 2016 (dollars in thousands, except per unit data):

|   | SPP                       |            |          | Total Portfolio           |            |            |
|---|---------------------------|------------|----------|---------------------------|------------|------------|
|   | Six Months Ended June 30, |            |          | Six Months Ended June 30, |            |            |
|   | 2017                      | 2016       | Change   | 2017                      | 2016       | Change     |
| Rental revenues <sup>(1)</sup>                    | \$185,855                 | \$183,830  | \$2,025  | \$265,644                 | \$329,964  | \$(64,320) |
| HCP share of unconsolidated JV revenues           | 154,362                   | 150,255    | 4,107    | 157,731                   | 103,284    | 54,447     |
| Operating expenses                                | (118,340 )                | (115,729 ) | (2,611 ) | (180,405 )                | (229,446 ) | 49,041     |
| HCP share of unconsolidated JV operating expenses | (126,588 )                | (122,698 ) | (3,890 ) | (125,014 )                | (83,668 )  | (41,346 )  |
| NOI   | 95,289                    | 95,658     | (369 )   | 117,956                   | 120,134    | (2,178 )   |
| Adjustments to NOI                                | (193 )                    | (1,304 )   | 1,111    | 7,679                     | 8,642      | (963 )     |
| Adjusted NOI                                      | \$95,096                  | \$94,354   | \$742    | 125,635                   | 128,776    | (3,141 )   |
| Non-SPP adjusted NOI                              |                           |            |          | (30,539 )                 | (34,422 )  | 3,883      |
| SPP adjusted NOI                                  |                           |            |          | \$95,096                  | \$94,354   | \$742      |
| Adjusted NOI % change                             |                           |            | 0.8 %    |                           |            |            |
| Property count <sup>(2)</sup>                     | 123                       | 123        |          | 153                       | 107        |            |
| Average capacity (units) <sup>(3)</sup>           | 21,703                    | 16,829     |          | 25,491                    | 23,386     |            |
| Average annual rent per unit                      | \$51,532                  | \$49,939   |          | \$53,712                  | \$56,119   |            |

(1) Represents rental and related revenues.

From our past presentation of SPP, we have recast the components of SPP to reflect our retained 40% equity

(2) interest in RIDEA II within HCP share of unconsolidated JV revenues and operating expenses resulting from our deconsolidation of RIDEA II during the first quarter of 2017.

(3) Represents average capacity as reported by the respective tenants or operators for the 12-month period and a quarter in arrears from the periods presented.

SPP adjusted NOI increased primarily as a result of the following:

• increased rates for resident fees and services; partially offset by

• higher expense growth and a decline in occupancy.

Total Portfolio NOI and adjusted NOI decreased primarily as a result of decreased non-SPP income from our partial sale of RIDEA II, partially offset by the aforementioned increases to SPP and increases to non-SPP income from the transition of 18 senior housing triple-net assets to SHOP.



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## Life Science

The following table summarizes results at and for the three months ended June 30, 2017 and 2016 (dollars and square feet in thousands, except per square foot data):

|  | SPP                         |           |          | Total Portfolio             |           |           |
|--|-----------------------------|-----------|----------|-----------------------------|-----------|-----------|
|  | Three Months Ended June 30, |           |          | Three Months Ended June 30, |           |           |
|  | 2017                        | 2016      | Change   | 2017                        | 2016      | Change    |
| Rental revenues <sup>(1)</sup>                         | \$81,740                    | \$79,247  | \$2,493  | \$86,730                    | \$90,201  | \$(3,471) |
| HCP share of unconsolidated JV revenues                | 1,975                       | 1,870     | 105      | 2,004                       | 1,898     | 106       |
| Operating expenses                                     | (16,559 )                   | (15,355 ) | (1,204 ) | (18,744 )                   | (17,961 ) | (783 )    |
| HCP share of unconsolidated JV operating expenses      | (429 )                      | (400 )    | (29 )    | (429 )                      | (400 )    | (29 )     |
| NOI  | 66,727                      | 65,362    | 1,365    | 69,561                      | 73,738    | (4,177 )  |
| Adjustments to NOI                                     | 1,022                       | 1         | 1,021    | (91 )                       | (544 )    | 453       |
| Adjusted NOI   | \$67,749                    | \$65,363  | \$2,386  | 69,470                      | 73,194    | (3,724 )  |
| Non-SPP adjusted NOI                                   |                             |           |          | (1,721 )                    | (7,831 )  | 6,110     |
| SPP adjusted NOI                                       |                             |           |          | \$67,749                    | \$65,363  | \$2,386   |
| Adjusted NOI % change                                  |                             |           | 3.7 %    |                             |           |           |
| Property count <sup>(2)</sup>                          | 116                         | 116       |          | 119                         | 117       |           |
| Average occupancy                                      | 96.2 %                      | 98.2 %    |          | 96.4 %                      | 98.4 %    |           |
| Average occupied square feet                           | 6,695                       | 6,825     |          | 6,948                       | 7,620     |           |
| Average annual total revenues per occupied square foot | \$52                        | \$48      |          | \$52                        | \$49      |           |
| Average annual base rent per occupied square foot      | \$42                        | \$39      |          | \$42                        | \$40      |           |

(1) Represents rental and related revenues and tenant recoveries.

(2) From our past presentation of SPP for the three months ended June 30, 2016, we removed five life science facilities that were sold.

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

- mark-to-market lease renewals;
- new leasing activity; and,
- specific to adjusted NOI, annual rent escalations.

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

- decreased income from the sale of life science facilities in 2016 and 2017; partially offset by
- increased income from (i) increased occupancy in portions of a development placed in operations in 2016 and 2017 and (ii) life science acquisitions in 2016 and 2017.

The decrease in Total Portfolio NOI and adjusted NOI was also partially offset by the aforementioned increases to SPP.

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The following table summarizes results at and for the six months ended June 30, 2017 and 2016 (dollars and square feet in thousands, except per square foot data):

|  | SPP                       |           |          | Total Portfolio           |           |           |
|--|---------------------------|-----------|----------|---------------------------|-----------|-----------|
|  | Six Months Ended June 30, |           |          | Six Months Ended June 30, |           |           |
|  | 2017                      | 2016      | Change   | 2017                      | 2016      | Change    |
| Rental revenues <sup>(1)</sup>                         | \$162,360                 | \$156,232 | \$6,128  | \$172,050                 | \$179,149 | \$(7,099) |
| HCP share of unconsolidated JV revenues                | 3,887                     | 3,665     | 222      | 3,944                     | 3,708     | 236       |
| Operating expenses                                     | (31,723 )                 | (29,359 ) | (2,364 ) | (36,064 )                 | (34,704 ) | (1,360 )  |
| HCP share of unconsolidated JV operating expenses      | (800 )                    | (774 )    | (26 )    | (800 )                    | (774 )    | (26 )     |
| NOI  | 133,724                   | 129,764   | 3,960    | 139,130                   | 147,379   | (8,249 )  |
| Adjustments to NOI                                     | 1,350                     | (73 )     | 1,423    | (345 )                    | (1,217 )  | 872       |
| Adjusted NOI   | \$135,074                 | \$129,691 | \$5,383  | 138,785                   | 146,162   | (7,377 )  |
| Non-SPP adjusted NOI                                   |                           |           |          | (3,711 )                  | (16,471 ) | 12,760    |
| SPP adjusted NOI                                       |                           |           |          | \$135,074                 | \$129,691 | \$5,383   |
| Adjusted NOI % change                                  |                           |           | 4.2 %    |                           |           |           |
| Property count <sup>(2)</sup>                          | 116                       | 116       |          | 119                       | 117       |           |
| Average occupancy                                      | 96.7 %                    | 98.0 %    |          | 96.3 %                    | 98.2 %    |           |
| Average occupied square feet                           | 6,726                     | 6,808     |          | 6,976                     | 7,640     |           |
| Average annual total revenues per occupied square foot | \$51                      | \$48      |          | \$51                      | \$48      |           |
| Average annual base rent per occupied square foot      | \$42                      | \$39      |          | \$42                      | \$40      |           |

(1) Represents rental and related revenues and tenant recoveries.

(2) From our past presentation of SPP for the six months ended June 30, 2016, we removed five life science facilities that were sold.

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

- mark-to-market lease renewals;
- new leasing activity; and,
- specific to adjusted NOI, annual rent escalations.

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

- decreased income from the sale of life science facilities in 2016 and 2017; partially offset by
  - increased income from (i) increased occupancy in portions of a development placed in operations in 2016 and 2017 and (ii) life science acquisitions in 2016 and 2017.

The decrease in Total Portfolio NOI and adjusted NOI was also partially offset by the aforementioned increases to SPP.

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## Medical Office

The following table summarizes results at and for the three months ended June 30, 2017 and 2016 (dollars and square feet in thousands, except per square foot data):

|  | SPP                         |           |          | Total Portfolio             |           |          |
|--|-----------------------------|-----------|----------|-----------------------------|-----------|----------|
|  | Three Months Ended June 30, |           |          | Three Months Ended June 30, |           |          |
|  | 2017                        | 2016      | Change   | 2017                        | 2016      | Change   |
| Rental revenues <sup>(1)</sup>                         | \$101,305                   | \$98,712  | \$2,593  | \$119,164                   | \$110,205 | \$8,959  |
| HCP share of unconsolidated JV revenues                | 473                         | 468       | 5        | 496                         | 524       | (28 )    |
| Operating expenses                                     | (38,449 )                   | (36,941 ) | (1,508 ) | (46,581 )                   | (43,028 ) | (3,553 ) |
| HCP share of unconsolidated JV operating expenses      | (145 )                      | (154 )    | 9        | (146 )                      | (155 )    | 9        |
| NOI  | 63,184                      | 62,085    | 1,099    | 72,933                      | 67,546    | 5,387    |
| Adjustments to NOI                                     | 568                         | 29        | 539      | (769 )                      | (753 )    | (16 )    |
| Adjusted NOI   | \$63,752                    | \$62,114  | \$1,638  | 72,164                      | 66,793    | 5,371    |
| Non-SPP adjusted NOI                                   |                             |           |          | (8,412 )                    | (4,679 )  | (3,733 ) |
| SPP adjusted NOI                                       |                             |           |          | \$63,752                    | \$62,114  | \$1,638  |
| Adjusted NOI % change                                  |                             |           | 2.6 %    |                             |           |          |
| Property count <sup>(2)</sup>                          | 215                         | 215       |          | 239                         | 227       |          |
| Average occupancy                                      | 91.9 %                      | 91.9 %    |          | 92.0 %                      | 91.4 %    |          |
| Average occupied square feet                           | 14,502                      | 14,519    |          | 16,833                      | 15,728    |          |
| Average annual total revenues per occupied square foot | \$28                        | \$27      |          | \$28                        | \$28      |          |
| Average annual base rent per occupied square foot      | \$24                        | \$23      |          | \$24                        | \$24      |          |

(1) Represents rental and related revenues and tenant recoveries.

(2) From our past presentation of SPP, we removed two MOB's that were sold and seven MOB's that were placed into redevelopment.

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

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

- increased income from 2016 acquisitions; and

- increased occupancy in former redevelopment and development properties that have been placed into operations; partially offset by

- decreased income from the sale of four MOB's during 2016 and 2017 and the placement of an MOB into redevelopment.

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The following table summarizes results at and for the six months ended June 30, 2017 and 2016 (dollars and square feet in thousands, except per square foot data):

|  | SPP                       |           |          | Total Portfolio           |           |          |
|--|---------------------------|-----------|----------|---------------------------|-----------|----------|
|  | Six Months Ended June 30, |           |          | Six Months Ended June 30, |           |          |
|  | 2017                      | 2016      | Change   | 2017                      | 2016      | Change   |
| Rental revenues <sup>(1)</sup>                         | \$201,561                 | \$196,027 | \$5,534  | \$237,535                 | \$218,228 | \$19,307 |
| HCP share of unconsolidated JV revenues                | 940                       | 937       | 3        | 985                       | 1,003     | (18 )    |
| Operating expenses                                     | (75,524 )                 | (73,179 ) | (2,345 ) | (91,444 )                 | (84,977 ) | (6,467 ) |
| HCP share of unconsolidated JV operating expenses      | (288 )                    | (304 )    | 16       | (288 )                    | (304 )    | 16       |
| NOI  | 126,689                   | 123,481   | 3,208    | 146,788                   | 133,950   | 12,838   |
| Adjustments to NOI                                     | 745                       | (495 )    | 1,240    | (1,739 )                  | (1,548 )  | (191 )   |
| Adjusted NOI   | \$127,434                 | \$122,986 | \$4,448  | 145,049                   | 132,402   | 12,647   |
| Non-SPP adjusted NOI                                   |                           |           |          | (17,615 )                 | (9,416 )  | (8,199 ) |
| SPP adjusted NOI                                       |                           |           |          | \$127,434                 | \$122,986 | \$4,448  |
| Adjusted NOI % change                                  |                           |           | 3.6 %    |                           |           |          |
| Property count <sup>(2)</sup>                          | 215                       | 215       |          | 239                       | 227       |          |
| Average occupancy                                      | 92.0                      | % 91.9    | %        | 92.0                      | % 91.3    | %        |
| Average occupied square feet                           | 14,522                    | 14,511    |          | 16,797                    | 15,669    |          |
| Average annual total revenues per occupied square foot | \$28                      | \$27      |          | \$28                      | \$28      |          |
| Average annual base rent per occupied square foot      | \$24                      | \$23      |          | \$24                      | \$24      |          |

(1) Represents rental and related revenues and tenant recoveries.

(2) From our past presentation of SPP, we removed two MOB's that were sold and seven MOB's that were placed into redevelopment.

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

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

- increased income from 2016 acquisitions; and

- increased occupancy in former redevelopment and development properties that have been placed into operations; partially offset by

- decreased income from the sale of four MOB's during 2016 and 2017 and the placement of an MOB into redevelopment.

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## Other Income and Expense Items

The following table summarizes our other income and expense items results for the three and six months ended June 30, 2017 and 2016 (in thousands):

|   | Three Months Ended June 30, |          |            | Six Months Ended June 30, |          |            |
|---|-----------------------------|----------|------------|---------------------------|----------|------------|
|   | 2017                        | 2016     | Change     | 2017                      | 2016     | Change     |
| Interest income   | \$20,869                    | \$32,787 | \$(11,918) | \$39,200                  | \$50,816 | \$(11,616) |
| Interest expense  | 77,788                      | 121,333  | (43,545 )  | 164,506                   | 243,395  | (78,889 )  |
| Depreciation and amortization                           | 130,751                     | 139,919  | (9,168 )   | 267,305                   | 279,774  | (12,469 )  |
| General and administrative                              | 21,286                      | 22,779   | (1,493 )   | 43,764                    | 48,230   | (4,466 )   |
| Acquisition and pursuit costs                           | 867                         | 823      | 44         | 1,924                     | 3,298    | (1,374 )   |
| Impairment, net   | 56,682                      | —        | 56,682     | 56,682                    | —        | 56,682     |
| Gain on sales of real estate, net                       | 412                         | 119,614  | (119,202 ) | 317,670                   | 119,614  | 198,056    |
| Other income, net                                       | 71                          | 2,340    | (2,269 )   | 51,279                    | 3,632    | 47,647     |
| Income tax benefit (expense)                            | 2,987                       | 2,179    | 808        | 9,149                     | (1,525 ) | 10,674     |
| Equity income (loss) from unconsolidated joint ventures | 240                         | (1,067 ) | 1,307      | 3,509                     | (1,975 ) | 5,484      |
| Total discontinued operations                           | —                           | 107,375  | (107,375 ) | —                         | 175,783  | (175,783 ) |
| Noncontrolling interests' share in earnings             | (2,718 )                    | (3,125 ) | 407        | (5,750 )                  | (6,751 ) | 1,001      |

## Interest income

Interest income decreased for the three and six months ended June 30, 2017 as a result of incremental interest income received during the second quarter of 2016 due to the payoff of two participating development loans.

## Interest expense

Interest expense decreased for the three and six months ended June 30, 2017 as a result of senior unsecured notes and mortgage debt payoffs, which occurred primarily in the second half of 2016.

Over 95% and 90% of our total debt, inclusive of \$44 million and \$365 million of variable rate debt swapped to fixed through interest rate swaps, was fixed-rate debt as of June 30, 2017 and 2016, respectively. At June 30, 2017, our fixed-rate debt and variable rate debt had weighted average interest rates of 4.29% and 1.58%, respectively. At June 30, 2016, our fixed-rate debt and variable rate debt had weighted average interest rates of 4.73% and 1.89%, respectively. For a more detailed discussion of our interest rate risk, see “Quantitative and Qualitative Disclosures About Market Risk” in Item 3 below.

## Depreciation and amortization expense

Depreciation and amortization expense decreased for the three and six months ended June 30, 2017 primarily as a result of the sale of 64 senior housing triple-net assets and the deconsolidation of RIDEA II during the first quarter of 2017, partially offset by depreciation and amortization of assets acquired during 2016.

## General and administrative expenses

General and administrative expenses decreased for the three and six months ended June 30, 2017 primarily as a result of lower stock compensation expense.

## Impairments

Impairments increased for the three and six months ended June 30, 2017 as a result of the impairment of our Tandem Health Care Loan in the second quarter of 2017. See Note 6 to the Consolidated Financial Statements for further information related to our Tandem Health Care Loan.

## Gain on sales of real estate, net

During the six months ended June 30, 2017 (primarily in the first quarter of 2017), we sold 64 senior housing triple-net assets, five life science facilities and a 40% interest in RIDEA II and recognized total net gain on sales of real estate of \$318 million. During the three months ended June 30, 2016, we sold five post-acute/skilled nursing and two senior housing facilities for \$130



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million, a life science facility for \$74 million, two MOB's for \$19 million and a senior housing facility for \$6 million, recognizing a total net gain on sales of \$120 million.

Other income, net

Other income, net, increased for the six months ended June 30, 2017 primarily as a result of the gain on sale of our Four Seasons Notes.

Income tax expense

The decrease in income taxes for the six months ended June 30, 2017 was primarily the result of: (i) a \$5 million tax benefit from the sale of a 40% interest in RIDEA II in 2017 and (ii) a \$4 million income tax expense associated with state built-in gain tax for the disposition of certain real estate assets during 2016.

Equity income (loss) from unconsolidated joint ventures

The increase in equity income from unconsolidated joint ventures for the three and six months ended June 30, 2017 was primarily the result of income from our investment in RIDEA II in our SHOP segment.

Total discontinued operations

For the three and six months ended June 30, 2017, there were no discontinued operations. Discontinued operations for the three and six months ended June 30, 2016 relates to income from the operations of QCP.

Liquidity and Capital Resources

We anticipate that our cash flow from operations, available cash balances and cash from our various financing activities will be adequate for at least the next 12 months for purposes of: (i) funding recurring operating expenses; (ii) meeting debt service requirements, including principal payments and maturities; and (iii) satisfying our distributions to our stockholders and non-controlling interest members.

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

• fund capital expenditures, including tenant improvements and leasing costs; and

• fund future acquisition, transactional and development activities.

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

• issuance of common or preferred stock;

• issuance of additional debt, including unsecured notes and mortgage debt;

• draws on our credit facilities; and/or

• sale or exchange of ownership interests in properties.

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

Credit ratings impact our ability to access capital and directly impact our cost of capital as well. For example, as noted below, our revolving line of credit facility accrues interest at a rate per annum equal to LIBOR plus a margin that depends upon our credit ratings. We also pay a facility fee on the entire revolving commitment that depends upon our credit ratings. At July 28, 2017, we had a credit rating of BBB from Fitch, Baa2 from Moody's and BBB from S&P Global on our senior unsecured debt securities.

Cash Flow Summary

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

Cash and cash equivalents were \$392 million and \$95 million at June 30, 2017 and December 31, 2016, respectively, representing an increase of \$297 million. The following table sets forth changes in cash flows (in thousands):

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|   | Six Months Ended June 30, |            |             |
|---|---------------------------|------------|-------------|
|   | 2017                      | 2016       | Change      |
| Net cash provided by operating activities   | \$431,589                 | \$666,912  | \$(235,323) |
| Net cash provided by (used in) investing activities   | 1,957,586                 | (153,618 ) | 2,111,204   |
| Net cash used in financing activities   | (2,092,167 )              | (742,748 ) | (1,349,419) |
| The decrease in operating cash flow is primarily the result of (i) decreased Adjusted NOI related to the QCP Spin-Off and dispositions in the second half of 2016 and first half of 2017 and (ii) decreased interest received from loan repayments during the first half of 2017; partially offset by (i) 2016 acquisitions, (ii) annual rent increases, and (iii) decreased interest paid as a result of lower balances on our senior unsecured notes, term loans and line of credit. Our cash flow from operations is dependent upon the occupancy levels of our buildings, rental rates on leases, our tenants' performance on their lease obligations, the level of operating expenses and other factors. |                           |            |             |
| The following are significant investing and financing activities for the six months ended June 30, 2017:  |                           |            |             |
| • received net proceeds of \$1.7 billion from the sale of real estate, including the sale and recapitalization of RIDEA II;   |                           |            |             |
| • received net proceeds of \$550 million primarily from the sale of our Four Seasons investments, the repayment of our HC-One Facility, and a DFL repayment;  |                           |            |             |
| • made investments of \$233 million primarily for the development of real estate;   |                           |            |             |
| • repaid \$1.7 billion under our bank line of credit, 2012 Term Loan, 2015 Term Loan, senior unsecured notes and mortgage debt; and   |                           |            |             |
| • paid dividends on common stock of \$347 million.  |                           |            |             |
| Debt  |                           |            |             |

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See Note 10 in the Consolidated financial Statements for information about our outstanding debt.

See “2017 Transaction Overview” for further information regarding our significant financing activities through August 1, 2017.

#### Equity

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At June 30, 2017, we had 469 million shares of common stock outstanding, equity totaled \$6.0 billion, and our equity securities had a market value of \$15.2 billion.

At June 30, 2017, non-managing members held an aggregate of 4 million units in five limited liability companies (“DownREITs”) for which we are the managing member. The DownREIT units are exchangeable for an amount of cash approximating the then-current market value of shares of our common stock or, at our option, shares of our common stock (subject to certain adjustments, such as stock splits and reclassifications). At June 30, 2017 the DownREIT units were convertible into 7 million shares of our common stock.

#### At-The-Market Program

In June 2015, we established an at-the-market program, in connection with the renewal of our Shelf Registration Statement. Under this program, we may sell shares of our common stock from time to time having an aggregate gross sales price of up to \$750 million through a consortium of banks acting as sales agents or directly to the banks acting as principals. There was no activity during the six months ended June 30, 2017 and, at June 30, 2017, shares of our common stock having an aggregate gross sales price of \$676 million were available for sale under the at-the-market program. Actual future sales will depend upon a variety of factors, including but not limited to market conditions, the trading price of our common stock and our capital needs. We have no obligation to sell the remaining shares available for sale under our program.

#### Shelf Registration

We filed a prospectus with the SEC as part of a registration statement on Form S-3ASR, using a shelf registration process, which expires in June 2018. Under the “shelf” process, we may sell any combination of the securities described in the prospectus through one or more offerings. The securities described in the prospectus include common stock, preferred stock, depositary shares, debt securities and warrants.





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## Off-Balance Sheet Arrangements

We own interests in certain unconsolidated joint ventures as described in Note 7 to the Consolidated Financial Statements. Except in limited circumstances, our risk of loss is limited to our investment in the joint venture and any outstanding loans receivable. In addition, we have certain properties which serve as collateral for debt that is owed by a previous owner of certain of our facilities. Our risk of loss for these certain properties is limited to the outstanding debt balance plus penalties, if any. We have no other material off-balance sheet arrangements that we expect would materially affect our liquidity and capital resources except those included in our Annual Report on Form 10-K for the year ended December 31, 2016 in “Contractual Obligations” under “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

## Non-GAAP Financial Measures Reconciliations

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

|  | Three Months Ended<br>June 30, |            | Six Months Ended<br>June 30, |            |
|--|--------------------------------|------------|------------------------------|------------|
|  | 2017                           | 2016       | 2017                         | 2016       |
| Net income applicable to common shares   | \$19,283                       | \$301,375  | \$479,854                    | \$417,185  |
| Real estate related depreciation and amortization                                  | 130,751                        | 141,386    | 267,305                      | 282,708    |
| Other depreciation and amortization <sup>(1)</sup>                                 | 2,347                          | 2,974      | 5,358                        | 5,936      |
| Gain on sales of real estate, net  | (412 )                         | (119,614 ) | (317,670 )                   | (119,614 ) |
| Taxes associated with real estate dispositions <sup>(2)</sup>                      | 1                              | —          | (5,498 )                     | 53,177     |
| Equity (income) loss from unconsolidated joint ventures                            | (240 )                         | 1,067      | (3,509 )                     | 1,975      |
| FFO from unconsolidated joint ventures   | 16,554                         | 11,172     | 34,862                       | 21,550     |
| Noncontrolling interests’ and participating securities’ share in earnings          | 2,818                          | 3,467      | 6,424                        | 7,402      |
| Noncontrolling interests’ and participating securities’ share in FFO               | (6,452 )                       | (8,609 )   | (14,244 )                    | (17,836 )  |
| FFO applicable to common shares  | 164,650                        | 333,218    | 452,882                      | 652,483    |
| Distributions on dilutive convertible units and other                              | —                              | 3,525      | 3,654                        | 7,109      |
| Diluted FFO applicable to common shares  | \$164,650                      | \$336,743  | \$456,536                    | \$659,592  |
| Weighted average shares used to calculate diluted FFO per common share             | 468,839                        | 473,149    | 473,366                      | 472,667    |
| Impact of adjustments to FFO:  |                                |            |                              |            |
| Transaction-related items <sup>(3)</sup>   | \$840                          | \$14,658   | \$1,896                      | \$17,176   |
| Other impairment, net <sup>(4)</sup>   | 56,682                         | —          | 5,787                        | —          |
| Litigation costs   | 3,366                          | —          | 5,205                        | —          |
| Foreign currency remeasurement gains   | (768 )                         | —          | (845 )                       | —          |
|  | \$60,120                       | \$14,658   | \$12,043                     | \$17,176   |
| FFO as adjusted applicable to common shares  | \$224,770                      | \$347,876  | \$464,925                    | \$669,659  |
| Distributions on dilutive convertible units and other                              | 1,738                          | 3,503      | 3,632                        | 7,083      |
| Diluted FFO as adjusted applicable to common shares                                | \$226,508                      | \$351,379  | \$468,557                    | \$676,742  |
| Diluted FFO as adjusted per common share   | \$0.48                         | \$0.74     | \$0.99                       | \$1.43     |
| Weighted average shares used to calculate diluted FFO as adjusted per common share | 473,528                        | 473,149    | 473,366                      | 472,667    |

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|   | Three Months Ended<br>June 30, |           | Six Months Ended<br>June 30, |           |
|---|--------------------------------|-----------|------------------------------|-----------|
|   | 2017                           | 2016      | 2017                         | 2016      |
| FFO as adjusted applicable to common shares   | \$224,770                      | \$347,876 | \$464,925                    | \$669,659 |
| Amortization of deferred compensation   | 3,327                          | 4,160     | 7,092                        | 9,505     |
| Amortization of deferred financing costs  | 3,843                          | 5,281     | 7,702                        | 10,561    |
| Straight-line rents   | (3,168 )                       | (3,541 )  | (8,176 )                     | (11,117 ) |
| Other depreciation and amortization   | (2,347 )                       | (2,974 )  | (5,358 )                     | (5,935 )  |
| Leasing costs and tenant and capital improvements <sup>(5)</sup>  | (27,834 )                      | (21,872 ) | (51,121 )                    | (42,354 ) |
| Lease restructure payments  | 314                            | 6,318     | 854                          | 12,612    |
| CCRC entrance fees <sup>(6)</sup>   | 4,713                          | 6,046     | 8,362                        | 11,549    |
| Deferred income taxes   | (4,342 )                       | (2,604 )  | (6,716 )                     | (5,546 )  |
| Other FAD adjustments   | 881                            | (824 )    | 1,138                        | (2,028 )  |
| FAD applicable to common shares   | \$200,157                      | \$337,866 | \$418,702                    | \$646,906 |
| Distributions on dilutive convertible units and other   | 1,738                          | 3,525     | —                            | 7,109     |
| Diluted FAD applicable to common shares   | \$201,895                      | \$341,391 | \$418,702                    | \$654,015 |
| The following is a reconciliation, on a per share basis, from net income (loss) applicable to common shares, the most directly comparable financial measure calculated and presented in accordance with GAAP, to FFO and FFO as adjusted: |                                |           |                              |           |

|  | Three<br>Months<br>Ended June<br>30, |         | Six Months<br>Ended June<br>30, |         |
|--|--------------------------------------|---------|---------------------------------|---------|
|  | 2017                                 | 2016    | 2017                            | 2016    |
| Diluted earnings per common share                          | \$0.04                               | \$0.64  | \$1.02                          | \$0.89  |
| Depreciation and amortization                              | 0.28                                 | 0.30    | 0.56                            | 0.61    |
| Other depreciation and amortization                        | —                                    | 0.01    | 0.01                            | 0.01    |
| Gain on sales of real estate, net                          | —                                    | —       | (0.67 )                         | —       |
| Taxes associated with real estate dispositions             | —                                    | (0.25 ) | (0.01 )                         | (0.14 ) |
| Joint venture and participating securities FFO adjustments | 0.03                                 | 0.01    | 0.05                            | 0.03    |
| Diluted FFO per common shares                              | \$0.35                               | \$0.71  | \$0.96                          | \$1.40  |
| Transaction-related items <sup>(3)</sup>                   | —                                    | 0.03    | 0.01                            | 0.03    |
| Other impairment, net <sup>(4)</sup>                       | 0.12                                 | —       | 0.01                            | —       |
| Litigation costs   | 0.01                                 | —       | 0.01                            | —       |
| Diluted FFO as adjusted per common shares                  | \$0.48                               | \$0.74  | \$0.99                          | \$1.43  |

Other depreciation and amortization includes DFL depreciation and lease incentive amortization (reduction of (1) straight-line rents) for the consideration given to terminate the 30 purchase options on the 153-property amended lease portfolio in the 2014 Brookdale transaction.

For the six months ended June 30, 2017, represents income tax benefit associated with the disposition of real estate assets in our RIDEA II transaction. For the six months ended June 30, 2016, represents income tax expense (2) associated with the state built-in gain tax payable upon the disposition of specific real estate assets, of which \$49 million relates to the HCR ManorCare, Inc. real estate portfolio.

(3) On January 1, 2017, we early adopted the Financial Accounting Standards Board Accounting Standards Update No. 2017-01, Clarifying the Definition of a Business (“ASU 2017-01”) which prospectively results in recognizing the majority of our real estate acquisitions as asset acquisitions rather than business combinations. Acquisition and pursuit costs relating to completed asset acquisitions are capitalized, including those costs incurred prior to January 1, 2017. Real estate acquisitions completed prior to January 1, 2017 were deemed business combinations and the related acquisition and pursuit costs were expensed as incurred. For the three and six months ended June 30, 2016,

primarily relates to the QCP spin-off.

For the three months ended June 30, 2017, relates to the impairment of our Tandem Health Care Loan. For the six (4) months ended June 30, 2017, relates to the impairment of our Tandem Health Care Loan, net of the impairment recovery upon the sale of our Four Seasons Notes in the first quarter of 2017.

(5) Includes our share of leasing costs and tenant and capital improvements from unconsolidated joint ventures.

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

#### Critical Accounting Policies

The preparation of financial statements in conformity with U.S. GAAP requires our management to use judgment in the application of accounting policies, including making estimates and assumptions. We base estimates on the best information available to us at the time, our experience and on various other assumptions believed to be reasonable under the circumstances. These estimates affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting periods. If our judgment or interpretation of the facts and circumstances relating to various transactions or other matters had been different, it is possible that different accounting would have been applied, resulting in a different presentation of our consolidated financial statements. From time to time, we re-

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evaluate our estimates and assumptions. In the event estimates or assumptions prove to be different from actual results, adjustments are made in subsequent periods to reflect more current estimates and assumptions about matters that are inherently uncertain. A summary of our critical accounting policies is included in our Annual Report on Form 10-K for the year ended December 31, 2016 in “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations” and Note 2 to the Consolidated Financial Statements. There have been no significant changes to our critical accounting policies during 2017.

### Recent Accounting Pronouncements

See Note 2 to the Consolidated Financial Statements for the impact of new accounting standards.

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

We are exposed to various market risks, including the potential loss arising from adverse changes in interest rates and foreign currency exchange rates, specifically the GBP. We use derivative financial instruments in the normal course of business to mitigate interest rate and foreign currency risk. We do not use derivative financial instruments for speculative or trading purposes. Derivatives are recorded on the consolidated balance sheets at fair value (see Note 19 to the Consolidated Financial Statements).

To illustrate the effect of movements in the interest rate and foreign currency markets, we performed a market sensitivity analysis on our hedging instruments. We applied various basis point spreads to the underlying interest rate curves and foreign currency exchange rates of the derivative portfolio in order to determine the change in fair value. Assuming a one percentage point change in the underlying interest rate curve, the estimated change in fair value of each of the underlying derivative instruments would not exceed \$3 million. Assuming a one percentage point change in the underlying foreign currency exchange rates, the estimated change in fair value of each of the underlying derivative instruments would not exceed \$2 million.

**Interest Rate Risk.** At June 30, 2017, we are exposed to market risks related to fluctuations in interest rates primarily on variable rate debt. At June 30, 2017, \$44 million of our variable-rate debt was hedged by interest rate swap transactions. The interest rate swaps are designated as cash flow hedges, with the objective of managing the exposure to interest rate risk by converting the interest rates on our variable-rate debt to fixed interest rates.

Interest rate fluctuations will generally not affect our future earnings or cash flows on our fixed rate debt and assets until their maturity or earlier prepayment and refinancing. If interest rates have risen at the time we seek to refinance our fixed rate debt, whether at maturity or otherwise, our future earnings and cash flows could be adversely affected by additional borrowing costs. Conversely, lower interest rates at the time of refinancing may reduce our overall borrowing costs. However, interest rate changes will affect the fair value of our fixed rate instruments. A one percentage point increase in interest rates would change the fair value of our fixed rate debt and investments by approximately \$270 million and \$1 million, respectively, and would not materially impact earnings or cash flows. Conversely, changes in interest rates on variable rate debt and investments would change our future earnings and cash flows, but not materially impact the fair value of those instruments. Assuming a one percentage point increase in the interest rate related to the variable-rate debt and variable-rate investments, and assuming no other changes in the outstanding balance at June 30, 2017, our annual interest expense and interest income would increase by approximately \$4 million and \$1 million, respectively.

**Foreign Currency Risk.** At June 30, 2017, our exposure to foreign currencies primarily relates to U.K. investments in leased real estate, senior notes and related GBP denominated cash flows. Our foreign currency exposure is partially mitigated through the use of GBP denominated borrowings and foreign currency swap contracts. Based solely on our operating results for the three months ended June 30, 2017, including the impact of existing hedging arrangements, if the value of the GBP relative to the U.S. dollar were to increase or decrease by 10% compared to the average exchange rate during the quarter ended June 30, 2017, our cash flows would have decreased or increased, as applicable, by less than \$1 million.

**Market Risk.** We have investments in marketable debt securities classified as held-to-maturity because we have the positive intent and ability to hold the securities to maturity. Held-to-maturity securities are recorded at amortized cost and adjusted for the amortization of premiums and discounts through maturity. We consider a variety of factors in evaluating an other-than-temporary decline in value, such as: the length of time and the extent to which the market value has been less than our current adjusted carrying value; the issuer’s financial condition, capital strength and

near-term prospects; any recent events specific to that issuer and economic conditions of its industry; and our investment horizon in relationship to an anticipated near-term recovery in the market value, if any. At June 30, 2017, both the fair value and carrying value of marketable debt securities was \$18 million.

Item 4. Controls and Procedures

Disclosure Controls and Procedures. We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms and that such information is

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accumulated and communicated to our management, including our Chief Executive Officer (Principal Executive Officer) and Chief Financial Officer (Principal Financial Officer), to allow for timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As required by Rules 13a-15(b) and 15d-15(b) of the Exchange Act, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer (Principal Executive Officer) and Chief Financial Officer (Principal Financial Officer), of the effectiveness of the design and operation of our disclosure controls and procedures as of June 30, 2017. Based upon that evaluation, our Chief Executive Officer (Principal Executive Officer) and Chief Financial Officer (Principal Financial Officer) concluded that our disclosure controls and procedures were effective at the reasonable assurance level as of June 30, 2017.

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

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## PART II. OTHER INFORMATION

## Item 1. Legal Proceedings

See the “Legal Proceedings” section of Note 11 to the consolidated financial statements for information regarding legal proceedings, which information is incorporated by reference in this Item 1.

## Item 1A. Risk Factors

There are no material changes to the risk factors previously disclosed in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2016, as updated by Part II, Item 1A of our Quarterly Report on Form 10-Q for the quarter ended March 31, 2017.

## Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(a)

None.

(b)

None.

(c)

The following table sets forth information with respect to purchases of our common stock made by us or on our behalf or by any “affiliated purchaser,” as such term is defined in Rule 10b-18(a)(3) under the Exchange Act, during the three months ended June 30, 2017.

| Period Covered   | Total Number<br>Of Shares<br>Purchased <sup>(1)</sup> | Average<br>Price<br>Paid Per<br>Share | Total Number Of Shares<br>(Or Units) Purchased As<br>Part Of Publicly<br>Announced Plans Or<br>Programs | Maximum Number (Or<br>Approximate Dollar Value)<br>Of Shares (Or Units) That<br>May Yet Be Purchased<br>Under The Plans Or<br>Programs |
|------------------|---|---------------------------------------|---|--|
| April 1-30, 2017 | 109   | \$ 32.50                              | —   | —  |
| May 1-31, 2017   | 14,440  | 30.13                                 | —   | —  |
| June 1-30, 2017  | 11,738  | 33.37                                 | —   | —  |
| Total            | 26,287  | 31.59                                 | —   | —  |

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

## Item 5. Other Information

(a)

None.

(b)

None.



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Item 6. Exhibits

- 3.1 Articles of Restatement of HCP (incorporated herein by reference to Exhibit 3.1 to HCP's Registration Statement on Form S-3 (Registration No. 333 182824) filed on July 24, 2012).
- 3.2 Articles Supplementary of HCP (incorporated herein by reference to Exhibit 3.1 to HCP's Current Report on Form 8-K (File No. 001-08895) filed August 1, 2017).
- 3.3 Fifth Amended and Restated Bylaws of HCP (incorporated herein by reference to Exhibit 3.1 to HCP's Current Report on Form 8-K (File No. 001-08895), filed February 11, 2015).
- 3.4 Amendment No. 1 to the Fifth Amended and Restated Bylaws of HCP (incorporated herein by reference to Exhibit 3.1 to HCP's Current Report on Form 8-K (File No. 001-08895), filed February 1, 2016).
- 3.5 Amendment No. 2 to the Fifth Amended and Restated Bylaws of HCP (incorporated herein by reference to Exhibit 3.2 to HCP's Current Report on Form 8-K (File No. 001-08895), filed August 1, 2017).
- 31.1 Certification by Thomas M. Herzog, HCP's Principal Executive Officer, Pursuant to Securities Exchange Act Rule 13a-14(a).\*
- 31.2 Certification by Peter A. Scott, HCP's Principal Financial Officer, Pursuant to Securities Exchange Act Rule 13a-14(a).\*
- 32.1 Certification by Thomas M. Herzog, HCP's Principal Executive Officer, Pursuant to Securities Exchange Act Rule 13a-14(b) and 18 U.S.C. Section 1350.\*\*
- 32.2 Certification by Peter A. Scott, HCP's Principal Financial Officer, Pursuant to Securities Exchange Act Rule 13a-14(b) and 18 U.S.C. Section 1350.\*\*
- 101.INS XBRL Instance Document.\*
- 101.SCH XBRL Taxonomy Extension Schema Document.\*
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document.\*
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document.\*
- 101.LAB XBRL Taxonomy Extension Labels Linkbase Document.\*
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document.\*

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\* Filed herewith.

\*\* Furnished herewith.



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SIGNATURES

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

Date: August 1, 2017 HCP, Inc.

(Registrant)

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

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

/s/ SCOTT A. ANDERSON  
Scott A. Anderson  
Executive Vice President and  
Chief Accounting Officer  
(Principal Accounting Officer)