Sabra Health Care REIT, Inc.
Form 10-Q
November 02, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2016
OR
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission file number 001-34950

SABRA HEALTH CARE REIT, INC.
(Exact Name of Registrant as Specified in Its Charter)

Maryland	27-2560479
(State of Incorporation)	(I.R.S. Employer Identification No.)

18500 Von Karman Avenue, Suite 550
Irvine, CA 92612
(888) 393-8248
(Address, zip code and telephone number of Registrant)

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 x No o
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No x
As of October 28, 2016, there were 65,259,836 shares of the registrant’s $0.01 par value Common Stock outstanding.

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References throughout this document to “Sabra,” “we,” “our,” “ours” and “us” refer to Sabra Health Care REIT, Inc. and its direct and indirect consolidated subsidiaries and not any other person.

STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

Certain statements in this Quarterly Report on Form 10-Q (this “10-Q”) contain “forward-looking” information as that term is defined by the Private Securities Litigation Reform Act of 1995. Any statements that do not relate to historical or current facts or matters are forward-looking statements. Examples of forward-looking statements include all statements regarding our expected future financial position, results of operations, cash flows, liquidity, financing plans, business strategy, budgets, the expected amounts and timing of dividends and other distributions, projected expenses and capital expenditures, competitive position, growth opportunities, potential investments, plans and objectives for future operations, and compliance with and changes in governmental regulations. You can identify some of the forward-looking statements by the use of forward-looking words such as “anticipate,” “believe,” “plan,” “estimate,” “expect,” “intend,” “should,” “may” and other similar expressions, although not all forward-looking statements contain these identifying words.

Our actual results may differ materially from those projected or contemplated by our forward-looking statements as a result of various factors, including, among others, the following:

- our dependence on Genesis Healthcare, Inc. (“Genesis”) and certain wholly owned subsidiaries of Holiday AL Holdings LP (collectively, “Holiday”) until we are able to further diversify our portfolio;
- our dependence on the operating success of our tenants;
- the significant amount of and our ability to service our indebtedness;
- covenants in our debt agreements that may restrict our ability to pay dividends, make investments, incur additional indebtedness and refinance indebtedness on favorable terms;
- increases in market interest rates;
- changes in foreign currency exchange rates;
- our ability to raise capital through equity and debt financings;
- the impact of required regulatory approvals of transfers of healthcare properties;
- the effect of increasing healthcare regulation and enforcement on our tenants and the dependence of our tenants on reimbursement from governmental and other third-party payors;
- the relatively illiquid nature of real estate investments;
- competitive conditions in our industry;
- the loss of key management personnel or other employees;
- the impact of litigation and rising insurance costs on the business of our tenants;
- the effect of our tenants declaring bankruptcy or becoming insolvent;
- uninsured or underinsured losses affecting our properties and the possibility of environmental compliance costs and liabilities;
- the ownership limits and anti-takeover defenses in our governing documents and Maryland law, which may restrict change of control or business combination opportunities;
- the impact of a failure or security breach of information technology in our operations;
- our ability to find replacement tenants and the impact of unforeseen costs in acquiring new properties;
- our ability to maintain our status as a real estate investment trust (“REIT”); and
- compliance with REIT requirements and certain tax and tax regulatory matters related to our status as a REIT.

We urge you to carefully consider these risks and review the additional disclosures we make concerning risks and other factors that may materially affect the outcome of our forward-looking statements and our future business and operating results, including those made in Part I, Item 1A, “Risk Factors” of our Annual Report on Form 10-K for the year ended December 31, 2015 (our “2015 Annual Report on Form 10-K”), as such risk factors may be amended, supplemented or superseded from time to time by other reports we file with the Securities and Exchange Commission (the “SEC”), including subsequent Annual Reports on Form 10-K and Quarterly Reports on Form 10-Q. We caution you that any forward-looking statements made in this 10-Q are not guarantees of future performance, events or results, and you should not place undue reliance on these forward-looking statements, which speak only as of the date of this

report. We do not intend, and we undertake no obligation, to update any forward-looking information to reflect events or circumstances after the date of this 10-Q or to reflect the occurrence of unanticipated events, unless required by law to do so.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS
SABRA HEALTH CARE REIT, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(dollars in thousands, except per share data)

	September 30, 2016 (unaudited)	December 31, 2015
Assets		
Real estate investments, net of accumulated depreciation of $272,953 and $237,841 as of September 30, 2016 and December 31, 2015, respectively	$ 1,999,778	$ 2,039,616
Loans receivable and other investments, net	94,466	300,177
Cash and cash equivalents	19,674	7,434
Restricted cash	9,150	9,813
Prepaid expenses, deferred financing costs and other assets, net	116,353	111,797
Total assets	$ 2,239,421	$ 2,468,837
Liabilities		
Mortgage notes, net	$ 162,130	$ 174,846
Revolving credit facility	—	255,000
Term loans, net	337,641	264,229
Senior unsecured notes, net	687,607	685,704
Accounts payable and accrued liabilities	38,156	35,182
Total liabilities	1,225,534	1,414,961
Commitments and contingencies (Note 14)		
Equity		
Preferred stock, $.01 par value; 10,000,000 shares authorized, 5,750,000 shares issued and outstanding as of September 30, 2016 and December 31, 2015	58	58
Common stock, $.01 par value; 125,000,000 shares authorized, 65,259,836 and 65,182,335 shares issued and outstanding as of September 30, 2016 and December 31, 2015, respectively	653	652
Additional paid-in capital	1,207,487	1,202,541
Cumulative distributions in excess of net income	(184,969)	(142,148)
Accumulated other comprehensive loss	(9,382)	(7,333)
Total Sabra Health Care REIT, Inc. stockholders' equity	1,013,847	1,053,770
Noncontrolling interests	40	106
Total equity	1,013,887	1,053,876
Total liabilities and equity	$ 2,239,421	$ 2,468,837

See accompanying notes to condensed consolidated financial statements.

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SABRA HEALTH CARE REIT, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(dollars in thousands, except per share data)
(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Revenues:				
Rental income	$56,833	$ 53,173	$167,442	$152,574
Interest and other income	3,157	6,211	25,482	17,594
Resident fees and services	1,937	550	5,811	1,924
Total revenues	61,927	59,934	198,735	172,092
Expenses:				
Depreciation and amortization	17,102	16,306	51,273	44,953
Interest	15,794	15,176	49,139	43,108
Operating expenses	1,404	444	4,256	1,442
General and administrative	6,171	3,547	15,521	19,270
Provision for doubtful accounts and loan losses	540	2,489	3,286	6,605
Impairment of real estate	—	—	29,811	—
Total expenses	41,011	37,962	153,286	115,378
Other income (expense):				
Loss on extinguishment of debt	—	—	(556)	—
Other income (expense)	2,945	(100)	5,345	(300)
Net gain (loss) on sale of real estate	1,451	(3,838)	(3,203)	(2,115)
Total other income (expense)	4,396	(3,938)	1,586	(2,415)
Net income	25,312	18,034	47,035	54,299
Net loss attributable to noncontrolling interests	25	27	66	47
Net income attributable to Sabra Health Care REIT, Inc.	25,337	18,061	47,101	54,346
Preferred stock dividends	(2,561)	(2,561)	(7,682)	(7,682)
Net income attributable to common stockholders	$22,776	$ 15,500	$39,419	$46,664
Net income attributable to common stockholders, per:				
Basic common share	$0.35	$ 0.24	$0.60	$0.76
Diluted common share	$0.35	$ 0.24	$0.60	$0.76
Weighted-average number of common shares outstanding, basic	65,312,288	65,160,290	65,285,591	61,244,991

Weighted-average number of common shares outstanding, diluted	65,591,428	65,398,175	65,470,589	61,468,603

See accompanying notes to condensed consolidated financial statements.

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SABRA HEALTH CARE REIT, INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(in thousands)
(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Net income	$25,312	$18,034	$47,035	$54,299
Other comprehensive (loss) income:				
Foreign currency translation (loss) income	(500)	970	(749)	375
Unrealized gain (loss) on cash flow hedges	398	(1,781)	(1,300)	(4,470)
Total other comprehensive loss	(102)	(811)	(2,049)	(4,095)
Comprehensive income	25,210	17,223	44,986	50,204
Comprehensive loss attributable to noncontrolling interest	25	27	66	47
Comprehensive income attributable to Sabra Health Care REIT, Inc.	$25,235	$17,250	$45,052	$50,251

See accompanying notes to condensed consolidated financial statements.

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SABRA HEALTH CARE REIT, INC.
CONDENSED CONSOLIDATED STATEMENTS OF EQUITY
(dollars in thousands, except per share data)
(unaudited)

	Preferred Stock		Common Stock		Additional Paid-in Capital	Cumulative Distributions in Excess of Net Income	Accumulated Other Comprehensive Loss	Total Stockholders' Equity	Noncontrolling Interests	Total Equity
	Shares	Amounts	Shares	Amounts						
Balance, December 31, 2014	5,750,000	$58	59,047,001	$590	$1,053,601	$(110,841)	$(1,542)	$941,866	$(43)	$941,823
Net income (loss)	—	—	—	—	—	54,346	—	54,346	(47)	54,299
Other comprehensive loss	—	—	—	—	—	—	(4,095)	(4,095)	—	(4,095)
Amortization of stock-based compensation	—	—	—	—	5,872	—	—	5,872	—	5,872
Common stock issuance, net	—	—	6,087,055	61	142,386	—	—	142,447	—	142,447
Preferred dividends	—	—	—	—	—	(7,682)	—	(7,682)	—	(7,682)
Common dividends ($1.19 per share)	—	—	—	—	—	(73,420)	—	(73,420)	—	(73,420)
Balance, September 30, 2015	5,750,000	$58	65,134,056	$651	$1,201,859	$(137,597)	$(5,637)	$1,059,334	$(90)	$1,059,244

	Preferred Stock		Common Stock		Additional Paid-in Capital	Cumulative Distributions in Excess of Net Income	Accumulated Other Comprehensive Loss	Total Stockholders' Equity	Noncontrolling Interests	Total Equity
	Shares	Amounts	Shares	Amounts						
Balance, December 31, 2015	5,750,000	$58	65,182,335	$652	$1,202,541	$(142,148)	$(7,333)	$1,053,770	$106	$1,053,876
Net income (loss)	—	—	—	—	—	47,101	—	47,101	(66)	47,035
Other comprehensive loss	—	—	—	—	—	—	(2,049)	(2,049)	—	(2,049)
Amortization of stock-based compensation	—	—	—	—	6,775	—	—	6,775	—	6,775

Common stock issuance, net	—	—	108,731	1	(1,104)	—	—	(1,103)	—	(1,103)
Repurchase of common stock	—	—	(31,230)	—	(725)	—	—	(725)	—	(725)
Preferred dividends	—	—	—	—	—	(7,682)	—	(7,682)	—	(7,682)
Common dividends ($1.25 per share)	—	—	—	—	—	(82,240)	—	(82,240)	—	(82,240)
Balance, September 30, 2016	5,750,000	$58	65,259,836	$653	$1,207,487	$(184,969)	$(9,382)	$1,013,847	$40	$1,013,887

See accompanying notes to condensed consolidated financial statements.

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SABRA HEALTH CARE REIT, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(unaudited)

	Nine Months Ended September 30,					
	2016			2015		
Cash flows from operating activities:						
Net income	$	47,035		$	54,299	
Adjustments to reconcile net income to net cash provided by operating activities:						
Depreciation and amortization	51,273			44,953		
Non-cash interest income adjustments	549			343		
Amortization of deferred financing costs	3,767			3,829		
Stock-based compensation expense	6,137			5,389		
Amortization of debt discount	81			77		
Loss on extinguishment of debt	556			—		
Straight-line rental income adjustments	(16,710		)	(18,272		)
Provision for doubtful accounts and loan losses	3,286			6,605		
Change in fair value of contingent consideration	50			300		
Net loss on sales of real estate	3,203			2,115		
Impairment of real estate	29,811			—		
Changes in operating assets and liabilities:						
Prepaid expenses and other assets	1,381			(15,035		)
Accounts payable and accrued liabilities	6,217			(2,410		)
Restricted cash	(2,820		)	(3,078		)
Net cash provided by operating activities	133,816			79,115		
Cash flows from investing activities:						
Acquisitions of real estate	(109,619		)	(386,572		)

Origination and fundings of loans receivable	(9,478	)	(26,207	)
Origination and fundings of preferred equity investments	(6,845	)	(9,281	)
Additions to real estate	(901	)	(1,596	)
DIP loan fundings	—		(3,302	)
Repayment of loans receivable	214,947		3,285	
Release of contingent consideration held in escrow	—		5,240	
Net proceeds from the sale of real estate	85,449		15,752	
Net cash provided by (used in) investing activities	173,553		(402,681	)
Cash flows from financing activities:				
Net (repayments of) proceeds from revolving credit facility	(255,000	)	136,000	
Proceeds from term loans	69,360		73,242	
Proceeds from mortgage notes	—		28,735	
Principal payments on mortgage notes	(13,756	)	(2,184	)
Payments of deferred financing costs	(5,933	)	(1,314	)
Issuance of common stock, net	(1,289	)	139,617	
Dividends paid on common and preferred stock	(89,283	)	(80,619	)
Net cash (used in) provided by financing activities	(295,901	)	293,477	
Net increase (decrease) in cash and cash equivalents	11,468		(30,089	)
Effect of foreign currency translation on cash and cash equivalents	772		(231	)
Cash and cash equivalents, beginning	7,434		61,793	

of period				
Cash and cash equivalents, end of period	$	19,674	$	31,473
Supplemental disclosure of cash flow information:				
Interest paid	$	49,009	$	43,405
Supplemental disclosure of non-cash investing and financing activities:				
Assumption of mortgage indebtedness	$	—	$	19,677
Real estate acquired through loan receivable foreclosure	$	10,100	$	—

See accompanying notes to condensed consolidated financial statements.

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SABRA HEALTH CARE REIT, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. BUSINESS

Overview

Sabra Health Care REIT, Inc. (“Sabra” or the “Company”) was incorporated on May 10, 2010 as a wholly owned subsidiary of Sun Healthcare Group, Inc. (“Sun”) and commenced operations on November 15, 2010 following Sabra's separation from Sun (the "Separation Date"). Sabra elected to be treated as a real estate investment trust (“REIT”) with the filing of its U.S. federal income tax return for the taxable year beginning January 1, 2011. Sabra believes that it has been organized and operated, and it intends to continue to operate, in a manner to qualify as a REIT. Sabra’s primary business consists of acquiring, financing and owning real estate property to be leased to third party tenants in the healthcare sector. Sabra primarily generates revenues by leasing properties to tenants and operators throughout the United States and Canada. Sabra owns substantially all of its assets and properties and conducts its operations through Sabra Health Care Limited Partnership, a Delaware limited partnership (the “Operating Partnership”), of which Sabra is the sole general partner and Sabra's wholly owned subsidiaries are currently the only limited partners, or by subsidiaries of the Operating Partnership. The Company’s investment portfolio is primarily comprised of skilled nursing/transitional care facilities, senior housing facilities, an acute care hospital, investments in loans receivable and preferred equity investments.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation and Basis of Presentation

The accompanying condensed consolidated financial statements include the accounts of Sabra and its wholly owned subsidiaries as of September 30, 2016 and December 31, 2015 and for the periods ended September 30, 2016 and 2015. All significant intercompany transactions and balances have been eliminated in consolidation.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) for interim financial information as contained within the Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) and the rules and regulations of the Securities and Exchange Commission (the “SEC”), including the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, the unaudited condensed consolidated financial statements do not include all of the information and footnotes required by GAAP for financial statements. In the opinion of management, the financial statements for the unaudited interim periods presented include all adjustments, which are of a normal and recurring nature, necessary for a fair statement of the results for such periods. Operating results for the three and nine months ended September 30, 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016. For further information, refer to the Company’s consolidated financial statements and notes thereto for the year ended December 31, 2015 included in the Company’s 2015 Annual Report on Form 10-K filed with the SEC.

GAAP requires the Company to identify entities for which control is achieved through voting rights or other means and to determine which business enterprise is the primary beneficiary of variable interest entities (“VIEs”). A VIE is broadly defined as an entity with one or more of the following characteristics: (a) the total equity investment at risk is insufficient to finance the entity's activities without additional subordinated financial support; (b) as a group, the holders of the equity investment at risk lack (i) the ability to make decisions about the entity's activities through voting or similar rights, (ii) the obligation to absorb the expected losses of the entity, or (iii) the right to receive the expected residual returns of the entity; or (c) the equity investors have voting rights that are not proportional to their economic interests, and substantially all of the entity's activities either involve, or are conducted on behalf of, an investor that has disproportionately few voting rights. If the Company were determined to be the primary beneficiary of the VIE, the Company would consolidate investments in the VIE. The Company may change its original assessment of a VIE due to events such as modifications of contractual arrangements that affect the characteristics or adequacy of the entity's equity investments at risk and the disposal of all or a portion of an interest held by the primary beneficiary.

The Company identifies the primary beneficiary of a VIE as the enterprise that has both: (i) the power to direct the activities of the VIE that most significantly impact the entity's economic performance; and (ii) the obligation to absorb losses or the right to receive benefits of the VIE that could be significant to the entity. The Company performs this analysis on an ongoing basis.

As of September 30, 2016, the Company determined it was the primary beneficiary of two senior housing facilities and

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has consolidated the operations of these facilities in the accompanying condensed consolidated financial statements. As of September 30, 2016, the Company determined that operations of these facilities were not material to the Company's results of operations, financial condition or cash flows.

As it relates to investments in loans, in addition to the Company's assessment of VIEs and whether the Company is the primary beneficiary of those VIEs, the Company evaluates the loan terms and other pertinent facts to determine if the loan investment should be accounted for as a loan or as a real estate joint venture. If an investment has the characteristics of a real estate joint venture, including if the Company participates in the majority of the borrower's expected residual profit, the Company would account for the investment as an investment in a real estate joint venture and not as a loan investment. Expected residual profit is defined as the amount of profit, whether called interest or another name, such as an equity kicker, above a reasonable amount of interest and fees expected to be earned by a lender. At September 30, 2016, none of the Company's investments in loans are accounted for as real estate joint ventures.

As it relates to investments in joint ventures, the Company assesses any limited partners' rights and their impact on the presumption of control of the limited partnership by any single partner. The Company reassesses its determination of which entity controls the joint venture if: there is a change to the terms or in the exercisability of the rights of any partners, the sole general partner increases or decreases its ownership of limited partnership interests, or there is an increase or decrease in the number of outstanding limited partnership interests. The Company also applies this guidance to managing member interests in limited liability companies.

Use of Estimates

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

Reclassifications

Certain amounts in the Company's condensed consolidated financial statements for prior periods have been reclassified to conform to the current period presentation. These reclassifications have not changed the results of operations of prior periods. As a result, certain reclassifications were made to the condensed consolidated balance sheets and condensed consolidated statements of income. As of December 31, 2015, there was $17.3 million of deferred financing costs related to the Company's mortgage notes, term loans and senior unsecured notes that were previously reported within "prepaid expenses, deferred financing costs and other assets, net" that were reclassified in accordance with ASU 2015-03 to their respective debt liability financial statement line items on the Company's condensed consolidated balance sheet.

Recently Issued Accounting Standards Update

In January 2016, the FASB issued ASU 2016-01, Financial Instruments–Overall (Subtopic 825-10) ("ASU 2016-01"). ASU 2016-01 updates guidance related to recognition and measurement of financial assets and financial liabilities. ASU 2016-01 requires all equity investments to be measured at fair value with changes in the fair value recognized through net income (other than those accounted for under the equity method of accounting or those that result in consolidation of the investee). The amendments in ASU 2016-01 also require an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. In addition, the amendments in ASU 2016-01 eliminate the requirement to disclose the methods and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet for public business entities. ASU 2016-01 is effective for fiscal years and interim periods within those years beginning after December 15, 2017, with early adoption permitted. The Company is currently evaluating the impact this guidance will have on its consolidated financial statements when adopted.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842) ("ASU 2016-02"). ASU 2016-02 supersedes guidance related to accounting for leases. ASU 2016-02 updates guidance around the recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases under previous GAAP. The objective of ASU 2016-02 is to establish the principles that lessees and lessors shall apply to report useful information to users of

financial statements about the amount, timing, and uncertainty of cash flows arising from a lease. ASU 2016-02 does not fundamentally change lessor accounting, however, some changes have been made to lessor accounting to conform and align that guidance with the lessee guidance and other areas within GAAP. ASU 2016-02 is effective for fiscal years and interim periods within those years beginning after December 15, 2018, with early adoption permitted. The Company is currently evaluating the impact this guidance will have on its consolidated financial statements when adopted.

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In March 2016, the FASB issued ASU 2016-07, Equity Method and Joint Ventures (Topic 323) (“ASU 2016-07”). ASU 2016-07 simplifies the accounting for equity method investments. ASU 2016-07 eliminates the requirement in Topic 323 that an entity retroactively adopt the equity method of accounting if an investment qualifies for use of the equity method as a result of an increase in the level of ownership or degree of influence. The amendments require that the equity method investor add the cost of acquiring the additional interest in the investee to the current basis of the investor’s previously held interest and adopt the equity method of accounting as of the date the investment becomes qualified for equity method accounting. ASU 2016-07 is effective for fiscal years and interim periods within those years beginning after December 15, 2016, with early adoption permitted. The Company is currently evaluating the impact this guidance will have on its consolidated financial statements when adopted.

In March 2016, the FASB issued ASU 2016-09, Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting (“ASU 2016-09”). ASU 2016-09 simplifies several aspects of the accounting for employee share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. In addition, the amendments in ASU 2016-09 eliminate the guidance in Topic 718 that was indefinitely deferred shortly after the issuance of FASB Statement No. 123 (revised 2004), Share-Based Payment. ASU 2016-09 is effective for fiscal years and interim periods within those years beginning after December 15, 2016, with early adoption permitted. The Company is currently evaluating the impact this guidance will have on its consolidated financial statements when adopted.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments (“ASU 2016-13”). ASU 2016-13 requires that a financial asset (or a group of financial assets) measured at amortized cost basis be presented at the net amount expected to be collected. The allowance for credit losses is a valuation account that is deducted from the amortized cost basis of the financial asset(s) to present the net carrying value at the amount expected to be collected on the financial asset. The amendments in ASU 2016-13 are an improvement because they eliminate the probable initial recognition threshold in current GAAP and, instead, reflect an entity’s current estimate of all expected credit losses. Previously, when credit losses were measured under GAAP, an entity generally only considered past events and current conditions in measuring the incurred loss. ASU 2016-13 is effective for fiscal years and interim periods within those years beginning after December 15, 2019, with early adoption permitted as of the fiscal years beginning after December 15, 2018. An entity will apply the amendments in this update through a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective (that is, a modified-retrospective approach). The Company is currently evaluating the impact this guidance will have on its consolidated financial statements when adopted.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (“ASU 2016-15”). ASU 2016-15 provides specific guidance on the following eight specific cash flow classification issues: debt prepayment or debt extinguishment costs; settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing; contingent consideration payments made after a business combination; proceeds from the settlement of insurance claims; proceeds from the settlement of corporate-owned life insurance policies (including bank-owned life insurance policies); distributions received from equity method investees; beneficial interests in securitization transactions; and separately identifiable cash flows and application of the predominance principle. ASU 2016-15 will reduce the current and potential future diversity in practice of cash flow classifications. ASU 2016-15 is effective for fiscal years and interim periods within those years beginning after December 15, 2017, with early adoption permitted. The Company is currently evaluating the impact this guidance will have on its consolidated financial statements when adopted.

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3. RECENT REAL ESTATE ACQUISITIONS

During the nine months ended September 30, 2016, the Company acquired one skilled nursing/transitional care facility and three senior housing facilities. During the nine months ended September 30, 2015, the Company acquired three skilled nursing/transitional care facilities and 19 senior housing facilities. The consideration was allocated as follows (in thousands):

	Nine Months Ended September 30,	
	2016	2015
Land	$5,521	$26,855
Building and Improvements	102,094	372,031
Tenant Origination and Absorption Costs	1,565	5,481
Tenant Relationship	439	1,881
Total Consideration	$109,619	$406,248

As of September 30, 2016, the purchase price allocation for one senior housing facility acquired during the nine months ended September 30, 2016 is preliminary pending the receipt of information necessary to complete the valuation of certain tangible and intangible assets and liabilities and therefore is subject to change.
The tenant origination and absorption costs intangible assets and tenant relationship intangible assets acquired in connection with these acquisitions have weighted-average amortization periods as of the respective date of acquisition of 15 years and 25 years, respectively.
For the three and nine months ended September 30, 2016, the Company recognized $1.7 million of total revenues and $0.1 million of net income attributable to common stockholders from properties acquired during the nine months ended September 30, 2016. These amounts include acquisition pursuit costs of $1.1 million.

4. REAL ESTATE PROPERTIES HELD FOR INVESTMENT
The Company’s real estate properties held for investment consisted of the following (dollars in thousands):
As of September 30, 2016

Property Type	Number of Properties	Number of Beds/Units	Total Real Estate at Cost	Accumulated Depreciation	Total Real Estate Investments, Net
Skilled Nursing/Transitional Care	102	11,503	$1,083,054	$(194,853)	$888,201
Senior Housing	79	7,059	1,127,631	(67,924)	1,059,707
Acute Care Hospital	1	70	61,640	(9,926)	51,714
	182	18,632	2,272,325	(272,703)	1,999,622
Corporate Level			406	(250)	156
			$2,272,731	$(272,953)	$1,999,778

As of December 31, 2015

Property Type	Number of Properties	Number of Beds/Units	Total Real Estate at Cost	Accumulated Depreciation	Total Real Estate Investments, Net
Skilled Nursing/Transitional Care	103	11,515	$1,051,189	$(174,662)	$876,527
Senior Housing	75	6,710	1,050,162	(45,800)	1,004,362
Acute Care Hospitals	2	124	175,807	(17,127)	158,680
	180	18,349	2,277,158	(237,589)	2,039,569
Corporate Level			299	(252)	47

	$2,277,457	$(237,841)	$2,039,616

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	September 30, 2016	December 31, 2015
Building and improvements	$ 1,962,520	$ 1,954,129
Furniture and equipment	85,423	97,840
Land improvements	3,888	3,594
Land	220,900	221,894
	2,272,731	2,277,457
Accumulated depreciation	(272,953)	(237,841)
	$ 1,999,778	$ 2,039,616

Contingent Consideration Arrangements

In connection with four of its real estate acquisitions, the Company entered into contingent consideration arrangements. Under the contingent consideration arrangements, the Company may pay out additional amounts based on incremental value created through the improvement of operations of the acquired facility (a contingent consideration liability) or may be entitled to receive a portion of the original purchase price of the acquired facility if the facility does not meet certain performance hurdles (a contingent consideration asset). The estimated value of the contingent consideration liabilities at the time of purchase was $3.2 million. The estimated value of the contingent consideration asset at the time of purchase was $0. The contingent consideration amounts would be determined based on portfolio performance and the tenant achieving certain performance hurdles during 2016 through 2018. To determine the value of the contingent consideration, the Company used significant inputs not observable in the market to estimate the contingent consideration, made assumptions regarding the probability of the portfolio achieving the incremental value and then applied an appropriate discount rate. As of September 30, 2016, based on the potential future performance of these facilities, the contingent consideration liabilities had an estimated value of $2.4 million, which amount is included in accounts payable in the accompanying condensed consolidated balance sheet, and the contingent consideration asset had an estimated value of $0. During the three and nine months ended September 30, 2016, the Company recorded an adjustment to increase the contingent consideration arrangements by $0.1 million and included this amount in other income (expense) on the accompanying condensed consolidated statements of income.

Operating Leases

As of September 30, 2016, all of the Company’s real estate properties were leased under triple-net operating leases with expirations ranging from one to 16 years. As of September 30, 2016, the leases had a weighted-average remaining term of 9 years. The leases include provisions to extend the lease terms and other negotiated terms and conditions. The Company, through its subsidiaries, retains substantially all of the risks and benefits of ownership of the real estate assets leased to the tenants. In addition, the Company may receive additional security under these operating leases in the form of letters of credit and security deposits from the lessee or guarantees from the parent of the lessee. Security deposits received in cash related to tenant leases are included in accounts payable and accrued liabilities in the accompanying condensed consolidated balance sheets and totaled $2.1 million as of September 30, 2016 and $1.3 million as of December 31, 2015. As of September 30, 2016, the Company had a $3.2 million reserve for unpaid cash rents and a $1.4 million reserve associated with accumulated straight-line rental income. As of December 31, 2015, the Company had a $3.5 million reserve for unpaid cash rents and a $5.3 million reserve associated with accumulated straight-line rental income. As of September 30, 2016, the Company's three largest tenants, Genesis, Holiday and NMS Healthcare, represented 32.6%, 16.3% and 12.4%, respectively, of the Company's annualized revenues. Other than these three tenants, none of the Company’s tenants individually represented 10% or more of the Company’s annualized revenues as of September 30, 2016.

The Company has entered into memoranda of understanding with Genesis to jointly market for sale 35 skilled nursing facilities and make certain other lease and corporate guarantee amendments for the remaining 43 facilities leased to Genesis. Marketing of these 35 facilities is ongoing and is expected to be completed over the next several quarters.

The Company monitors the creditworthiness of its tenants by reviewing credit ratings (if available) and evaluating the ability of the tenants to meet their lease obligations to the Company based on the tenants’ financial performance, including the evaluation of any parent guarantees (or the guarantees of other related parties) of tenant lease obligations. Because formal credit ratings may not be available for most of the Company’s tenants, the primary basis

for the Company’s evaluation of the credit quality of its tenants (and more specifically the tenants’ ability to pay their rent obligations to the Company) is the tenants’ lease coverage ratios. These coverage ratios include earnings before interest, taxes, depreciation, amortization and rent (“EBITDAR”) to rent and earnings before interest, taxes, depreciation, amortization, rent and management fees (“EBITDARM”) to rent at the lease level and consolidated EBITDAR to total fixed charges at the parent guarantor level when such a guarantee exists. The Company obtains various financial and operational information from its tenants each month and reviews this information in conjunction with the above-described coverage metrics to identify financial and operational trends, evaluate the impact of the industry's operational and financial environment (including the impact of government

reimbursement), and evaluate the management of the tenant's operations. These metrics help the Company identify potential areas of concern relative to its tenants' credit quality and ultimately the tenants' ability to generate sufficient liquidity to meet its obligations, including its obligation to continue to pay the rent due to the Company.

As of September 30, 2016, the future minimum rental payments from the Company's properties held for investment under non-cancelable operating leases was as follows (in thousands):

October 1, 2016 through December 31, 2016	$52,272
2017	212,373
2018	217,914
2019	224,207
2020	230,351
Thereafter	1,306,497
	$2,243,614

5. DISPOSITIONS

2016 Dispositions

During the nine months ended September 30, 2016, the Company completed the sale of two skilled nursing/transitional care facilities and one acute care hospital for aggregate consideration of $85.4 million after selling expenses of $2.3 million. The net carrying value of the assets and liabilities of these facilities, after the impairment loss of $29.8 million recognized in relation to the acute care hospital, was $88.6 million, resulting in an aggregate $3.2 million loss on sale.

Excluding the net loss on sale and real estate impairment, the Company recognized $0.8 million and $3.1 million of net loss from these facilities during the nine months ended September 30, 2016 and 2015, respectively. The sale of these facilities does not represent a strategic shift that has and is not expected to have a major effect on the Company's operations and financial results and therefore the results of operations attributable to these facilities have remained in continuing operations.

2015 Dispositions

During the nine months ended September 30, 2015, the Company completed the sale of three skilled nursing/transitional care facilities and one senior housing facility for aggregate consideration of $16.3 million. The carrying value of the assets and liabilities of these facilities was $18.4 million, which resulted in an aggregate $2.1 million loss on sale.

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6. LOANS RECEIVABLE AND OTHER INVESTMENTS

As of September 30, 2016 and December 31, 2015, the Company’s loans receivable and other investments consisted of the following (dollars in thousands):

Investment	Quantity	Facility Type	Principal Balance as of September 30, 2016 [1]	Book Value as of September 30, 2016	Book Value as of December 31, 2015	September 30, 2016 Weighted Average Contractual Interest Rate / Rate of Return	September 30, 2016 Weighted Average Annualized Effective Interest Rate / Rate of Return	Maturity Dates
Loans Receivable:								
Mortgage	5	Skilled Nursing / Senior Housing	$ 38,492	$ 38,534	$ 166,277	9.1 %	8.9 %	11/07/16-3/31/21
Construction	1	Senior Housing	590	637	75,201	8.0 %	7.7 %	3/31/21
Mezzanine	1	Senior Housing	9,640	9,660	15,613	11.0 %	10.8 %	08/31/17
Pre-development	3	Senior Housing	3,926	3,959	3,768	9.0 %	7.6 %	1/28/17 - 9/09/17
Debtor-in-possession	1	Acute Care Hospital	1,823	1,823	13,625	5.0 %	5.0 %	NA
	11		54,471	54,613	274,484	9.3 %	9.1 %	
Loan loss reserve			—	(3,120)	(4,300)			
			$ 54,471	$ 51,493	$ 270,184			
Other Investments:								
Preferred Equity	11	Skilled Nursing / Senior Housing	42,594	42,973	29,993	12.9 %	12.9 %	N/A
Total	22		$ 97,065	$ 94,466	$ 300,177	10.9 %	10.8 %	

[1] Principal balance includes amounts funded and accrued but unpaid interest / preferred return and excludes capitalizable fees.

During the nine months ended September 30, 2016, the Company received aggregate proceeds of $196.1 million, consisting of outstanding principal balance of $170.8 million and $25.3 million of accrued and unpaid interest and fees, in final repayments of the Forest Park - Fort Worth construction loan and the Forest Park - Dallas mortgage loan. As of September 30, 2016, the Company considered three loan receivable investments to be impaired. The principal balances of the impaired loans were $18.4 million and $30.0 million as of September 30, 2016 and December 31, 2015, respectively. The Company recorded a provision for loan losses related to these loans of $0.2 million and $3.5 million during the three and nine months ended September 30, 2016, respectively. As of September 30, 2016, these three loan receivable investments were on nonaccrual status. During the three and nine months ended September 30, 2016, the Company increased its provision for portfolio-based loan losses by $50,000 and decreased it by $1.4 million, respectively. The Company's specific loan loss reserve and portfolio-based loan loss reserve were $2.7 million and $0.4 million, respectively, as of September 30, 2016. The Company did not record any specific loan loss reserve or portfolio-based loan loss reserve during the three and nine months ended September 30, 2015.

7. DEBT

Mortgage Indebtedness

The Company’s mortgage notes payable consist of the following (dollars in thousands):

Interest Rate Type	Principal Balance as of September 30, 2016 [1]	Principal Balance as of December 31, 2015 [1]	Weighted Average Effective Interest Rate at September 30, 2016 [2]	Maturity Date
Fixed Rate	$ 165,045	$ 177,850	3.86 %	December 2021 - August 2051

[1] Principal balance does not include deferred financing costs of $2.9 million and $3.0 million as of September 30, 2016 and December 31, 2015, respectively.
[2] Weighted average effective interest rate includes private mortgage insurance.

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Mortgage Debt Repayment. In August 2016, the Company repaid a $10.7 million fixed rate mortgage note having an interest rate of 5.60%.

Senior Unsecured Notes

The Company's senior unsecured notes consist of the following (dollars in thousands):

Title	Maturity Date	Principal Balance as of September 30, 2016 [(1)]	Principal Balance as of December 31, 2015 [(1)]
5.5% senior unsecured notes due 2021 ("2021 Notes")	February 1, 2021	$500,000	$500,000
5.375% senior unsecured notes due 2023 ("2023 Notes")	June 1, 2023	200,000	200,000
		$700,000	$700,000

(1) Principal balance does not include discount of $0.5 million and $0.6 million as of September 30, 2016 and December 31, 2015, respectively, and also excludes deferred financing costs of $11.9 million and $13.7 million as of September 30, 2016 and December 31, 2015, respectively.

The 2021 Notes and the 2023 Notes (collectively, the "Senior Notes") were issued by the Operating Partnership and Sabra Capital Corporation, wholly owned subsidiaries of the Company (the "Issuers"). The 2021 Notes accrue interest at a rate of 5.5% per annum payable semiannually on February 1 and August 1 of each year and the 2023 Notes accrue interest at a rate of 5.375% per annum payable semiannually on June 1 and December 1 of each year.

The obligations under the Senior Notes are fully and unconditionally guaranteed, jointly and severally, on an unsecured basis, by Sabra and certain of Sabra's other existing and, subject to certain exceptions, future material subsidiaries; provided, however, that such guarantees are subject to release under certain customary circumstances. See Note 12, "Summarized Condensed Consolidating Information" for additional information concerning the circumstances pursuant to which the guarantors will be automatically and unconditionally released from their obligations under the guarantees.

The indentures governing the Senior Notes (the "Senior Notes Indentures") include customary events of default and require us to comply with specified restrictive covenants. As of September 30, 2016, the Company was in compliance with all applicable financial covenants under the Senior Notes Indentures.

Revolving Credit Facility and Term Loans

On September 10, 2014, the Operating Partnership entered into an unsecured revolving credit facility (the "Prior Revolving Credit Facility") that provided for a borrowing capacity of $650.0 million and provided an accordion feature allowing for an additional $100.0 million of capacity, subject to terms and conditions. On October 10, 2014, the Operating Partnership converted $200.0 million of the outstanding borrowings under the Prior Revolving Credit Facility to a term loan. Concurrent with the term loan conversion, the Company entered into a five-year interest rate cap contract that caps LIBOR at 2.0%.

Borrowings under the Prior Revolving Credit Facility bore interest on the outstanding principal amount at a rate equal to an applicable percentage plus, at the Operating Partnership's option, either (a) LIBOR or (b) a base rate determined as the greater of (i) the federal funds rate plus 0.5%, (ii) the prime rate, and (iii) one-month LIBOR plus 1.0% (referred to as the "Base Rate"). The applicable percentage for borrowings varied based on the Consolidated Leverage Ratio, as defined in the credit agreement for the Prior Revolving Credit Facility, and ranged from 2.00% to 2.60% per annum for LIBOR based borrowings and 1.00% to 1.60% per annum for borrowings at the Base Rate. In addition, the Operating Partnership was required to pay an unused fee to the lenders equal to 0.25% or 0.35% per annum based on the amount of unused borrowings under the Prior Revolving Credit Facility.

On June 10, 2015, Sabra Canadian Holdings, LLC, a wholly-owned subsidiary of the Company, entered into a new Canadian dollar denominated term loan of CAD $90.0 million (U.S. $73.2 million) (the "Prior Canadian Term Loan") that bore a variable interest rate of the Canadian Dollar Offer Rate (“CDOR”) plus 2.00%-2.60% depending on the Company's consolidated leverage ratio.
On January 14, 2016, the Operating Partnership and Sabra Canadian Holdings, LLC (together, the “Borrowers”), entered into a third amended and restated unsecured credit facility (the “Credit Facility”). The Credit Facility amends and restates the Prior Revolving Credit Facility and replaces the Prior Canadian Term Loan.

The Credit Facility includes a revolving credit facility (the “Revolving Credit Facility”) and U.S. dollar and Canadian dollar term loans (collectively, the “Term Loans”). The Revolving Credit Facility provides for a borrowing capacity of $500.0

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million and, in addition, increases the Company's U.S. dollar and Canadian dollar term loans to $245.0 million and CAD $125.0 million, respectively. Further, up to $125.0 million of the Revolving Credit Facility may be used for borrowings in certain foreign currencies. The Credit Facility also contains an accordion feature that can increase the total available borrowings to $1.25 billion, subject to terms and conditions. In addition, the Canadian dollar term loan was re-designated as a net investment hedge (see Note 8, “Derivative and Hedging Instruments” for further information).

The Revolving Credit Facility has a maturity date of January 14, 2020, and includes two six-month extension options. The Term Loans have a maturity date of January 14, 2021.

As of September 30, 2016, there were no amounts outstanding under the Revolving Credit Facility and $500.0 million available for borrowing.
Borrowings under the Revolving Credit Facility bear interest on the outstanding principal amount at a rate equal to an applicable percentage plus, at the Operating Partnership's option, either (a) LIBOR or (b) a base rate determined as the greater of (i) the federal funds rate plus 0.5%, (ii) the prime rate, and (iii) one-month LIBOR plus 1.0% (the "Base Rate"). The applicable percentage for borrowings will vary based on the Consolidated Leverage Ratio, as defined in the credit agreement, and will range from 1.80% to 2.40% per annum for LIBOR based borrowings and 0.80% to 1.40% per annum for borrowings at the Base Rate. As of September 30, 2016, the interest rate on the Revolving Credit Facility was 2.53%. In addition, the Operating Partnership pays an unused facility fee to the lenders equal to 0.25% or 0.30% per annum, which is determined by usage under the Revolving Credit Facility. During the three and nine months ended September 30, 2016, the Company incurred $23,000 and $2.3 million, respectively, in interest expense on amounts outstanding under the Revolving Credit Facility. During the three and nine months ended September 30, 2016, the Company incurred $0.4 million and $0.9 million, respectively, of unused facility fees.

The U.S. dollar term loan bears interest on the outstanding principal amount at a rate equal to an applicable percentage plus, at the Operating Partnership’s option, either (a) LIBOR or (b) the Base Rate. The applicable percentage for borrowings will vary based on the Consolidated Leverage Ratio, as defined in the credit agreement, and will range from 1.75% to 2.35% per annum for LIBOR based borrowings and 0.75% to 1.35% per annum for borrowings at the Base Rate. The Canadian dollar term loan bears interest on the outstanding principal amount at a rate equal to the Canadian Dollar Offer Rate (“CDOR”) plus 1.75% to 2.35% depending on the Consolidated Leverage Ratio.

On June 10, 2015, concurrently with entering into the Prior Canadian Term Loan, the Company entered into an interest rate swap agreement to fix the CDOR portion of the interest rate for this CAD $90.0 million term loan at 1.59%. In addition, the Prior Canadian Term Loan was designated as a net investment hedge (see Note 8, “Derivative and Hedging Instruments” for further information). On August 10, 2016, the Company entered into two interest rate swap agreements to fix the LIBOR portion of the interest rate for its $245.0 million U.S. dollar term loan at 0.90% and one interest rate swap agreement to fix the CDOR portion on CAD $35.0 million of its Canadian dollar term loan at 0.93%. In addition, the Company terminated the five-year interest rate cap contract that capped LIBOR at 2.0%.

In the event that Sabra achieves investment grade ratings from at least two of S&P, Moody’s and/or Fitch, the Operating Partnership can elect to reduce the applicable percentage for LIBOR or Base Rate borrowings. If the Operating Partnership makes this election, the applicable percentage for borrowings will vary based on the Debt Ratings at each Pricing Level, as defined in the credit agreement, and will range from 0.90% to 1.70% per annum for LIBOR based borrowings under the Revolving Credit Facility, 1.00% to 1.95% per annum for LIBOR or CDOR based borrowings under the Term Loans, 0.00% to 0.70% per annum for borrowings at the Base Rate under the Revolving Credit Facility, and 0.00% to 0.95% per annum for borrowings at the Base Rate under the U.S. dollar term loan. In addition, should the Operating Partnership elect this option, the unused fee will no longer apply and a facility fee ranging between 0.125% and 0.300% per annum will take effect based on the borrowing capacity regardless of amounts outstanding under the Revolving Credit Facility.
The obligations of the Borrowers under the Credit Facility are guaranteed by Sabra and certain subsidiaries of Sabra.

The Credit Facility contains customary covenants that include restrictions or limitations on the ability to make acquisitions and other investments, pay dividends, incur additional indebtedness, engage in non-healthcare related business activities, enter into transactions with affiliates and sell or otherwise transfer certain assets as well as customary events of default. The Credit Facility also requires Sabra, through the Operating Partnership, to comply with specified financial covenants, which include a maximum leverage ratio, a minimum fixed charge coverage ratio and a minimum tangible net worth requirement. As of September 30, 2016, the Company was in compliance with all applicable financial covenants under the Credit Facility.

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Interest Expense

During the three and nine months ended September 30, 2016, the Company incurred interest expense of $15.8 million and $49.1 million, respectively, and $15.2 million and $43.1 million during the three and nine months ended September 30, 2015, respectively. Interest expense includes financing costs amortization of $1.3 million and $3.8 million for the three and nine months ended September 30, 2016, respectively, and $1.3 million and $3.8 million for the three and nine months ended September 30, 2015, respectively. As of September 30, 2016 and December 31, 2015, the Company had $9.6 million and $13.3 million, respectively, of accrued interest included in accounts payable and accrued liabilities on the accompanying condensed consolidated balance sheets.

Maturities

The following is a schedule of maturities for the Company's outstanding debt as of September 30, 2016 (in thousands):

	Mortgage Indebtedness	Term Loans	Senior Notes	Total
October 1, 2016 through December 31, 2016	$ 1,013	$—	$—	$1,013
2017	4,139	—	—	4,139
2018	4,277	—	—	4,277
2019	4,420	—	—	4,420
2020	4,568	—	—	4,568
Thereafter	146,628	340,112	700,000	1,186,740
Total Principal Balance	165,045	340,112	700,000	1,205,157
Discount	—	—	(543)	(543)
Deferred financing costs	(2,915)	(2,471)	(11,850)	(17,236)
Total Debt, net	$ 162,130	$337,641	$687,607	$1,187,378

8. DERIVATIVE AND HEDGING INSTRUMENTS

The Company is exposed to various market risks, including the potential loss arising from adverse changes in interest rates and foreign exchange rates. The Company enters into derivative financial instruments to manage exposures that arise from business activities that result in the receipt or payment of future known and uncertain cash amounts, the value of which are determined by interest rates and foreign exchange rates. The Company's derivative financial instruments are used to manage differences in the amount of the Company's known or expected cash receipts and its known or expected cash payments principally related to the Company's investments and borrowings.

Certain of the Company's foreign operations expose the Company to fluctuations of foreign interest rates and exchange rates. These fluctuations may impact the value in the Company's functional currency, the U.S. dollar, of the Company's investment in foreign operations, the cash receipts and payments related to these foreign operations and payments of interest and principal under Canadian dollar denominated debt. The Company enters into derivative financial instruments to protect the value of its foreign investments and fix a portion of the interest payments for certain debt obligations. The Company does not enter into derivatives for speculative purposes.

Cash Flow Hedges

The Company's objectives in using interest rate derivatives are to add stability to interest expense and to manage its exposure to interest rate movements. To accomplish these objectives, the Company primarily uses interest rate swaps and caps as part of its interest rate risk management strategy. Approximately $3.6 million of losses, which are included in accumulated other comprehensive loss, as of September 30, 2016, are expected to be reclassified into earnings in the next 12 months. During the nine months ended September 30, 2016, the Company terminated its interest rate cap, generating cash proceeds of $0.3 million. The balance of the loss in other comprehensive income will be reclassified to earnings through 2019.

Net Investment Hedges

The Company is exposed to fluctuations in foreign exchange rates on investments it holds in Canada. The Company uses cross currency interest rate swaps to hedge its exposure to changes in foreign exchange rates on these foreign

investments.

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The following presents the notional amount of derivatives instruments as of the dates indicated (in thousands):

	September 30, 2016	December 31, 2015
Derivatives designated as cash flow hedges:		
Denominated in U.S. Dollars	$245,000	$200,000
Denominated in Canadian Dollars	$125,000	$90,000
Derivatives designated as net investment hedges:		
Denominated in Canadian Dollars	$56,300	$56,300
Financial instrument designated as net investment hedge:		
Denominated in Canadian Dollars	$125,000	$90,000

The following is a summary of the derivative and financial instruments designated as hedging instruments held by the Company at September 30, 2016 and December 31, 2015 (in thousands):

			September 30, 2016	December 31, 2015	Maturity Dates	
Type	Designation	Count	Fair Value			Balance Sheet Location
Assets:						
Interest rate cap	Cash Flow	—	$—	$ 1,695	2019	Prepaid expenses, deferred financing costs and other assets, net
Interest rate swap	Cash Flow	2	452	—	2021	Prepaid expenses, deferred financing costs and other assets, net
Cross currency interest rate swaps	Net Investment	2	3,173	5,392	2025	Prepaid expenses, deferred financing costs and other assets, net
			$3,625	$ 7,087		
Liabilities:						
Interest rate swap	Cash Flow	2	$1,724	$ 1,468	2020 - 2021	Accounts payable and accrued liabilities
CAD Term Loan	Net Investment	1	95,112	64,890	2020	Term loans, net
			$96,836	$ 66,358		

The following presents the effect of the Company's derivative financial instruments on the condensed consolidated statements of income and the condensed consolidated statements of equity for the three and nine months ended September 30, 2016:

	Gain (Loss) Recognized in Other Comprehensive Income (Effective Portion)				Income Statement Location
	Three Months Ended September 30,		Nine Months Ended September 30,		
	2016	2015	2016	2015	
Cash Flow Hedges:					
Interest Rate Products	$(40)	$(1,991)	$(2,019)	$(4,626)	Interest Expense

Net Investment Hedges:					
Foreign Currency Products	102	4,600	(2,118)	4,436	N/A
CAD Term Loan	1,363	(5,733)	(5,863)	(6,129)	N/A
	$1,425	$(3,124)	$(10,000)	$(6,319)	

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	Gain (Loss) Reclassified from Accumulated Other Comprehensive Income into Income (Effective Portion)				Income Statement Location
	Three Months Ended September 30,		Nine Months Ended September 30,		
	2016	2015	2016	2015	
Cash Flow Hedges:					
Interest Rate Products	$ (413)	$ (136)	$ (802)	$ (161)	Interest Expense
Net Investment Hedges:					
Foreign Currency Products	—	—	—	—	N/A
CAD Term Loan	—	—	—	—	N/A
	$ (413)	$ (136)	$ (802)	$ (161)	

During the three and nine months ended September 30, 2016, the Company determined that a portion of a cash flow hedge was ineffective and recognized $0.4 million of unrealized gains related to its interest rate swaps to other income (expense) in the condensed consolidated statements of income.

Offsetting Derivatives

The Company enters into master netting arrangements, which reduce credit risk by permitting net settlement of transactions with the same counterparty. The table below presents a gross presentation, the effects of offsetting, and a net presentation of the Company’s derivatives as of September 30, 2016 and December 31, 2015:

	As of September 30, 2016					
				Gross Amounts Not Offset in the Balance Sheet		
	Gross Amounts of Recognized Assets / Liabilities	Gross Amounts Offset in the Balance Sheet	Net Amounts of Assets / Liabilities presented in the Balance Sheet	Financial Instruments	Cash Collateral Received	Net Amount
Offsetting Assets:						
Derivatives	$3,625	$ —	$ 3,625	$(1,607)	$ —	$ 2,018
Offsetting Liabilities:						
Derivatives	$1,724	$ —	$ 1,724	$(1,607)	$ —	$ 117

	As of December 31, 2015					
				Gross Amounts Not Offset in the Balance Sheet		
	Gross Amounts of Recognized	Gross Amounts Offset in the	Net Amounts of Assets / Liabilities	Financial Instruments	Cash Collateral Received	Net Amount

	Assets / Liabilities	Balance Sheet	presented in the Balance Sheet			
Offsetting Assets:						
Derivatives	$7,087	$ —	$ 7,087	$(1,468)	$ —	$ 5,619
Offsetting Liabilities:						
Derivatives	$1,468	$ —	$ 1,468	$(1,468)	$ —	$ —

Credit-risk-related Contingent Features

The Company has agreements with each of its derivative counterparties that contain a provision where if the Company defaults on any of its indebtedness, including a default where repayment of the indebtedness has not been accelerated by the lender, then the Company could also be declared in default on its derivative obligations.

As of September 30, 2016, the fair value of derivatives in a net liability position, which includes accrued interest but excludes any adjustment for nonperformance risk, related to these agreements was $0.4 million. As of September 30, 2016, the Company has not posted any collateral related to these agreements. If the Company had breached any of these provisions at

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September 30, 2016, it could have been required to settle its obligations under the agreements at their termination value of $0.4 million.

9. FAIR VALUE DISCLOSURES

Financial Instruments

The fair value for certain financial instruments is derived using a combination of market quotes, pricing models and other valuation techniques that involve significant management judgment. The price transparency of financial instruments is a key determinant of the degree of judgment involved in determining the fair value of the Company's financial instruments.

Financial instruments for which actively quoted prices or pricing parameters are available and whose markets contain orderly transactions will generally have a higher degree of price transparency than financial instruments whose markets are inactive or consist of non-orderly trades. The Company evaluates several factors when determining if a market is inactive or when market transactions are not orderly. The carrying values of cash and cash equivalents, restricted cash, accounts payable, accrued liabilities and the Credit Facility are reasonable estimates of fair value because of the short-term maturities of these instruments. Fair values for other financial instruments are derived as follows:

Loans receivable: These instruments are presented in the accompanying condensed consolidated balance sheets at their amortized cost and not at fair value. The fair value of the loans receivable were estimated using an internal valuation model that considered the expected cash flows for the loans receivable, the underlying collateral value and other credit enhancements. As such, the Company classifies these instruments as Level 3.

Preferred equity investments: These instruments are presented in the accompanying condensed consolidated balance sheets at their cost and not at fair value. The fair value of the preferred equity investments were estimated using an internal valuation model that considered the expected future cash flows for the preferred equity investment, the underlying collateral value and other credit enhancements. As such, the Company classifies these instruments as Level 3.

Derivative instruments: The Company's derivative instruments are presented at fair value on the accompanying condensed consolidated balance sheets. The Company estimates the fair value of derivative instruments, including its interest rate cap, interest rate swap and cross currency swaps, using the assistance of a third party using inputs that are observable in the market, which includes forward yield curves and other relevant information. Although the Company has determined that the majority of the inputs used to value its derivative financial instruments fall within level 2 of the fair value hierarchy, the credit valuation adjustments associated with its derivative financial instruments utilize level 3 inputs, such as estimates of current credit spreads to evaluate the likelihood of default by itself and its counterparties. The Company has assessed the significance of the impact of the credit valuation adjustments on the overall valuation of its derivative positions and has determined that the credit valuation adjustments are not significant to the overall valuation of its derivative financial instruments. As a result, the Company has determined that its derivative financial instruments valuations in their entirety are classified in level 2 of the fair value hierarchy.

Senior Notes: These instruments are presented in the accompanying condensed consolidated balance sheets at their outstanding principal balance, net of unamortized deferred financing costs and premiums (discounts) and not at fair value. The fair values of the Senior Notes were determined using third-party market quotes derived from orderly trades. As such, the Company classifies these instruments as Level 2.

Mortgage indebtedness: These instruments are presented in the accompanying condensed consolidated balance sheets at their outstanding principal balance, net of unamortized deferred financing costs and premiums (discounts) and not at fair value. The fair values of the Company's mortgage notes payable were estimated using a discounted cash flow analysis based on management's estimates of current market interest rates for instruments with similar characteristics, including remaining loan term, loan-to-value ratio, type of collateral and other credit enhancements. As such, the Company classifies these instruments as Level 3.

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The following are the face values, carrying amounts and fair values of the Company's financial instruments as of September 30, 2016 and December 31, 2015 whose carrying amounts do not approximate their fair value (in thousands):

	September 30, 2016			December 31, 2015		
	Carrying Amount (1)	Face Value (2)	Fair Value	Carrying Amount (1)	Face Value (2)	Fair Value
Financial assets:						
Loans receivable	$54,613	$54,471	$55,485	$270,184	$273,811	$274,628
Preferred equity investments	42,973	42,594	45,538	29,993	29,643	30,838
Financial liabilities:						
Senior Notes	687,607	700,000	726,000	685,704	700,000	718,500
Mortgage indebtedness	162,130	165,045	161,922	174,846	177,850	165,296

(1) Carrying amounts represent the book value of financial instruments and are net of unamortized premiums (discounts) and deferred financing costs.
(2) Face value represents amounts contractually due under the terms of the respective agreements.

The Company determined the fair value of financial instruments as of September 30, 2016 whose carrying amounts do not approximate their fair value with valuation methods utilizing the following types of inputs (in thousands):

		Fair Value Measurements Using		
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial assets:				
Loans receivable	$55,485			