IMMUNOGEN INC
Form 10-Q
October 29, 2013
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2013

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 0-17999

ImmunoGen, Inc.

Massachusetts	**04-2726691**

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

830 Winter Street, Waltham, MA 02451

(Address of principal executive offices, including zip code)

(781) 895-0600

(Registrant s telephone number, including area code)

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. xYes o No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, 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). x Yes o No

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). o Yes x No

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

Shares of common stock, par value $.01 per share: 85,395,256 shares outstanding as of October 21, 2013.

Table of Contents

IMMUNOGEN, INC.

FORM 10-Q

FOR THE QUARTER ENDED SEPTEMBER 30, 2013

TABLE OF CONTENTS

Item		Page Number
	Part I	
1.	Financial Statements (Unaudited):	
1a.	Consolidated Balance Sheets as of September 30, 2013 and June 30, 2013	3
1b.	Consolidated Statements of Operations and Comprehensive Loss for the three months ended September 30, 2013 and 2012	4
1c.	Consolidated Statements of Cash Flows for the three months ended September 30, 2013 and 2012	5
1d.	Notes to Consolidated Financial Statements	6
2.	Management s Discussion and Analysis of Financial Condition and Results of Operations	18
3.	Quantitative and Qualitative Disclosures about Market Risk	24
4.	Controls and Procedures	25
	Part II	
1A.	Risk Factors	26
6.	Exhibits	26
	Signatures	27

Table of Contents

ITEM 1. ***Financial Statements***

IMMUNOGEN, INC.

CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

In thousands, except per share amounts

	September 30, 2013	June 30, 2013
ASSETS		
Cash and cash equivalents	$ 174,838	$ 194,960
Accounts receivable	5,789	
Unbilled revenue	1,979	2,121
Inventory	1,671	703
Restricted cash	319	319
Prepaid and other current assets	3,140	2,581
Total current assets	187,736	200,684
Property and equipment, net of accumulated depreciation	10,173	10,783
Long-term restricted cash	1,912	1,912
Other assets	203	217
Total assets	$ 200,024	$ 213,596
LIABILITIES AND SHAREHOLDERS EQUITY		
Accounts payable	$ 3,122	$ 4,498
Accrued compensation	3,276	6,153
Other accrued liabilities	6,904	6,049
Current portion of deferred lease incentive	979	979
Current portion of deferred revenue	2,260	1,494
Total current liabilities	16,541	19,173
Deferred lease incentive, net of current portion	5,382	5,626
Deferred revenue, net of current portion	55,275	63,384
Other long-term liabilities	3,385	3,566
Total liabilities	80,583	91,749
Commitments and contingencies (Note E)		
Shareholders equity:		
Preferred stock, $.01 par value; authorized 5,000 shares; no shares issued and outstanding		
Common stock, $.01 par value; authorized 150,000 shares; issued and outstanding 85,270 and 84,725 shares as of September 30, 2013 and June 30, 2013, respectively	853	847
Additional paid-in capital	706,581	697,767
Accumulated deficit	(587,993)	(576,767)
Total shareholders equity	119,441	121,847
Total liabilities and shareholders equity	$ 200,024	$ 213,596

The accompanying notes are an integral part of the consolidated financial statements.

Table of Contents

IMMUNOGEN, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS

(UNAUDITED)

In thousands, except per share amounts

	Three Months Ended September 30,	
	2013	2012
Revenues:		
License and milestone fees	$ 13,167	$ 933
Research and development support	1,990	1,377
Clinical materials revenue	8	1,781
Royalty revenue	2,053	
Total revenues	17,218	4,091
Operating Expenses:		
Research and development	22,029	23,700
General and administrative	6,526	5,639
Total operating expenses	28,555	29,339
Loss from operations	(11,337)	(25,248)
Other income, net	111	56
Net loss	$ (11,226)	$ (25,192)
Basic and diluted net loss per common share	$ (0.13)	$ (0.30)
Basic and diluted weighted average common shares outstanding	85,010	83,350
Total comprehensive loss	$ (11,226)	$ (25,192)

The accompanying notes are an integral part of the consolidated financial statements.

Table of Contents

IMMUNOGEN, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

In thousands, except per share amounts

	Three Months ended September 30, 2013	2012
Cash flows from operating activities:		
Net loss	$ (11,226)	$ (25,192)
Adjustments to reconcile net loss to net cash used for operating activities:		
Depreciation and amortization	1,162	1,174
Loss (gain) on sale/disposal of fixed assets	20	(17)
(Gain) loss on forward contracts	(2)	2
Stock and deferred share unit compensation	4,795	3,920
Deferred rent	(6)	(27)
Changes in operating assets and liabilities:		
Accounts receivable	(5,789)	(724)
Unbilled revenue	142	(250)
Inventory	(968)	1,118
Prepaid and other current assets	(559)	(11)
Other assets	14	
Accounts payable	(1,376)	(179)
Accrued compensation	(2,877)	(2,506)
Other accrued liabilities	438	2,651
Deferred revenue	(7,343)	(965)
Net cash used for operating activities	(23,575)	(21,006)
Cash flows from investing activities:		
Purchases of property and equipment, net	(572)	(966)
Payments from settlement of forward contracts		(46)
Net cash used for investing activities	(572)	(1,012)
Cash flows from financing activities:		
Proceeds from common stock issuance, net		94,006
Proceeds from stock options exercised	4,025	688
Net cash provided by financing activities	4,025	94,694
Net change in cash and cash equivalents	(20,122)	72,676
Cash and cash equivalents, beginning balance	194,960	160,938
Cash and cash equivalents, ending balance	$ 174,838	$ 233,614

The accompanying notes are an integral part of the consolidated financial statements.

Table of Contents

IMMUNOGEN, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2013

A. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited consolidated financial statements at September 30, 2013 and June 30, 2013 and for the three months ended September 30, 2013 and 2012 include the accounts of ImmunoGen, Inc., or the Company, and its wholly owned subsidiaries, ImmunoGen Securities Corp. and ImmunoGen Europe Limited. The consolidated financial statements include all of the adjustments, consisting only of normal recurring adjustments, which management considers necessary for a fair presentation of the Company s financial position in accordance with accounting principles generally accepted in the U.S. for interim financial information. Certain information and footnote disclosures normally included in the Company s annual financial statements have been condensed or omitted. The preparation of interim financial statements requires the use of management s estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the interim financial statements and the reported amounts of revenues and expenditures during the reported periods. The results of the interim periods are not necessarily indicative of the results for the entire year. Accordingly, the interim financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company s Annual Report on Form 10-K for the year ended June 30, 2013.

Subsequent Events

The Company has evaluated all events or transactions that occurred after September 30, 2013 up through the date the Company issued these financial statements. In October 2013, Novartis extended the initial three-year term of its right-to-test agreement with the Company for an additional one-year period by payment of a $5 million fee and took its second license under the agreement which resulted in a $1 million payment to the Company. Additionally, Amgen converted its one non-exclusive license agreement to an exclusive license by payment of a $500,000 fee to the Company. The Company did not have any other material recognizable or unrecognizable subsequent events during this period.

Revenue Recognition

The Company enters into licensing and development agreements with collaborative partners for the development of monoclonal antibody-based anticancer therapeutics. The terms of these agreements contain multiple deliverables which may include (i) licenses, or options to obtain licenses, to the Company s Targeted Antibody Payload, or TAP, technology, (ii) rights to future technological improvements, (iii) research activities to be performed on behalf of the collaborative partner, (iv) delivery of cytotoxic agents and (v) the manufacture of preclinical or clinical materials for the collaborative partner. Payments to the Company under these agreements may include upfront fees, option fees, exercise fees, payments for research activities, payments for the manufacture of preclinical or clinical materials, payments based upon the achievement of

certain milestones and royalties on product sales. The Company follows the provisions of the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 605-25, Revenue Recognition Multiple-Element Arrangements, and ASC Topic 605-28, Revenue Recognition Milestone Method, in accounting for these agreements. In order to account for these agreements, the Company must identify the deliverables included within the agreement and evaluate which deliverables represent separate units of accounting based on whether certain criteria are met, including whether the delivered element has stand-alone value to the collaborator. The consideration received is allocated among the separate units of accounting, and the applicable revenue recognition criteria are applied to each of the separate units.

At September 30, 2013, the Company had the following two types of agreements with the parties identified below:

- Development and commercialization licenses to use the Company s TAP technology and/or certain other intellectual property to develop compounds to a specified target antigen (referred to as development and commercialization licenses, as distinguished from the Company s right-to-test agreements described elsewhere):

Amgen (three exclusive single-target licenses; one non-exclusive single- target license)

Bayer HealthCare (one exclusive single-target license)

Biotest (one exclusive single-target license)

Lilly (one exclusive single-target license)

Table of Contents

Novartis (one license to two related targets: one target on an exclusive basis and the second target on a non-exclusive basis)

Roche, through its Genentech unit (five exclusive single-target licenses)

Sanofi (exclusive license to multiple individual targets)

- Option/research agreement for a defined period of time to secure development and commercialization licenses to use the Company s TAP technology to develop anticancer compounds to specified targets on established terms (referred to herein as right-to-test agreements):

Sanofi

Novartis

Lilly

There are no performance, cancellation, termination or refund provisions in any of the arrangements that contain material financial consequences to the Company.

Development and Commercialization Licenses

The deliverables under a development and commercialization license agreement generally include the license to the Company s TAP technology with respect to a specified antigen target, and may also include deliverables related to rights to future technological improvements, research activities to be performed on behalf of the collaborative partner and the manufacture of preclinical or clinical materials for the collaborative partner.

Generally, development and commercialization licenses contain non-refundable terms for payments and, depending on the terms of the agreement, provide that the Company will (i) at the collaborator s request, provide research services at negotiated prices which are generally consistent with what other third parties would charge, (ii) at the collaborator s request, manufacture and provide to it preclinical and clinical materials or deliver cytotoxic agents at negotiated prices which are generally consistent with what other third parties would charge, (iii) earn payments upon the achievement of certain milestones and (iv) earn royalty payments, generally until the later of the last applicable patent expiration or 10 to 12 years after product launch. In the case of Kadcyla®, however, the minimum royalty term is 10 years and the maximum royalty term is 12 years on a country-by-country basis. Royalty rates may vary over the royalty term depending on the Company s intellectual

property rights. The Company may provide technical assistance and share any technology improvements with its collaborators during the term of the collaboration agreements. The Company does not directly control when or whether any collaborator will request research or manufacturing services, achieve milestones or become liable for royalty payments. As a result, the Company cannot predict when or if it will recognize revenues in connection with any of the foregoing.

In determining the units of accounting, management evaluates whether the license has stand-alone value from the undelivered elements to the collaborative partner based on the consideration of the relevant facts and circumstances for each arrangement. Factors considered in this determination include the research capabilities of the partner and the availability of TAP technology research expertise in the general marketplace. If the Company concludes that the license has stand-alone value and therefore will be accounted for as a separate unit of accounting, the Company then determines the estimated selling prices of the license and all other units of accounting based on market conditions, similar arrangements entered into by third parties, and entity-specific factors such as the terms of the Company s previous collaborative agreements, recent preclinical and clinical testing results of therapeutic products that use the Company s TAP technology, the Company s pricing practices and pricing objectives, the likelihood that technological improvements will be made, the likelihood that technological improvements made will be used by the Company s collaborators and the nature of the research services to be performed on behalf of its collaborators and market rates for similar services.

Upfront payments on development and commercialization licenses are deferred if facts and circumstances dictate that the license does not have stand-alone value. Prior to the adoption of Accounting Standards Update (ASU) No. 2009-13, Revenue Arrangements with Multiple Deliverables on July 1, 2010, the Company determined that its licenses lacked stand-alone value and were combined with other elements of the arrangement and any amounts associated with the license were deferred and amortized over a certain period, which the Company refers to as the Company s period of substantial involvement. The determination of the length of the period over which to defer revenue is subject to judgment and estimation and can have an impact on the amount of revenue recognized in a given period. Historically the Company s involvement with the development of a collaborator s product candidate has

been significant at the early stages of development, and lessens as it progresses into clinical trials. Also, as a drug candidate gets closer to commencing pivotal testing the Company s collaborators have sought an alternative site to manufacture their products, as the Company s facility does not produce pivotal or commercial drug product. Accordingly, the Company generally estimates this period of substantial involvement to begin at the inception of the collaboration agreement and conclude at the end of non-pivotal Phase II testing. The Company believes this period of substantial involvement is, depending on the nature of the license, on average six and one-half years. Quarterly, the Company reassesses its periods of substantial involvement over which the Company amortizes its upfront license fees and makes adjustments as appropriate. In the event a collaborator elects to discontinue development of a specific product candidate under a development and commercialization license, but retains its right to use the Company s technology to develop an alternative product candidate to the same target or a target substitute, the Company would cease amortization of any remaining portion of the upfront fee until there is substantial preclinical activity on another product candidate and its remaining period of substantial involvement can be estimated. In the event that a development and commercialization license were to be terminated, the Company would recognize as revenue any portion of the upfront fee that had not previously been recorded as revenue, but was classified as deferred revenue, at the date of such termination.

Subsequent to the adoption of ASU No. 2009-13, the Company determined that its research licenses lack stand-alone value and are considered for aggregation with the other elements of the arrangement and accounted for as one unit of accounting.

Upfront payments on development and commercialization licenses may be recognized upon delivery of the license if facts and circumstances dictate that the license has stand-alone value from the undelivered elements, which generally include rights to future technological improvements, research services, delivery of cytotoxic agents and the manufacture of preclinical and clinical materials.

The Company recognizes revenue related to research services that represent separate units of accounting as they are performed, as long as there is persuasive evidence of an arrangement, the fee is fixed or determinable, and collection of the related receivable is probable. The Company recognizes revenue related to the rights to future technological improvements over the estimated term of the applicable license.

The Company may also provide cytotoxic agents to its collaborators or produce preclinical and clinical materials at negotiated prices which are generally consistent with what other third parties would charge. The Company recognizes revenue on cytotoxic agents and on preclinical and clinical materials when the materials have passed all quality testing required for collaborator acceptance and title and risk of loss have transferred to the collaborator. Arrangement consideration allocated to the manufacture of preclinical and clinical materials in a multiple-deliverable arrangement is below the Company s full cost, and the Company s full cost is not expected to be below its contract selling prices for its existing collaborations for the foreseeable future. During the three months ended September 30, 2012, the difference between the Company s full cost to manufacture preclinical and clinical materials on behalf of its collaborators as compared to total amounts received from collaborators for the manufacture of preclinical and clinical materials was $755,000. There were no sales of manufactured preclinical or clinical materials during the three months ended September 30, 2013. The majority of the Company s costs to produce these preclinical and clinical materials are fixed and then allocated to each batch based on the number of batches produced during the period. Therefore, the Company s costs to produce these materials are significantly impacted by the number of batches produced during the period. The volume of preclinical and clinical materials the Company produces is directly related to the number of clinical trials for which the Company and its collaborators are preparing or currently have underway, the speed of enrollment in those trials, the dosage schedule of each clinical trial and the time period such trials last. Accordingly, the volume of preclinical and clinical materials produced, and therefore the Company s per batch costs to manufacture these preclinical and clinical materials, may vary significantly from period to period.

The Company may also produce research material for potential collaborators under material transfer agreements. Additionally, the Company performs research activities, including developing antibody specific conjugation processes, on behalf of its collaborators and potential collaborators during the early evaluation and preclinical testing stages of drug development. The Company records amounts received for research materials produced or services performed as a component of research and development support revenue. The Company also develops

conjugation processes for materials for later stage testing and commercialization for certain collaborators. The Company is compensated at negotiated rates and may receive milestone payments for developing these processes which are recorded as a component of research and development support revenue.

The Company s development and commercialization license agreements have milestone payments which for reporting purposes are aggregated into three categories: (i) development milestones, (ii) regulatory milestones, and (iii) sales milestones. Development milestones are typically payable when a product candidate initiates or advances into different clinical trial phases. Regulatory milestones are typically payable upon submission for marketing approval with the U.S. Food and Drug Administration, or FDA, or other countries regulatory authorities or on receipt of actual marketing approvals for the compound or for additional indications. Sales milestones are typically payable when annual sales reach certain levels.

Table of Contents

At the inception of each agreement that includes milestone payments, the Company evaluates whether each milestone is substantive and at risk to both parties on the basis of the contingent nature of the milestone. This evaluation includes an assessment of whether (a) the consideration is commensurate with either (1) the entity s performance to achieve the milestone, or (2) the enhancement of the value of the delivered item(s) as a result of a specific outcome resulting from the entity s performance to achieve the milestone, (b) the consideration relates solely to past performance and (c) the consideration is reasonable relative to all of the deliverables and payment terms within the arrangement. The Company evaluates factors such as the scientific, regulatory, commercial and other risks that must be overcome to achieve the respective milestone, the level of effort and investment required to achieve the respective milestone and whether the milestone consideration is reasonable relative to all deliverables and payment terms in the arrangement in making this assessment.

Non-refundable development and regulatory milestones that are expected to be achieved as a result of the Company s efforts during the period of substantial involvement are considered substantive and are recognized as revenue upon the achievement of the milestone, assuming all other revenue recognition criteria are met. Milestones that are not considered substantive because we do not contribute effort to the achievement of such milestones are generally achieved after the period of substantial involvement and are recognized as revenue upon achievement of the milestone, as there are no undelivered elements remaining and no continuing performance obligations, assuming all other revenue recognition criteria are met.

Under the Company s development and commercialization license agreements, the Company receives royalty payments based upon its licensees net sales of covered products. Generally, under these agreements the Company is to receive royalty reports and payments from its licensees approximately one quarter in arrears, that is, generally in the second month of the quarter after the licensee has sold the royalty-bearing product or products. The Company recognizes royalty revenues when it can reliably estimate such amounts and collectability is reasonably assured. As such, the Company generally recognizes royalty revenues in the quarter reported to the Company by its licensees, or one quarter following the quarter in which sales by the Company s licensees occurred.

Right-to-Test Agreements

The Company s right-to-test agreements provide collaborators the right to (a) test the Company s TAP technology for a defined period of time through a research, or right-to-test, license, (b) take options, for a defined period of time, to specified targets and (c) upon exercise of those options, secure or take licenses to develop and commercialize products for the specified targets on established terms. Under these agreements, fees may be due to the Company (i) at the inception of the arrangement (referred to as upfront fees or payments), (ii) upon taking an option with respect to a specific target (referred to as option fees or payments earned, if any, when the option is taken), (iii) upon the exercise of a previously taken option to acquire a development and commercialization license(s) (referred to as exercise fees or payments earned, if any, when the development and commercialization license is taken), or (iv) some combination of all of these fees.

The accounting for right-to-test agreements is dependent on the nature of the options granted to the collaborative partner. Options are considered substantive if, at the inception of a right-to-test agreement, the Company is at risk as to whether the collaborative partner will choose to exercise the options to secure development and commercialization licenses. Factors that are considered in evaluating whether options are substantive include the overall objective of the arrangement, the benefit the collaborator might obtain from the agreement without exercising the options, the cost to exercise the options relative to the total upfront consideration, and the additional financial commitments or economic penalties imposed on the collaborator as a result of exercising the options.

For right-to-test agreements where the options to secure development and commercialization licenses to the Company s TAP technology are considered substantive, the Company does not consider the development and commercialization licenses to be a deliverable at the inception of

the agreement. For those right-to-test agreements entered into prior to the adoption of ASU No. 2009-13 where the options to secure development and commercialization licenses are considered substantive, the Company has deferred the upfront payments received and recognizes this revenue over the period during which the collaborator could elect to take options for development and commercialization licenses. These periods are specific to each collaboration agreement. If a collaborator takes an option to acquire a development and commercialization license under these agreements, any substantive option fee is deferred and recognized over the life of the option, generally 12 to 18 months. If a collaborator exercises an option and takes a development and commercialization license to a specific target, the Company attributes the exercise fee to the development and commercialization license. Upon exercise of an option to acquire a development and commercialization license, the Company would also attribute any remaining deferred option fee to the development and commercialization license and apply the multiple-element revenue recognition criteria to the development and commercialization license and any other deliverables to determine the appropriate revenue recognition, which will be consistent with the Company s accounting policy for upfront payments on single-target licenses. In the event a right-to-test agreement were to be terminated, the Company would recognize as revenue any portion of the upfront fee that had not previously been recorded as revenue, but was classified as deferred revenue, at the date of such termination. None of the Company s

Table of Contents

right-to-test agreements entered into subsequent to the adoption of ASU No. 2009-13 has been determined to contain substantive options.

For right-to-test agreements where the options to secure development and commercialization licenses to the Company s TAP technology are not considered substantive, the Company considers the development and commercialization licenses to be a deliverable at the inception of the agreement and applies the multiple-element revenue recognition criteria to determine the appropriate revenue recognition. None of the Company s right-to-test agreements entered into prior to the adoption of ASU No. 2009-13 has been determined to contain non-substantive options.

The Company does not directly control when or if any collaborator will exercise its options for development and commercialization licenses. As a result, the Company cannot predict when or if it will recognize revenues in connection with any of the foregoing.

Fair Value of Financial Instruments

Fair value is defined under ASC Topic 820, Fair Value Measurements and Disclosures, as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy to measure fair value which is based on three levels of inputs, of which the first two are considered observable and the last unobservable, as follows:

- Level 1 - Quoted prices in active markets for identical assets or liabilities.

- Level 2 - Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

- Level 3 - Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

As of September 30, 2013, the Company held certain assets that are required to be measured at fair value on a recurring basis. The following table represents the fair value hierarchy for the Company s financial assets measured at fair value on a recurring basis as of September 30, 2013 (in thousands):

Fair Value Measurements at September 30, 2013 Using

	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash, cash equivalents and restricted cash	$ 177,069	$ 177,069	$	$

As of June 30, 2013, the Company held certain assets that are required to be measured at fair value on a recurring basis. The following table represents the fair value hierarchy for the Company s financial assets measured at fair value on a recurring basis as of June 30, 2013 (in thousands):

		Fair Value Measurements at June 30, 2013 Using		
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash, cash equivalents and restricted cash	$ 197,191	$ 197,191	$	$

The fair value of the Company s cash equivalents is based primarily on quoted prices from active markets.

Unbilled Revenue

The majority of the Company s unbilled revenue at September 30, 2013 and June 30, 2013 represents research funding earned prior to those dates based on actual resources utilized under the Company s agreements with various collaborators.

Table of Contents

Inventory

Inventory costs relate to clinical trial materials being manufactured for sale to the Company s collaborators. Inventory is stated at the lower of cost or market as determined on a first-in, first-out (FIFO) basis.

Inventory at September 30, 2013 and June 30, 2013 is summarized below (in thousands):

	September 30, 2013	June 30, 2013
Raw materials	$ 363	$ 75
Work in process	1,308	628
Total	$ 1,671	$ 703

Raw materials inventory consists entirely of DM1 and DM4, proprietary cell-killing agents the Company developed as part of its TAP technology. The Company considers more than a twelve month supply of raw materials that is not supported by firm, fixed orders and/or projections from its collaborators to be excess and establishes a reserve to reduce to zero the value of any such excess raw material inventory with a corresponding charge to research and development expense. In accordance with this policy, the Company recorded $135,000 of expense related to excess inventory during the three-month period ended September 30, 2013 compared to $390,000 recorded during the same period last year.

Work in process inventory consists of conjugate manufactured for sale to the Company s collaborators to be used in preclinical and clinical studies. All conjugate is made to order at the request of the collaborators and subject to the terms and conditions of respective supply agreements. As such, no reserve for work in process inventory is required.

Computation of Net Loss per Common Share

Basic and diluted net loss per share is calculated based upon the weighted average number of common shares outstanding during the period. During periods of income, participating securities are allocated a proportional share of income determined by dividing total weighted average participating securities by the sum of the total weighted average common shares and participating securities (the two-class method). The Company s restricted stock participates in any dividends declared by the Company and are therefore considered to be participating securities. Participating securities have the effect of diluting both basic and diluted earnings per share during periods of income. During periods of loss, no loss is allocated to participating securities since they have no contractual obligation to share in the losses of the Company. Diluted (loss) earnings per share is computed after giving consideration to the dilutive effect of stock options that are outstanding during the period, except where such non-participating securities would be anti-dilutive.

The Company s common stock equivalents, as calculated in accordance with the treasury-stock method, are shown in the following table (in thousands):

	Three Months Ended September 30,	
	2013	2012
Options outstanding to purchase common stock and unvested restricted stock	8,733	7,960
Common stock equivalents under treasury stock method	2,215	2,552

The Company s common stock equivalents have not been included in the net loss per share calculation because their effect is anti-dilutive due to the Company s net loss position.

Stock-Based Compensation

As of September 30, 2013, the Company is authorized to grant future awards under one employee share-based compensation plan, which is the ImmunoGen, Inc. 2006 Employee, Director and Consultant Equity Incentive Plan, or the 2006 Plan. At the annual meeting of shareholders on November 13, 2012, an amendment to the 2006 Plan was approved and an additional 3,500,000 shares were authorized for issuance under this plan. As amended, the 2006 Plan provides for the issuance of Stock Grants, the grant of Options and the grant of Stock-Based Awards for up to 12,000,000 shares of the Company s common stock, as well as any shares of common stock that are represented by awards granted under the previous stock option plan, the ImmunoGen, Inc. Restated Stock Option Plan, or the Former Plan, that are forfeited, expire or are cancelled without delivery of shares of common stock; provided, however, that no more than 5,900,000 shares shall be added to the 2006 Plan from the Former Plan, pursuant to this provision. Option awards are granted with an exercise price equal to the market price of the Company s stock at the date of grant. Options vest at various periods of up to four years and may be exercised within ten years of the date of grant.

The stock-based awards are accounted for under ASC Topic 718, Compensation Stock Compensation. Pursuant to Topic 718, the estimated grant date fair value of awards is charged to the statement of operations and comprehensive loss over the requisite service period, which is the vesting period. Such amounts have been reduced by an estimate of forfeitures of all unvested awards. The

Table of Contents

fair value of each stock option is estimated on the date of grant using the Black-Scholes option-pricing model with the assumptions noted in the following table. As the Company has not paid dividends since inception, nor does it expect to pay any dividends for the foreseeable future, the expected dividend yield assumption is zero. Expected volatility is based exclusively on historical volatility data of the Company s stock. The expected term of stock options granted is based exclusively on historical data and represents the period of time that stock options granted are expected to be outstanding. The expected term is calculated for and applied to one group of stock options as the Company does not expect substantially different exercise or post-vesting termination behavior among its option recipients. The risk-free rate of the stock options is based on the U.S. Treasury rate in effect at the time of grant for the expected term of the stock options.

	Three Months Ended September 30,	
	2013	**2012**
Dividend	None	None
Volatility	60.44%	60.44%
Risk-free interest rate	1.69%	0.84%
Expected life (years)	6.3	6.3

Using the Black-Scholes option-pricing model, the weighted average grant date fair values of options granted during the three months ended September 30, 2013 and 2012 were $10.93 and $8.91 per share, respectively.

Stock compensation expense related to stock options and restricted stock awards granted under the 2006 Plan was $4.7 million and $3.8 million during the three months ended September 30, 2013 and 2012, respectively. As of September 30, 2013, the estimated fair value of unvested employee awards was $28.5 million, net of estimated forfeitures. The weighted-average remaining vesting period for these awards is approximately two and a half years.

During the three months ended September 30, 2013, holders of options issued under the Company s equity plans exercised their rights to acquire an aggregate of approximately 545,000 shares of common stock at prices ranging from $3.19 to $15.83 per share. The total proceeds to the Company from these option exercises were approximately $4.0 million.

Financial Instruments and Concentration of Credit Risk

The Company s cash equivalents consist of money market funds with underlying investments primarily being U.S. Government-issued securities and high quality, short-term commercial paper. All of the Company s cash and cash equivalents are maintained with three financial institutions in the U.S. The Company uses a Euro-denominated bank account to manage the foreign currency exposures that exist as part of our ongoing business operations. Our foreign currency risk management strategy is principally designed to mitigate the future potential financial impact of changes in the value of transactions, anticipated transactions and balances denominated in foreign currency, resulting from changes in foreign currency exchange rates.

Segment Information

During the three months ended September 30, 2013, the Company continued to operate in one reportable business segment which is the business of discovery of monoclonal antibody-based anticancer therapeutics.

The percentages of revenues recognized from significant customers of the Company in the three months ended September 30, 2013 and 2012 are included in the following table:

	Three Months Ended September 30,	
Collaborative Partner:	**2013**	**2012**
Amgen	1%	23%
Bayer HealthCare	%	20%
Biotest	1%	23%
Lilly	49%	6%
Novartis	7%	24%
Roche	41%	%

There were no other customers of the Company with significant revenues in the three months ended September 30, 2013 and 2012.

Table of Contents

Recent Accounting Pronouncements

In July 2013, the FASB issued guidance to address the diversity in practice related to the financial statement presentation of unrecognized tax benefits as either a reduction of a deferred tax asset or a liability when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. This guidance is effective prospectively for fiscal years, and interim periods within those years, beginning after December 15, 2013. The adoption of this guidance is not expected to have a material impact on the Company s consolidated financial statements.

B. Collaborative Agreements

Roche

In May 2000, the Company granted Genentech, now a unit of Roche, an exclusive license to use the Company s maytansinoid TAP technology with antibodies, such as trastuzumab, or other proteins that target HER2. Under the terms of this agreement, Roche has exclusive worldwide rights to develop and commercialize maytansinoid TAP compounds targeting HER2. In February 2013, the U.S. FDA granted marketing approval to the HER2-targeting TAP compound, Kadcyla. In September 2013, Roche received marketing approval for Kadcyla in Japan. Roche is responsible for the manufacturing, product development and marketing of Kadcyla and any other products resulting from the agreement. The Company received a $2 million non-refundable upfront payment from Roche upon execution of the agreement. The Company is also entitled to receive up to a total of $44 million in milestone payments, plus royalties on the commercial sales of Kadcyla or any other resulting products. Total milestones are categorized as follows: development milestones $13.5 million; and regulatory milestones $30.5 million. The marketing approval of Kadcyla in Japan in September 2013 triggered a $5 million regulatory milestone payment to the Company. Based on an evaluation of the effort contributed to the achievement of this milestone, the Company determined this milestone was not substantive. In consideration that there were no undelivered elements remaining, no continuing performance obligations and all other revenue recognition criteria had been met, the Company recognized the $5 million non-refundable payments as revenue upon achievement of the milestone, which is included in license and milestone fees for the three months ended September 30, 2013. Through September 30, 2013, the Company has received and recognized $13.5 million and $15.5 million in development and regulatory milestone payments, respectively, related to Kadcyla. The next potential milestone the Company will be entitled to receive is a $5 million regulatory milestone for marketing approval of Kadcyla in the European Union. Based on an evaluation of the effort contributed to the achievement of this milestone, the Company has determined this milestone is not substantive. The Company receives royalty reports and payments related to sales of Kadcyla from Roche one quarter in arrears. In accordance with the Company s revenue recognition policy, $2.1 million of royalties on net sales of Kadcyla for the three-month period ended June 30, 2013 were recorded and included in royalty revenue for the three months ended September 30, 2013.

Novartis

In October 2010, the Company entered into a three-year right-to-test agreement with Novartis Institutes for BioMedical Research, Inc. (Novartis). The agreement provides Novartis with the right to (a) test the Company s TAP technology with individual antibodies selected by Novartis under a right-to-test, or research, license, (b) take exclusive options, with certain restrictions, to individual targets selected by Novartis for specified option periods and (c) upon exercise of those options, take exclusive licenses to use the Company s TAP technology to develop and commercialize products for a specified number of individual targets on terms agreed upon at the inception of the right-to-test agreement. The initial three-year term of the right-to-test agreement was extended by Novartis in October 2013 for an additional one-year period by payment of a $5 million fee to the Company. In addition to the one-year extension taken in October 2013, the terms of the right-to-test agreement allow Novartis to extend the research term for one additional one-year period by payment of additional consideration. The terms of the right-to-test agreement require Novartis to exercise its options for the development and commercialization licenses by the end of the term of the research

license. The Company received a $45 million upfront payment in connection with the execution of the right-to-test agreement, and for each development and commercialization license for a specific target, the Company is entitled to receive an exercise fee of $1 million and up to a total of $199.5 million in milestone payments, plus royalties on the commercial sales of any resulting products. The total milestones are categorized as follows: development milestones $22.5 million; regulatory milestones $77 million; and sales milestones $100 million. The Company also is entitled to receive payments for research and development activities performed on behalf of Novartis. Novartis is responsible for the manufacturing, product development and marketing of any products resulting from this agreement.

Effective March 29, 2013, the Company and Novartis amended the right-to-test agreement so that Novartis can take a license to develop and commercialize products directed at two pre-defined and related undisclosed targets, one target licensed on an exclusive basis and the other target initially licensed on a non-exclusive basis. The target licensed on a non-exclusive basis may be converted to an exclusive target by notice and payment to the Company of an agreed-upon fee of at least $5 million, depending on specific

Table of Contents

circumstances. The Company received a $3.5 million fee in connection with the execution of the amendment to the agreement. The Company may be required to credit this fee against future milestone payments if Novartis discontinues the development of a specified product under certain circumstances.

In connection with the amendment, on March 29, 2013, Novartis took the license referenced above under the right-to-test agreement, as amended, enabling it to develop and commercialize products directed at the two targets. The Company was entitled to a $1 million upfront fee with the execution of this license. Additionally, the execution of this license provides the Company the opportunity to receive milestone payments totaling $199.5 million (development milestones $22.5 million; regulatory milestones $77 million; and sales milestones $100 million) or $238 million (development milestones $22.5 million; regulatory milestones $115.5 million; and sales milestones $100 million), depending on the composition of any resulting products. In October 2013, Novartis took a second exclusive license to a single target, triggering a $1 million payment to the Company and the opportunity to receive milestone payments totaling $199.5 million, as outlined above. The first potential milestone the Company will be entitled to receive under either of these licenses will be a $5 million development milestone for commencement of a Phase I clinical trial. At the time of execution of these agreements, there was significant uncertainty as to whether these milestones would be achieved. In consideration of this, as well as the Company s past involvement in the research and manufacturing of these product candidates, these milestones were deemed substantive. Additionally, the Company is entitled to receive royalties on product sales, if any. Novartis also has the right to convert the noted non-exclusive license to an exclusive license, in which case the Company would be entitled to receive, depending on the composition of resultant products, an upward adjustment on milestone payments.

In accordance with ACS 605-25 (as amended by ASU No. 2009-13), the Company identified all of the deliverables at the inception of the right-to-test agreement and subsequently when amended. The significant deliverables were determined to be the right-to-test, or research, license, the development and commercialization licenses, rights to future technological improvements, and the research services. The options to obtain development and commercialization licenses in the right-to-test agreement were determined not to be substantive and, as a result, the exclusive development and commercialization licenses were considered deliverables at the inception of the right-to-test agreement. Factors that were considered in determining the options were not substantive included (i) the overall objective of the agreement was for Novartis to obtain development and commercialization licenses, (ii) the size of the exercise fee of $1 million for each development and commercialization license obtained is not significant relative to the $45 million upfront payment that was due at the inception of the right-to-test agreement, (iii) the limited economic benefit that Novartis could obtain from the right-to-test agreement unless it exercised its options to obtain development and commercialization licenses, and (iv) the lack of economic penalties as a result of exercising the options.

The Company has determined that the research license together with the development and commercialization licenses represent one unit of accounting as the research license does not have stand-alone value from the development and commercialization licenses due to the lack of transferability of the research license and the limited economic benefit Novartis would derive if they did not obtain any development and commercialization licenses. The Company has also determined that this unit of accounting does have stand-alone value from the rights to future technological improvements and the research services. The rights to future technological improvements and the research services are considered separate units of accounting as each of these was determined to have stand-alone value. The rights to future technological improvements have stand-alone value as Novartis would be able to use those items for their intended purpose without the undelivered elements. The research services have stand-alone value as similar services are sold separately by other vendors.

The estimated selling prices for the development and commercialization licenses are the Company s best estimate of selling price and were determined based on market conditions, similar arrangements entered into by third parties, including the Company s understanding of pricing terms offered by its competitors for single-target development and commercialization licenses that utilize antibody-drug conjugate technology, and entity-specific factors such as the pricing terms of the Company s previous single-target development and commercialization licenses, recent preclinical and clinical testing results of therapeutic products that use the Company s TAP technology, and the Company s pricing practices and pricing objectives. The estimated selling price of the right to technological improvements is the Company s best estimate of selling price and was determined by estimating the probability that technological improvements will be made and the probability that such technological improvements made will be used by Novartis. In estimating these probabilities, we considered factors such as the technology that is the subject of the development and commercialization licenses, our history of making technological improvements, and when such improvements, if any,

were likely to occur relative to the stage of development of any product candidates pursuant to the development and commercialization licenses. The Company s estimate of probability considered the likely period of time that any improvements would be utilized, which was estimated to be ten years following delivery of a commercialization and development license. The value of any technological improvements made available after this ten year period was considered to be *de minimis* due to the significant additional costs that would be incurred to incorporate such technology into any existing product candidates. The estimate of probability was multiplied by the estimated selling price of the development and commercialization licenses and the resulting cash flow was discounted at a rate of 16%, representing the Company s estimate of its cost of capital. The estimated selling price of the research services was based on third-party evidence given the nature of the research services to be performed for Novartis and market rates for similar services.

Table of Contents

The total arrangement consideration of $55.2 million (which comprises the $45 million upfront payment, the amendment fee of $3.5 million, the exercise fee for each license, and the expected fees for the research services to be provided under the remainder of the arrangement) was allocated to the deliverables based on the relative selling price method as follows: $55.4 million to the development and commercialization licenses; $4.1 million to the rights to future technological improvements; and $710,000 to the research services. Since execution of the first development and commercialization license taken in March 2013, the amount of the total arrangement consideration allocated to future technological improvements is being recognized as revenue ratably over the period the Company is obligated to make available any technological improvements, which is equivalent to the estimated term of the agreement. The Company estimates the term of a development and commercialization license to be approximately 25 years, which reflects management s estimate of the time necessary to develop and commercialize products pursuant to the license plus the estimated royalty term. The Company reassesses the estimated term at the end of each reporting period. The Company does not control when Novartis will exercise its options for development and commercialization licenses. As a result, the Company cannot predict when it will recognize the related license revenue except that it will be within the term of the research license. The Company will recognize research services revenue as the related services are delivered.

Lilly

In December 2011, the Company entered into a three-year right-to-test agreement with Eli Lilly and Company (Lilly). The agreement provides Lilly with the right to (a) take exclusive options, with certain restrictions, to individual targets selected by Lilly for specified option periods, (b) test the Company s maytansinoid TAP technology with Lilly s antibodies directed to the optioned targets under a right-to-test, or research, license, and (c) upon exercise of those options, take exclusive licenses to use the Company s maytansinoid TAP technology to develop and commercialize products for a specified number of individual targets on terms agreed upon at the inception of the right-to-test agreement. The terms of the right-to-test agreement require Lilly to exercise its options for the development and commercialization licenses by the end of the term of the research license. In August 2013, Lilly took its first exclusive license to a single target.

The Company received a $20 million upfront payment in connection with the execution of the right-to-test agreement, and for the first development and commercialization license taken, which occurred in August 2013, the Company is entitled to receive up to a total of $200.5 million in milestone payments, plus royalties on the commercial sales of any resulting products. For each subsequent development and commercialization license taken, the Company is entitled to receive an exercise fee in the amount of $2 million and up to a total of $199 million in milestone payments, plus royalties on the commercial sales of any resulting products. The total milestones are categorized as follows: development milestones $30.5 million for the first development and commercialization license and $29 million for each subsequent license; regulatory milestones $70 million; and sales milestones $100 million. The next payment the Company could receive would either be a $5 million development milestone payment with the initiation of a Phase I clinical trial under the first development and commercialization license taken, or a $2 million exercise fee for the execution of a second license. At the time of execution of this agreement, there was significant uncertainty as to whether the milestone related to initiation of a Phase I clinical trial under the first development and commercialization license would be achieved. In consideration of this, as well as the Company s expected involvement in the research and manufacturing of these product candidates, this milestone was deemed substantive. The Company also is entitled to receive payments for delivery of cytotoxic agents to Lilly and research and development activities performed on behalf of Lilly. Lilly is responsible for the manufacturing, product development and marketing of any products resulting from this collaboration.

In accordance with ASC 605-25 (as amended by ASU No. 2009-13), the Company identified all of the deliverables at the inception of the right-to-test agreement. The significant deliverables were determined to be the right-to-test, or research, license, the exclusive development and commercialization licenses, rights to future technological improvements, delivery of cytotoxic agents and the research services. The options to obtain development and commercialization licenses in the right-to-test agreement were determined not to be substantive and, as a result, the exclusive development and commercialization licenses were considered deliverables at the inception of the right-to-test agreement. Factors that were considered in determining the options were not substantive included (i) the overall objective of the agreement was for Lilly to obtain development and commercialization licenses, (ii) the size of the exercise fees of $2 million for each development and commercialization license taken beyond the first license is not significant relative to the $20 million upfront payment that was due at the inception of the right-to-test agreement, (iii) the limited economic benefit that Lilly could obtain from the right-to-test agreement unless it exercised its options to obtain

development and commercialization licenses, and (iv) the lack of economic penalties as a result of exercising the options.

The Company has determined that the research license together with the development and commercialization licenses represent one unit of accounting as the research license does not have stand-alone value from the development and commercialization licenses due to the lack of transferability of the research license and the limited economic benefit Lilly would derive if they did not obtain any development and commercialization licenses. The Company has also determined that this unit of accounting has stand-alone value from the rights to future technological improvements, the delivery of cytotoxic agents and the research services. The rights to future technological improvements, delivery of cytotoxic agents and the research services are considered separate units of

Table of Contents

accounting as each of these was determined to have stand-alone value. The rights to future technological improvements have stand-alone value as Lilly would be able to use those items for their intended purpose without the undelivered elements. The research services and cytotoxic agents have stand-alone value as similar services and products are sold separately by other vendors.

The estimated selling prices for the development and commercialization licenses are the Company s best estimate of selling price and were determined based on market conditions, similar arrangements entered into by third parties, including pricing terms offered by our competitors for single-target development and commercialization licenses that utilize antibody-drug conjugate technology, and entity-specific factors such as the pricing terms of the Company s previous single-target development and commercialization licenses, recent preclinical and clinical testing results of therapeutic products that use the Company s TAP technology, and the Company s pricing practices and pricing objectives. The estimated selling price of the rights to technological improvements is the Company s best estimate of selling price and was determined by estimating the probability that technological improvements will be made, and the probability that technological improvements made will be used by Lilly. In estimating these probabilities, we considered factors such as the technology that is the subject of the development and commercialization licenses, our history of making technological improvements, and when such improvements, if any, were likely to occur relative to the stage of development of any product candidates pursuant to the development and commercialization licenses. The company s estimate of probability considered the likely period of time that any improvements would be utilized, which was estimated to be ten years following delivery of a commercialization and development license. The value of any technological improvements made available after this ten year period was considered to be *de minimis* due to the significant additional costs that would be incurred to incorporate such technology into any existing product candidates. The estimate of probability was multiplied by the estimated selling price of the development and commercialization licenses and the resulting cash flow was discounted at a rate of 16%, representing the Company s estimate of its cost of capital. The estimated selling price of the cytotoxic agent was based on third-party evidence given market rates for the manufacture of such cytotoxic agents. The estimated selling price of the research services was based on third-party evidence given the nature of the research services to be performed for Lilly and market rates for similar services.

The total arrangement consideration of $28.2 million (which comprises the $20 million upfront payment, the exercise fee, if any, for each license, the expected fees for the research services to be provided and the cytotoxic agent to be delivered under the arrangement) was allocated to the deliverables based on the relative selling price method as follows: $23.5 million to the development and commercialization licenses; $0.6 million to the rights to future technological improvements, $0.8 million to the sale of cytotoxic agent; and $3.3 million to the research services. Upon execution of the development and commercialization license taken by Lilly in August 2013, the Company recorded $7.8 million of the $23.5 million of the arrangement consideration outlined above, which is included in license and milestone fee revenue for the three month period ended September 30, 2013. With this first development and commercialization license taken, the amount of the total arrangement consideration allocated to future technological improvements will commence to be recognized as revenue ratably over the period the Company is obligated to make available any technological improvements, which is the equivalent to the estimated term of the license. The Company estimates the term of a development and commercialization license to be approximately 25 years, which reflects management s estimate of the time necessary to develop and commercialize therapeutic products pursuant to the license plus the estimated royalty term. The Company will reassess the estimated term at each subsequent reporting period. The Company will recognize as license revenue an equal amount of the total remaining $15.7 million of arrangement consideration allocated to the development and commercialization licenses as each individual license is delivered to Lilly upon Lilly s exercise of its remaining options to such licenses. The Company does not control when Lilly will exercise its options for development and commercialization licenses. As a result, the Company cannot predict when it will recognize the related license revenue except that it will be within the term of the research license. The Company will recognize research services revenue and revenue from the delivery of cytotoxic agents as the related services and cytotoxic agents are delivered.

For additional information related to these agreements, as well as the Company s other significant collaborative agreements, please read Note C, *Agreements* to our consolidated financial statements included within the Company s 2013 Form 10-K.

Kadcyla® is a registered trademark of Genentech, Inc., a member of the Roche Group.

C. Capital Stock

2001 Non-Employee Director Stock Plan

During the three months ended September 30, 2013 and 2012, the Company recorded approximately $3,000 and $14,000 in expense, respectively, related to stock units outstanding under the Company s 2001 Non-Employee Director Stock Plan, or the 2001 Plan. The value of the stock units are classified as a liability and adjusted to market value at each reporting period as the redemption amount of stock units for this plan will be paid in cash. No stock units have been issued under the 2001 Plan subsequent to June 30, 2004.

Table of Contents

Compensation Policy for Non-Employee Directors

During the three months ended September 30, 2013 and 2012, the Company recorded approximately $98,000 and $78,000 in compensation expense, respectively, related to deferred share units issued and outstanding under the Company s Compensation Policy for Non-Employee Directors. Pursuant to the Compensation Policy for Non-Employee Directors, the redemption amount of deferred share units issued will be paid in shares of common stock of the Company on the date a director ceases to be a member of the Board. Annual retainers vest quarterly over approximately one year from the date of grant, contingent upon the individual remaining a director of ImmunoGen as of each vesting date, and the number of deferred share units awarded is based on the market value of the Company s common stock on the date of the award. All unvested deferred stock awards will automatically vest immediately prior to the occurrence of a change of control.

In addition to the deferred share units, the Non-Employee Directors are also entitled to receive stock option awards having a grant date fair value of $30,000, determined using the Black-Scholes option pricing model measured on the date of grant, which would be the date of the annual meeting of shareholders. These options vest quarterly over approximately one year from the date of grant. Any new directors will receive a pro-rated award, depending on their date of election to the Board. The directors received a total of 41,805 and 33,187 options in fiscal 2013 and 2012, respectively, and the related compensation expense for the three months ended September 30, 2013 and 2012 is included in the amounts discussed in the Stock-Based Compensation section of footnote A above.

D. Cash and Cash Equivalents

As of September 30, 2013 and June 30, 2013, the Company held $174.8 million and $195.0 million, respectively, in cash and money market funds consisting principally of U.S. Government-issued securities and high quality, short-term commercial paper which were classified as cash and cash equivalents.

E. Commitments and Contingencies

Leases

Effective July 27, 2007, the Company entered into a lease agreement with Intercontinental Fund III for the rental of approximately 89,000 square feet of laboratory and office space at 830 Winter Street, Waltham, MA. The Company uses this space for its corporate headquarters, research and other operations. The initial term of the lease is for twelve years with an option for the Company to extend the lease for two additional terms of five years. The Company is required to pay certain operating expenses for the leased premises subject to escalation charges for certain expense increases over a base amount. The Company entered into a sublease in December 2009 for 14,100 square feet of this space in Waltham through January 2015, with the sublessee having a conditional option to extend the term for an additional two years.

Effective April 2012, the Company entered into a sublease agreement for the rental of 7,310 square feet of laboratory and office space at 830 Winter Street, Waltham, MA from Histogenics Corporation. The initial term of the sublease is for three years with a conditional option for the

Company to extend the lease through October 2017. The Company is required to pay certain operating expenses for the leased premises subject to escalation charges for certain expense increases over a base amount.

Effective March 2013, the Company entered into a lease agreement for the rental of 43,850 square feet in Norwood, MA through 2018 with an option to extend the lease for an additional term of five years. The Company is required to pay certain operating expenses for the leased premises subject to escalation charges for certain expense increases over a base amount.

Effective April 2013, the Company entered into a lease agreement with River Ridge Limited Partnership for the rental of 7,507 square feet of additional office space at 100 River Ridge Drive, Norwood, MA. The initial term of the lease is for five years and two months commencing in August 2013 with an option for the Company to extend the lease for an additional term of five years. The Company is required to pay certain operating expenses for the leased premises subject to escalation charges for certain expense increases over a base amount.

As of September 30, 2013, the minimum rental commitments for the Company s facilities, including real estate taxes and other expenses, for the next five fiscal years and thereafter under the non-cancelable operating lease agreements discussed above are as follows (in thousands):

Table of Contents

2014 (nine months remaining)	$	5,012
2015		6,780
2016		6,549
2017		6,624
2018		6,831
Thereafter		10,029
Total minimum lease payments	$	41,825
Total minimum rental payments from sublease		(781)
Total minimum lease payments, net	$	41,044

Purchase Obligations

At September 30, 2013, the Company is obligated to a vendor for certain contractual services to be performed in fiscal 2014. Pursuant to the contract, the Company is required to make a $1.2 million payment to the vendor unless the contract is terminated by the Company for cause.

Collaborations

The Company is contractually obligated to make potential future success-based regulatory milestone payments in conjunction with a certain collaborative agreement. These payments are contingent upon the occurrence of certain future events and, given the nature of these events, it is unclear when, if ever, the Company may be required to pay such amounts. Further, the timing of any future payment is not reasonably estimable. As of September 30, 2013, the maximum amount that may be payable in the future under the Company s current collaborative agreement is $2.0 million, $1.4 million of which is reimbursable by a third party under a separate agreement.

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

OVERVIEW

Since our inception, we have been principally engaged in the development of novel, antibody-drug conjugates, or ADCs, for the treatment of cancer using our expertise in cancer biology, monoclonal antibodies, highly potent cytotoxic, or cell-killing, agents, and the design of linkers that enable these agents to remain stably attached to the antibodies while in the blood stream and released in their fully active form after delivery to a cancer cell. An anticancer compound made using our Targeted Antibody Payload, or TAP, technology consists of a monoclonal antibody that binds specifically to an antigen target found on the surface of cancer cells with one of our proprietary cell-killing agents attached to the antibody using one of our engineered linkers. Its antibody component enables a TAP compound to bind to cancer cells that express its target antigen, the highly potent cytotoxic agent serves to kill the cancer cell, and the engineered linker controls the release and activation of the cytotoxic agent inside the cancer cell. With some TAP compounds, the antibody component also has anticancer activity of its own. Our TAP technology is designed to enable the creation of highly effective, well-tolerated anticancer products. All of the TAP compounds currently in clinical testing contain either DM1 or DM4 as the cytotoxic agent. Both DM1 and DM4, collectively DMx, are our proprietary derivatives of a cytotoxic agent called maytansine. We also have expertise in antibodies and cancer biology to develop naked, or non-conjugated, antibody anticancer product candidates.

We have used our proprietary TAP technology in conjunction with our in-house antibody expertise to develop our own anticancer product candidates. We have also entered into collaborative agreements that enable companies to use our TAP technology to develop and commercialize product candidates to specified targets. Under the terms of our collaborative agreements, we are generally entitled to upfront fees, milestone payments and royalties on any commercial product sales. In addition, under certain agreements we are compensated for research and development activities performed at our collaborative partner s request at negotiated prices which are generally consistent with what other third parties would charge. We are compensated to manufacture preclinical and clinical materials and deliver cytotoxic agent at negotiated prices which are generally consistent with what other third parties would charge. Currently, our collaborative partners are Amgen, Bayer HealthCare, Biotest, Lilly, Novartis, Roche and Sanofi. We expect that substantially all of our revenue for the foreseeable future will result from payments under our collaborative arrangements. Details for some of our collaborative agreements with recent activity follow. Details for our other significant agreements can be found in our 2013 Annual Report on Form 10-K

Roche In May 2000, we granted Genentech, now a unit of Roche, an exclusive license to use our maytansinoid TAP technology with antibodies, such as trastuzumab, or other proteins that target HER2. Under the terms of this agreement, Roche has exclusive worldwide rights to develop and commercialize maytansinoid TAP compounds targeting HER2. In February 2013, the US FDA granted marketing approval to the HER2-targeting TAP compound, Kadcyla®. In September 2013, Roche received marketing approval for Kadcyla in Japan. Roche is responsible for the manufacturing, product development and marketing of Kadcyla and any other products resulting from the agreement. We received a $2 million non-refundable upfront payment from Roche upon execution of the agreement. We are also entitled to receive up to a total of $44 million in milestone payments, plus royalties on the commercial sales of Kadcyla and any other resulting products. Total milestones are categorized as follows: development milestones $13.5 million; and regulatory milestones $30.5 million. The marketing approval of Kadcyla in Japan in September 2013 triggered a $5 million regulatory milestone payment to us, which is included in license and milestone fees for the three months ended September 30, 2013. Through September 30, 2013, we have received and recognized $13.5 million and $15.5 million in development and regulatory milestone payments, respectively, related to Kadcyla. We will receive royalty reports and payments related to sales of Kadcyla from Roche one quarter in arrears. In accordance with our revenue recognition policy, $2.1 million of royalties on net sales of Kadcyla for the three-month period ended June 30, 2013 were recorded and included in royalty revenue for the three months ended September 30, 2013.

Novartis   In October 2010, we entered into a three-year right-to-test agreement with Novartis. The agreement provides Novartis with the right to (a) test our TAP technology with individual antibodies selected by Novartis under a right-to-test, or research, license, (b) take exclusive options, with certain restrictions, to individual targets selected by Novartis for specified option periods and (c) upon exercise of those options, take exclusive licenses to use our TAP technology to develop and commercialize products for a specified number of individual targets on terms agreed upon at the inception of the right-to-test agreement. The initial three-year term of the right-to-test agreement was extended by Novartis in October 2013 for an additional one-year period by payment of a $5 million fee. In addition to the one-year extension taken in October 2013, the terms of the right-to-test agreement allow Novartis to extend the research term for one additional one-year period by payment of additional consideration. The terms of the right-to-test agreement require Novartis to exercise its options for the development and commercialization licenses by the end of the term of the research license. We received a $45 million upfront payment in connection with the execution of the right-to-test agreement, and for each development and commercialization license for a specific target, we are entitled to receive an exercise fee of $1 million and up to a total of $199.5 million in milestone payments, plus royalties on the commercial sales of any resulting products. The total milestones are categorized as follows: development milestones $22.5 million; regulatory milestones $77 million; and sales milestones $100 million.

Effective March 29, 2013, we and Novartis amended the right-to-test agreement so that Novartis can take a license to develop and commercialize products directed at two pre-defined and related undisclosed targets, one target licensed on an exclusive basis and the other target initially licensed on a non-exclusive basis. The target licensed on a non-exclusive basis may be converted to an exclusive target by notice and payment to us of an agreed-upon fee of at least $5 million, depending on specific circumstances. We received a $3.5 million fee in connection with the execution of the amendment to the agreement. We may be required to credit this fee against future milestone payments if Novartis discontinues the development of a specified product under certain circumstances.

In connection with the amendment, on March 29, 2013, Novartis took the license referenced above under the right-to-test agreement, as amended, enabling it to develop and commercialize products directed at the two targets. We received a $1 million upfront fee with the execution of this license. Additionally, the execution of this license provides us the opportunity to receive milestone payments totaling $199.5 million (development milestones $22.5 million; regulatory milestones $77 million; and sales milestones $100 million) or $238 million (development milestones $22.5 million; regulatory milestones $115.5 million; and sales milestones $100 million), depending on the composition of any resulting products. Novartis also has the right to convert the noted non-exclusive license to an exclusive license, in which case we would be entitled to receive a conversion fee and, depending on the composition of resultant products, an upward adjustment on milestone payments. In October 2013, Novartis took a second exclusive license to a single target, triggering a $1 million payment to us and the opportunity to receive milestone payments totaling $199.5 million, as outlined above. Additionally, under the license agreements, we are entitled to receive royalties on product sales, if any.

Lilly In December 2011, we entered into a three-year right-to-test agreement with Lilly. The agreement provides Lilly with the right to (a) take exclusive options, with certain restrictions, to individual targets selected by Lilly for specified option periods, (b) test our maytansinoid TAP technology with Lilly s antibodies directed to the optioned targets under a right-to-test, or research, license, and (c) upon exercise of those options, take exclusive licenses to use our maytansinoid TAP technology to develop and commercialize products for a specified number of individual targets on terms agreed upon at the inception of the right-to-test agreement. The terms of the right-to-test agreement require Lilly to exercise its options for the development and commercialization licenses by the end of the term of the research license.

We received a $20 million upfront payment in connection with the execution of the right-to-test agreement, and for the first development and commercialization license taken, which occurred in August 2013, we are entitled to receive up to a total of $200.5 million in milestone payments, plus royalties on the commercial sales of any resulting products. For each subsequent

Table of Contents

development and commercialization license taken, we are entitled to receive an exercise fee in the amount of $2 million and up to a total of $199 million in milestone payments, plus royalties on the commercial sales of any resulting products. The total milestones are categorized as follows: development milestones $30.5 million for the first development and commercialization license and $29 million for each subsequent license; regulatory milestones $70 million; and sales milestones $100 million. In accordance with our revenue recognition policy, upon execution of the development and commercialization license taken by Lilly in August 2013, we recorded $7.8 million of revenue which is included in license and milestone fee revenue for the three months ended September 30, 2013.

To date, we have not generated revenues from our proprietary commercial product sales and we expect to incur significant operating losses for the foreseeable future. As of September 30, 2013, we had approximately $174.8 million in cash and cash equivalents compared to $195.0 million in cash and cash equivalents as of June 30, 2013.

We anticipate that future cash expenditures will be partially offset by collaboration-derived proceeds, including milestone payments, royalties and upfront fees. Accordingly, period-to-period operating results may fluctuate dramatically based upon the timing of receipt of the proceeds. We believe that our established collaboration agreements, while subject to specified milestone achievements, will provide funding to assist us in meeting obligations under our collaborative agreements while also providing funding for the development of internal product candidates and technologies. However, we can give no assurances that such collaborative agreement funding will, in fact, be realized in the time frames we expect, or at all. Should we or our partners not meet some or all of the terms and conditions of our various collaboration agreements, we may be required to pursue additional strategic partners, secure alternative financing arrangements, and/or defer or limit some or all of our research, development and/or clinical projects. However, we cannot provide assurance that any such opportunities presented by additional strategic partners or alternative financing arrangements will be entirely available to us, if at all.

Critical Accounting Policies

We prepare our consolidated financial statements in accordance with accounting principles generally accepted in the U.S. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to our collaborative agreements, inventory and stock-based compensation. We base our estimates on historical experience and various other assumptions that we believe to be reasonable under the circumstances. Actual results may differ from these estimates.

There were no significant changes to our critical accounting policies from those disclosed in our Annual Report on Form 10-K for the fiscal year ended June 30, 2013.

RESULTS OF OPERATIONS

Comparison of Three Months ended September 30, 2013 and 2012

Revenues

Our total revenues for the three months ended September 30, 2013 and 2012 were $17.2 million and $4.1 million, respectively. The $13.1 million increase in revenues in the three months ended September 30, 2013 from the same period in the prior year is attributable to an increase in license and milestone fees, research and development support revenue and royalty revenue, partially offset by a decrease in clinical materials revenue, all of which are discussed below.

Revenues from license and milestone fees for the three months ended September 30, 2013 increased $12.2 million to $13.2 million from $933,000 in the same period ended September 30, 2012. Included in license and milestone fees for the three months ended September 30, 2013 is a $5 million regulatory milestone achieved under our collaboration agreement with Roche and $7.8 million of license revenue earned upon the execution of a development and commercialization license by Lilly. The amount of license and milestone fees we earn is directly related to the number of our collaborators, the collaborators advancement of the product candidates, and the overall success in the clinical trials of the product candidates. As such, the amount of license and milestone fees may vary significantly from quarter to quarter and year to year. Total revenue from license and milestone fees recognized from each of our collaborative partners in the three-month periods ended September 30, 2013 and 2012 is included in the following table (in thousands):

Table of Contents

License and Milestone Fees	Three Months Ended September 30, 2013		2012	
Collaborative Partner:				
Amgen	$	115	$	239
Bayer HealthCare				521
Biotest		6		6
Lilly		7,813		
Novartis		41		
Sanofi		192		167
Roche		5,000		
Total	$	13,167	$	933

Deferred revenue of $57.5 million as of September 30, 2013 primarily represents payments received from our collaborators pursuant to our license agreements, which we have yet to earn pursuant to our revenue recognition policy.

Research and development support revenue was $2.0 million for the three months ended September 30, 2013 compared with $1.4 million for the three months ended September 30, 2012. These amounts primarily represent research funding earned based on actual resources utilized under our agreements with our collaborators shown in the table below. Also included in research and development support revenue are fees for developing antibody-specific conjugation processes on behalf of our collaborators and potential collaborators during the early evaluation and preclinical testing stages of drug development. The amount of research and development support revenue we earn is directly related to the number of our collaborators and potential collaborators, the stage of development of our collaborators product candidates and the resources our collaborators allocate to the development effort. As such, the amount of research and development support revenue may vary widely from quarter to quarter and year to year. Total revenue recognized from research and development support from each of our collaborative partners in the three-month periods ended September 30, 2013 and 2012 is included in the following table (in thousands):

Research and Development Support	Three Months Ended September 30, 2013		2012	
Collaborative Partner:				
Amgen	$	66	$	85
Biotest		239		115
Lilly		528		223
Novartis		1,155		947
Other		2		7
Total	$	1,990	$	1,377

Clinical materials revenue decreased $1.8 million in the three months ended September 30, 2013 to $8,000 from $1.8 million in the three months ended September 30, 2012. We are compensated at negotiated prices which are generally consistent with what other third-parties would charge. The amount of clinical materials revenue we earn, and the related cost of clinical materials charged to research and development expense, is directly related to the number of clinical trials our collaborators who use us to manufacture clinical materials are preparing or have underway, the speed of enrollment in those trials, the dosage schedule of each clinical trial and the time period, if any, during which patients in the trial receive clinical benefit from the clinical materials, and the demand our collaborators have for clinical-grade material for process development and analytical purposes. As such, the amount of clinical materials revenue and the related cost of clinical materials charged to research and development expense may vary significantly from quarter to quarter and year to year.

In February 2013, the U.S. FDA granted marketing approval to Kadcyla, a product resulting from one of our development and commercialization licenses with Roche, through its Genentech unit. We receive royalty reports and payments related to sales of Kadcyla from Roche one quarter in arrears. In accordance with our revenue recognition policy, $2.1 million of royalties on net sales of Kadcyla for the

three-month period ended June 30, 2013 were recorded and included in royalty revenue for the three months ended September 30, 2013. No royalty revenue was recorded in the three months ended September 30, 2012. We expect royalty revenue to increase in future periods as the underlying net sales of Kadcyla increase.

Research and Development Expenses

Our research and development expenses relate to (i) research to evaluate new targets and to develop and evaluate new antibodies, linkers and cytotoxic agents, (ii) preclinical testing of our own and, in certain instances, our collaborators product candidates, and the cost of our own clinical trials, (iii) development related to clinical and commercial manufacturing processes and (iv) manufacturing operations which also includes raw materials.

Table of Contents

Research and development expense for the three months ended September 30, 2013 decreased $1.7 million to $22.0 million from $23.7 million for the three months ended September 30, 2012. The decrease was primarily due to decreased costs for third-party production of antibody and costs to fill conjugated material for use in clinical materials due to timing, as well as a decrease in cost of clinical materials revenue due to timing of orders of such clinical materials from our partners and lower amounts of DMx written off as excess. Partially offsetting these decreases, salaries and related expenses increased due to additional headcount, increased incentive compensation and increased stock compensation costs. The number of our research and development personnel increased to 247 as of September 30, 2013 compared to 216 at September 30, 2012. The higher stock compensation is driven by higher stock prices and increases in the number the number of options granted due to increases in personnel. A more detailed discussion of research and development expense in the period follows.

We are unable to accurately estimate which potential product candidates, if any, will eventually move into our internal preclinical research program. We are unable to reliably estimate the costs to develop these products as a result of the uncertainties related to discovery research efforts as well as preclinical and clinical testing. Our decision to move a product candidate into the clinical development phase is predicated upon the results of preclinical tests. We cannot accurately predict which, if any, of the discovery stage product candidates will advance from preclinical testing and move into our internal clinical development program. The clinical trial and regulatory approval processes for our product candidates that have advanced or that we intend to advance to clinical testing are lengthy, expensive and uncertain in both timing and outcome. As a result, the pace and timing of the clinical development of our product candidates is highly uncertain and may not ever result in approved products. Completion dates and development costs will vary significantly for each product candidate and are difficult to predict. A variety of factors, many of which are outside our control, could cause or contribute to the prevention or delay of the successful completion of our clinical trials, or delay or prevent our obtaining necessary regulatory approvals. The costs to take a product through clinical trials are dependent upon, among other factors, the clinical indications, the timing, size and design of each clinical trial, the number of patients enrolled in each trial, and the speed at which patients are enrolled and treated. Product candidates may be found to be ineffective or to cause unacceptable side effects during clinical trials, may take longer to progress through clinical trials than anticipated, may fail to receive necessary regulatory approvals or may prove impractical to manufacture in commercial quantities at reasonable cost or with acceptable quality.

The lengthy process of securing FDA approvals for new drugs requires the expenditure of substantial resources. Any failure by us to obtain, or any delay in obtaining regulatory approvals would materially adversely affect our product development efforts and our business overall. Accordingly, we cannot currently estimate, with any degree of certainty, the amount of time or money that we will be required to expend in the future on our product candidates prior to their regulatory approval, if such approval is ever granted. As a result of these uncertainties surrounding the timing and outcome of our clinical trials, we are currently unable to estimate when, if ever, our product candidates that have advanced into clinical testing will generate revenues and cash flows.

We do not track our research and development costs by project. Since we use our research and development resources across multiple research and development projects, we manage our research and development expenses within each of the categories listed in the following table and described in more detail below (in thousands):

	Three Months Ended September 30,	
Research and Development Expense	**2013**	**2012**
Research	$ 4,558	$ 4,309
Preclinical and Clinical Testing	8,612	6,851
Process and Product Development	2,038	1,962
Manufacturing Operations	6,821	10,578
Total Research and Development Expense	$ 22,029	$ 23,700

Research: Research includes expenses primarily associated with activities to identify and evaluate new targets and to develop and evaluate new antibodies, linkers and cytotoxic agents for our products and in support of our collaborators. Such expenses primarily include personnel, contract services, facilities and lab supplies. Research expenses for the three months ended September 30, 2013 increased $249,000 compared to the three

months ended September 30, 2012. This increase is primarily the result of an increase in salaries and related expenses. We expect research expenses for fiscal 2014 to be marginally higher than fiscal 2013.

Preclinical and Clinical Testing: Preclinical and clinical testing includes expenses related to preclinical testing of our own and, in certain instances, our collaborators product candidates, regulatory activities, and the cost of our own clinical trials. Such expenses include personnel, patient enrollment at our clinical testing sites, consultant fees, contract services, and facility expenses. Preclinical and clinical testing expenses for the three months ended September 30, 2013 increased $1.7 million to $8.6 million compared to $6.9 million for the three months ended September 30, 2012. This increase is primarily the result of higher salaries and related expenses and an increase in clinical trial costs due primarily to additional sites participating and higher patient enrollment for the IMGN901 007 Phase II study for small-cell lung cancer, as well as start-up costs incurred for the IMGN289 Phase I trial for treatment of EGFR-positive tumors. We expect preclinical and clinical testing expenses for fiscal 2014 to be significantly higher than fiscal 2013 due to increased activities to advance our wholly owned product candidates.

Table of Contents

Process and Product Development: Process and product development expenses include costs for development of clinical and commercial manufacturing processes for our own and collaborator compounds. Such expenses include the costs of personnel, contract services and facility expenses. For the three months ended September 30, 2013, total development expenses increased $76,000 compared to the three months ended September 30, 2012. This increase is primarily the result of an increase in salaries and related expenses. We expect process and product development expenses for fiscal 2014 to be marginally higher than fiscal 2013.

Manufacturing Operations: Manufacturing operations expense includes costs to manufacture preclinical and clinical materials for our own and our collaborator s product candidates, and quality control and quality assurance activities and costs to support the operation and maintenance of our conjugate manufacturing facility. Such expenses include personnel, raw materials for our and our collaborators preclinical studies and clinical trials, development costs with contract manufacturing organizations, manufacturing supplies, and facilities expense. For the three months ended September 30, 2013, manufacturing operations expense decreased $3.8 million to $6.8 million compared to $10.6 million in the same period last year. The decrease in the three months ended September 30, 2013 as compared to the three months ended September 30, 2012 is primarily the result of (i) a decrease in antibody development and supply expense driven primarily by timing of supply required for our IMGN853 program and timing of pivotal activities for our IMGN901 program; (ii) a decrease in cost of clinical materials revenue due to timing of orders of such clinical materials from our partners and lower amounts of DMx written off as excess; (iii) a decrease in fill/finish costs due primarily to costs to transfer our internal programs to a new supplier during the prior year period; and (iv) an increase in costs capitalized into inventory due to a greater number of manufactured batches of conjugated materials on behalf of our collaborators. Partially offsetting these decreases, salaries and related expenses increased during the current period. We expect manufacturing operations expense for fiscal 2014 to be significantly higher than fiscal 2013 due primarily to increased activities to advance our wholly owned product candidates.

General and Administrative Expenses

General and administrative expenses for the three months ended September 30, 2013 increased $887,000 from the three months ended September 30, 2012. This increase is primarily due to an increase in salaries and related expenses, including severance expense related to the departure of the CFO, as well as an increase in professional service fees, particularly patent expenses and consulting fees. We expect general and administrative expenses for fiscal 2014 to be marginally higher than fiscal 2013.

Other Income, net

Other income, net for the three months ended September 30, 2013 and 2012 is included in the following table (in thousands):

	Three Months Ended September 30,			
Other Income, net		**2013**		**2012**
Interest Income	$	11	$	46
Other Income, net		100		10
Total Other Income, net	$	111	$	56

LIQUIDITY AND CAPITAL RESOURCES

	As of	
	September 30, 2013	June 30, 2013
	(In thousands)	
Cash and cash equivalents	$ 174,838	$ 194,960
Working capital	171,195	181,511
Shareholders equity	119,441	121,847

	Three Months Ended September 30,	
	2013	2012
	(In thousands)	
Cash used for operating activities	$ (23,575)	$ (21,006)
Cash used for investing activities	(572)	(1,012)
Cash provided by financing activities	4,025	94,694

Cash Flows

We require cash to fund our operating expenses, including the advancement of our own clinical programs, and to make capital expenditures. Historically, we have funded our cash requirements primarily through equity financings in public markets and payments from our collaborators, including equity investments, license fees, milestones and research funding. As of September 30, 2013, we had approximately $174.8 million in cash and cash equivalents. Net cash used for operations was $23.6 million and $21.0 million for the three months ended September 30, 2013 and 2012, respectively. The principal use of cash in operating activities for all periods presented was to fund our net loss.

Net cash used for investing activities was $572,000 and $1.0 million for the three months ended September 30, 2013 and 2012, respectively, and primarily represents cash outflows for capital expenditures. Capital expenditures, primarily for the purchase of new equipment and leasehold improvements, were $572,000 and $966,000 for the three-month periods ended September 30, 2013 and 2012, respectively.

Net cash provided by financing activities was $4.0 million and $94.7 million for the three months ended September 30, 2013 and 2012, respectively, which represents proceeds from the exercise of approximately 545,000 and 108,000 stock options, respectively. Also, pursuant to a public offering in the prior year period, we issued and sold 6,250,000 shares of our common stock resulting in net proceeds of $94.0 million.

We anticipate that our current capital resources and expected future collaborator payments under existing collaborations will enable us to meet our operational expenses and capital expenditures through fiscal year 2015. However, we cannot provide assurance that such future collaborative agreement funding will, in fact, be received. Should we or our partners not meet some or all of the terms and conditions of our various collaboration agreements, we may be required to pursue additional strategic partners, secure alternative financing arrangements, and/or defer or limit some or all of our research, development and/or clinical projects.

Contractual Obligations

The Company is obligated to a vendor for certain contractual services to be performed in fiscal 2014. Pursuant to the contract, the Company is required to make a $1.2 million payment to the vendor unless the contract is terminated by the Company for cause. There have been no other material changes to our contractual obligations during the current period from those disclosed in our Annual Report on Form 10-K for the fiscal year ended June 30, 2013.

Recent Accounting Pronouncements

In July 2013, the FASB issued guidance to address the diversity in practice related to the financial statement presentation of unrecognized tax benefits as either a reduction of a deferred tax asset or a liability when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. This guidance is effective prospectively for fiscal years, and interim periods within those years, beginning after December 15, 2013. The adoption of this guidance is not expected to have a material impact on our consolidated financial statements.

Forward-Looking Statements

This quarterly report includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements relate to analyses and other information which are based on forecasts of future results and estimates of amounts that are not yet determinable. These statements also relate to our future prospects, developments and business strategies.

These forward-looking statements can be identified by their use of terms and phrases, such as anticipate, believe, could, estimate, expect, i may, plan, predict, project, will and other similar terms and phrases, including references to assumptions. They may also use words such as would, should, could or may . These forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results to be materially different from those contemplated by our forward-looking statements. These known and unknown risks, uncertainties and other factors are described in detail in the Risk Factors section and in other sections of this Annual Report on Form 10-K for the year ended June 30, 2013. We disclaim any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

OFF-BALANCE SHEET ARRANGEMENTS

None.

ITEM 3. ***Quantitative and Qualitative Disclosure about Market Risk***

Our market risks, and the ways we manage them, are summarized in Part II, Item 7A, Quantitative and Qualitative Disclosures About Market Risk of our Annual Report on Form 10-K for the fiscal year ended June 30, 2013. Since then there have been no material changes to our market risks or to our management of such risks.

Table of Contents

ITEM 4. ***Controls and Procedures***

(a) *Disclosure Controls and Procedures*

The Company s management, with the participation of its principal executive officer and principal financial officer, has evaluated the effectiveness of the Company s disclosure controls and procedures (as defined in Rules 13a-15(e) or 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on such evaluation, the Company s principal executive officer and principal financial officer have concluded that, as of the end of such period, the Company s disclosure controls and procedures were adequate and effective.

(b) *Changes in Internal Controls*

There have not been any changes in the Company s internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended September 30, 2013 that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

Table of Contents

PART II. OTHER INFORMATION

ITEM 1A. *Risk Factors*

You should carefully review and consider the information regarding certain factors that could materially affect our business, financial condition or future results set forth under Item 1A. (Risk Factors) in our Annual Report on Form 10-K for the fiscal year ended June 30, 2013. There have been no material changes from the factors disclosed in our 2013 Annual Report on Form 10-K, although we may disclose changes to such factors or disclose additional factors from time to time in our future filings with the Securities and Exchange Commission.

ITEM 6. *Exhibits*

Exhibit No.	Description
10.1	Transition and Separation Agreement dated as of September 13, 2013 between the Registrant and Gregory D. Perry
31.1	Certification of Principal Executive Officer under Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Principal Financial Officer under Section 302 of the Sarbanes-Oxley Act of 2002.

We capitalize costs directly related to the successful origination of a lease. These costs include leasing commissions paid to third parties for new leases or lease renewals, as well as an allocation of compensation costs, including payroll, bonus and non-cash equity compensation of employees who spend time on lease

origination activities. In determining the amount of compensation costs to be capitalized for these employees, allocations are made based on estimates of the actual amount of time spent working on successful leases in comparison to time spent on unsuccessful origination efforts. We capitalized compensation costs for these employees of $0.3 million and $0.3 million during the three months ended September 30, 2018 and 2017, respectively, and $0.7 million and $0.8 million during the nine months ended September 30, 2018 and 2017, respectively.

Impairment of Long-Lived Assets

In accordance with the provisions of the Impairment or Disposal of Long-Lived Assets Subsections of ASC Topic 360: Property, Plant, and Equipment, we assess the carrying values of our respective long-lived assets, including goodwill, whenever events or changes in circumstances indicate that the carrying amounts of these assets may not be fully recoverable.

Recoverability of real estate assets is measured by comparison of the carrying amount of the asset to the estimated future undiscounted cash flows. In order to review real estate assets for recoverability, we consider current market conditions as well as our intent with respect to holding or disposing of the asset. The intent with regards to the underlying assets might change as market conditions and other factors change. Fair value is determined through various valuation techniques; including discounted cash flow models, applying a capitalization rate to estimated net operating income of a property, quoted market values and third-party appraisals, where considered necessary. The use of projected future cash flows is based on assumptions that are consistent with estimates of future expectations and the strategic plan used to manage our underlying business. If our analysis indicates that the carrying value of the real estate asset is not recoverable on an undiscounted cash flow basis, we will recognize an impairment charge for the amount by which the carrying value exceeds the current estimated fair value of the real estate property.
Assumptions and estimates used in the recoverability analyses for future cash flows, discount rates and capitalization rates are complex and subjective. Changes in economic and operating conditions or our intent with respect to our investment that occur subsequent to our impairment analyses could impact these assumptions and result in future impairment of our real estate properties.

Investment in Unconsolidated Real Estate Entities

Investment in unconsolidated real estate entities in which we have the ability to exercise significant influence (but not control) are accounted for under the equity method of investment. Under the equity method, we initially record our investment at cost, and subsequently adjust for equity in earnings or losses and cash contributions and distributions. Any difference between the carrying amount of these investments on the balance sheet and the underlying equity in net assets is amortized as an adjustment to equity in income (loss) from unconsolidated real estate entities over the life of the related asset. Under the equity method of accounting, our net equity investment is reflected within the consolidated balance sheets, and our share of net income or loss from the joint venture is included within the consolidated statements of operations. Furthermore, distributions received from equity method investments are classified as either operating cash inflows or investing cash inflows in the consolidated statements of cash flows using the “nature of the distribution approach,” in which each distribution is evaluated on the basis of the source of the payment.

Income Taxes

We have elected to be taxed as a REIT under the Internal Revenue Code of 1986, as amended (the “Code”) commencing with our initial taxable year ended December 31, 2013. To qualify as a REIT, we are required (among other things) to distribute at least 90% of our REIT taxable income to our stockholders and meet the various other requirements imposed by the Code relating to matters such as operating results, asset holdings, distribution levels and diversity of stock ownership. Provided we qualify for taxation as a REIT, we are generally not subject to corporate-level income tax on the

earnings distributed currently to our stockholders. If we fail to qualify as a REIT in any taxable year, and were unable to avail ourselves of certain savings provisions set forth in the Code, all of our taxable income would be subject to federal income tax at regular corporate rates, including any applicable alternative minimum tax.

In addition, we are subject to taxation by various state and local jurisdictions, including those in which we transact business or reside. Our non-taxable REIT subsidiaries, including our Operating Partnership, are either partnerships or disregarded entities for federal income tax purposes. Under applicable federal and state income tax rules, the allocated share of net income or loss from disregarded entities and flow-through entities such as partnerships is reportable in the income tax returns of the respective equity holders. Accordingly, no income tax provision is included in the accompanying consolidated financial statements for the nine months ended September 30, 2018 and 2017.

We periodically evaluate our tax positions to determine whether it is more likely than not that such positions would be sustained upon examination by a tax authority for all open tax years, as defined by the statute of limitations, based on their technical merits. As of September 30, 2018, and December 31, 2017, we have not established a liability for uncertain tax positions.

Derivative Instruments and Hedging Activities

FASB ASC Topic 815: Derivatives and Hedging (“ASC 815”), provides the disclosure requirements for derivatives and hedging activities with the intent to provide users of financial statements with an enhanced understanding of: (a) how and why an entity uses derivative instruments, (b) how the entity accounts for derivative instruments and related hedged items, and (c) how derivative instruments and related hedged items affect an entity’s financial position, financial performance, and cash flows. Further, qualitative disclosures are required that explain the Company’s objectives and strategies for using derivatives, as well as quantitative disclosures about the fair value of and gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative instruments.

As required by ASC 815, we record all derivatives on the balance sheet at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative, and whether we have elected to designate a derivative in a hedging relationship and apply hedge accounting and whether the hedging relationship has satisfied the criteria necessary to apply hedge accounting. Derivatives designated and qualifying as a hedge of the exposure to changes in the fair value of an asset, liability, or firm commitment attributable to a particular risk, such as interest rate risk, are considered fair value hedges. Derivatives designated and qualifying as a hedge of the exposure to variability in expected future cash flows, or other types of forecasted transactions, are considered cash flow hedges. Hedge accounting generally provides for the matching of the timing of gain or loss recognition on the hedging instrument with the recognition of the changes in the fair value of the hedged asset or liability that are attributable to the hedged risk in a fair value hedge or the earnings effect of the hedged forecasted transactions in a cash flow hedge. We may enter into derivative contracts that are intended to economically hedge certain risks, even though hedge accounting does not apply or we elect not to apply hedge accounting. See Note 7.

Revenue Recognition

Our primary sources of revenue are rental income, tenant reimbursements, other income, management, leasing and development services and gains on sale of real estate.

Rental Income

Minimum annual rental revenues are recognized in rental income on a straight-line basis over the term of the related lease, regardless of when payments are contractually due. Rental revenue recognition commences when the tenant takes possession or controls the physical use of the leased space. Lease termination fees, which are included in rental income, are recognized when the related lease is canceled and we have no continuing obligation to provide services to such former tenant.

Tenant Reimbursements

Our lease agreements with tenants generally contain provisions that require tenants to reimburse us for certain property expenses. Estimated reimbursements from tenants for real estate taxes, common area maintenance and other recoverable operating expenses are recognized as revenues in the period that the expenses are incurred. Subsequent to year-end, we perform final reconciliations on a lease-by-lease basis and bill or credit each tenant for any cumulative annual adjustments.

Other Income

Other income primarily consists of late payment fees and other miscellaneous tenant related revenues.

Management, leasing and development services

14

We provide property management services and leasing services to related party and third-party property owners, the customer, in exchange for fees and commissions. Property management services include performing property inspections, monitoring repairs and maintenance, negotiating vendor contracts, maintaining tenant relations and providing financial and accounting oversight. For these services, we earn monthly management fees, which are based on a fixed percentage of each managed property's monthly tenant cash receipts. We have determined that control over the services is passed to the customer simultaneously as performance occurs. Accordingly, management fee revenue is earned as the services are provided to our customers.

Leasing commissions are earned when we provide leasing services that result in an executed lease with a tenant. We have determined that control over the services is transferred to the customer upon execution of each lease agreement. We earn leasing commissions based on a fixed percentage of rental income generated for each executed lease agreement and there is no variable income component.

Gain or Loss on Sale of Real Estate

We account for dispositions of real estate properties, which are considered nonfinancial assets, in accordance with ASC 610-20: Other Income—Gains and Losses from the Derecognition of Nonfinancial Assets and recognize a gain or loss on sale of real estate upon transferring control of the nonfinancial asset to the purchaser, which is generally satisfied at the time of sale. If we were to conduct a partial sale of real estate by transferring a controlling interest in a nonfinancial asset, while retaining a noncontrolling ownership interest, we would measure any noncontrolling interest received or retained at fair value, and recognize a full gain or loss. If we receive consideration before transferring control of a nonfinancial asset, we recognize a contract liability. If we transfer control of the asset before consideration is received, we recognize a contract asset.

Valuation of Receivables

We may be subject to tenant defaults and bankruptcies that could affect the collection of outstanding receivables. In order to mitigate these risks, we perform credit reviews and analyses on prospective tenants before significant leases are executed and on existing tenants before properties are acquired. We specifically analyze aged receivables, customer credit-worthiness, historical bad debts and current economic trends when evaluating the adequacy of the allowance for doubtful accounts. As a result of our periodic analysis, we maintain an allowance for estimated losses that may result from the inability of our tenants to make required payments. This estimate requires significant judgment related to the lessees' ability to fulfill their obligations under the leases. We believe our allowance for doubtful accounts is adequate for our outstanding receivables for the periods presented. If a tenant is insolvent or files for bankruptcy protection and fails to make contractual payments beyond any allowance, we may recognize additional bad debt expense in future periods equal to the net outstanding balances, which include amounts recognized as straight-line revenue not realizable until future periods.

Rents and other receivables, net and deferred rent receivable, net consisted of the following as of September 30, 2018 and December 31, 2017 (in thousands):

	September 30, 2018	December 31, 2017
Rents and other receivables	$ 6,882	$ 5,369
Allowance for doubtful accounts	(1,840)	(1,705)
Rents and other receivables, net	$ 5,042	$ 3,664
Deferred rent receivable	$ 20,877	$ 15,912
Allowance for doubtful accounts	(107)	(86)
Deferred rent receivable, net	$ 20,770	$ 15,826

We recorded the following provision for doubtful accounts, including amounts related to deferred rents, as a reduction to rental revenues in our consolidated statements of operations for the three and nine months ended September 30, 2018 and 2017 (in thousands):

15

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Provision for doubtful accounts	$481	$231	$824	$897

Equity Based Compensation

We account for equity based compensation in accordance with ASC Topic 718 Compensation - Stock Compensation. Total compensation cost for all share-based awards is based on the estimated fair market value on the grant date. For share-based awards that vest based solely on a service condition, we recognize compensation cost on a straight-line basis over the total requisite service period for the entire award. For share-based awards that vest based on a market or performance condition, we recognize compensation cost on a straight-line basis over the requisite service period of each separately vesting tranche. Forfeitures are recognized in the period in which they occur. See Note 12.

Equity Offering Costs

Underwriting commissions and offering costs related to our common stock issuances have been reflected as a reduction of additional paid-in capital. Underwriting commissions and offering costs related to our preferred stock issuances have been reflected as a direct reduction of the preferred stock balance.

Earnings Per Share

We calculate earnings per share (“EPS”) in accordance with ASC 260 - Earnings Per Share (“ASC 260”). Under ASC 260, nonvested share-based payment awards that contain non-forfeitable rights to dividends are participating securities and, therefore, are included in the computation of basic EPS pursuant to the two-class method. The two-class method determines EPS for each class of common stock and participating securities according to dividends declared (or accumulated) and their respective participation rights in undistributed earnings.

Basic EPS is calculated by dividing the net income (loss) attributable to common stockholders by the weighted average number of shares of common stock outstanding for the period.

Diluted EPS is calculated by dividing the net income (loss) attributable to common stockholders by the weighted average number of shares of common stock outstanding determined for the basic EPS computation plus the effect of any dilutive securities. We include unvested shares of restricted stock and unvested LTIP units in the computation of diluted EPS by using the more dilutive of the two-class method or treasury stock method. We include unvested performance units as contingently issuable shares in the computation of diluted EPS once the market criteria are met, assuming that the end of the reporting period is the end of the contingency period. Any anti-dilutive securities are excluded from the diluted EPS calculation. See Note 13.

Segment Reporting

Management views the Company as a single reportable segment based on its method of internal reporting in addition to its allocation of capital and resources.

Adoption of New Accounting Pronouncements

Revenue Recognition

On May 28, 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606), and subsequently issued additional ASUs which provide practical expedients, technical corrections and clarification of the new standard (collectively “ASC 606”). ASC 606 establishes principles for reporting the nature, amount, timing and uncertainty of revenues and cash flows arising from an entity’s contracts with customers. The core principle of the new standard is that an entity recognizes revenue to represent the transfer of 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. Effective January 1, 2018, we adopted ASC 606 using the modified retrospective approach. We evaluated each of our revenue streams to determine the sources of revenue that are impacted by ASC 606 and concluded that management services and leasing services fall within the scope of ASC 606. We evaluated the impact of ASC 606 on the timing and pattern of

16

revenue recognition for our management and leasing services contracts and determined there was no change in the timing or pattern of revenue recognition for these contracts as compared to prior accounting practice. Accordingly, the adoption of ASC 606 did not have an impact on our consolidated financial statements. See “Revenue Recognition” above for further details.

Derecognition of Non-Financial Assets

On February 22, 2017, the FASB issued ASU 2017-05, Other Income - Gains and Losses from the Derecognition of Nonfinancial Assets (Subtopic 610-20): Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets (“ASU 2017-05). ASU 2017-05 clarifies the scope of asset derecognition and adds further guidance for recognizing gains and losses from the transfer of nonfinancial assets in contracts with non-customers. Effective January 1, 2018, we adopted ASU 2017-05 using the modified retrospective approach. There was no cumulative effect adjustment recorded to retained earnings as of January 1, 2018 as a result of the adoption of ASU 2017-05.

Derivatives

On August 28, 2017, the FASB issued ASU 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities (“ASU 2017-12”). ASU 2017-12 simplifies hedge accounting by eliminating the requirement to separately measure and report hedge ineffectiveness and generally requires the entire change in the fair value of a hedging instrument to be presented in the same income statement line as the hedged item. For cash flow hedges, ASU 2017-12 requires all changes in the fair value of the hedging instrument to be deferred in other comprehensive income and recognized in earnings at the same time that the hedged item affects earnings. ASU 2017-12 also eases certain documentation and assessment requirements and modifies the accounting for components excluded from the assessment of hedge effectiveness. ASU 2017-12 is effective for interim and annual reporting periods beginning after December 15, 2018, with early adoption permitted. Effective January 1, 2018, we early adopted ASU 2017-12 using the modified retrospective approach. We did not record a cumulative effect adjustment to eliminate ineffectiveness amounts as we did not have any ineffectiveness in our historical consolidated financial statements. In addition, certain provisions of ASU 2017-12 require modifications to existing presentation and disclosure requirements on a prospective basis. See Note 7 for disclosures relating to our derivative instruments.

Stock Compensation

On May 10, 2017, the FASB issued ASU 2017-09, Compensation-Stock Compensation (Topic 718): Scope of Modification Accounting (“ASU 2017-09”), which clarifies the scope of modification accounting for share-based compensation arrangements by providing guidance on the types of changes to the terms and conditions of share-based compensation awards to which an entity would be required to apply modification accounting under ASC 718. ASU 2017-09 is effective for annual periods beginning after December 15, 2017, with early adoption permitted. Effective January 1, 2018, we early adopted ASU 2017-09. There was no change to our consolidated financial statements or notes to our consolidated financial statements as a result of the adoption of ASU 2017-09.

Recently Issued Accounting Pronouncements

Changes to GAAP are established by the FASB in the form of ASUs to the FASB’s Accounting Standards Codification. We consider the applicability and impact of all ASUs.

Leases

On February 25, 2016, the FASB issued ASU 2016-02, Leases (“ASC 842”), which sets out the principals for the recognition, measurement, presentation and disclosure of leases for both lessees and lessors.

ASC 842 requires lessees to recognize the following for all leases (with the exception of short-term leases) at the commencement date: (1) a lease liability, which is a lessee’s obligation to make lease payments arising from a lease, measured on a discounted basis; and (2) a right-of-use asset, which is an asset that represents the lessee’s right to use, or control the use of, a specified asset for the lease term. ASC 842 also requires lessees to classify leases as either finance or operating leases based on whether or not the lease is effectively a financed purchase of the leased asset by the lessee. This classification is used to evaluate whether the lease expense should be recognized based on an effective interest method or on a straight-line basis over the term of the lease. As of September 30, 2018, we are the lessee on one ground lease and multiple office space leases. Upon the adoption of ASC 842, we will be required to record a lease liability and a right-of-use asset for these leases on our consolidated balance sheets. See Note 10 for a summary

of rent expense and remaining contractual payments under our ground lease and office space leases.

ASC 842 requires lessors to account for leases using an approach that is substantially equivalent to existing guidance for sales-type leases, direct financing leases, and operating leases. ASC 842 specifies that payments for certain lease-related services (for example, maintenance services, including common area maintenance), which are often included in lease agreements, represent "non-lease" components that will become subject to the guidance in ASC 606 when ASC 842 becomes effective. In July 2018, the FASB issued ASU 2018-11, Leases: Targeted Improvements ("ASU 2018-11"), which provides lessors with an optional practical expedient to not separate lease and non-lease components if both of the following criteria are met: (1) the timing and pattern of transfer of the lease and non-lease component(s) are the same and (2) the lease component would be classified as an operating lease, if it were accounted for separately. We anticipate the majority of our leases will qualify for the practical expedient and as such, we plan to adopt the practical expedient.

Additionally, ASC 842 requires lessors to capitalize, as initial direct costs, only those costs that are incurred due to the execution of a lease. As a result, compensation costs related to employees who spend time on lease origination activities, regardless of whether their time leads to a successful lease, will no longer be capitalized as initial direct costs and instead will be expensed as incurred. See "Deferred Leasing Costs" above for a summary of employee related compensation costs capitalized during the three and nine months ended September 30, 2018 and 2017.

ASC 842 is effective for annual periods beginning after December 15, 2018, which for us is January 1, 2019, and early adoption is permitted. ASC 842 requires the use of a modified retrospective transition approach for all leases existing at, or entered into after, the beginning of the earliest period presented in the consolidated financial statements, with certain practical expedients available. ASU 2018-11 provides for an optional transition method (the "effective date method") which would allow an entity to apply the transition provisions as of the effective date by recognizing its cumulative adjustment to the opening balance sheet of retained earnings in the period of adoption rather than in the earliest comparative period presented. In this case, an entity would continue to apply the legacy guidance in current GAAP (ASC 840), including its disclosure requirements, in the comparative periods presented in the financial statements. We plan to adopt ASC 842 using the effective date method and are currently completing our assessment of the impact of the guidance on our consolidated financial statements and notes to our consolidated financial statements.

3. Investments in Real Estate

Acquisitions

The following table summarizes the wholly-owned industrial properties we acquired during the nine months ended September 30, 2018:

Property	Submarket	Date of Acquisition	Rentable Square Feet	Number of Buildings	Contractual Purchase Price[1] (in thousands)
13971 Norton Avenue[2]	Inland Empire - West	1/17/2018	103,208	1	$ 11,364
Ontario Airport Commerce Center[3]	Inland Empire - West	2/23/2018	213,603	3	24,122
16010 Shoemaker Avenue[4]	Los Angeles - Mid-Counties	3/13/2018	115,600	1	17,218
4039 Calle Platino[5]	Oceanside	4/4/2018	143,274	1	20,000
851 Lawrence Drive[6]	Thousand Oaks	4/5/2018	49,976	1	6,600
1581 North Main Street[6]	Orange	4/6/2018	39,661	1	7,150
1580 West Carson Street[7]	Long Beach	4/26/2018	43,787	1	7,500
660 & 664 North Twin Oaks Valley Road[6]	San Marcos	4/26/2018	96,993	2	14,000
1190 Stanford Court[6]	North Orange County	5/8/2018	34,494	1	6,080
5300 Sheila Street[6]	Central LA	5/9/2018	695,120	1	121,000
15777 Gateway Circle[4]	OC Airport	5/17/2018	37,592	1	8,050
1998 Surveyor Avenue[4][8]	Ventura	5/18/2018	— [8]	— [8]	5,821
3100 Fujita Street[4]	South Bay	5/31/2018	91,516	1	14,037
4416 Azusa Canyon Road[4]	San Gabriel Valley	6/8/2018	70,510	1	12,000
1420 Mckinley Avenue[4]	South Bay	6/12/2018	136,685	1	30,000
12154 Montague Street[4]	Greater San Fernando Valley	6/29/2018	122,868	1	22,525
10747 Norwalk Boulevard[4]	Los Angeles - Mid-Counties	7/18/2018	52,691	1	10,835
29003 Avenue Sherman[4]	Greater San Fernando Valley	7/19/2018	68,123	1	9,500
16121 Carmenita Road[4]	Los Angeles - Mid-Counties	8/14/2018	108,500	1	13,300
Total 2018 Wholly-Owned Property Acquisitions			2,224,201	21	$ 361,102

(1) Represents the gross contractual purchase price before prorations, closing costs and other acquisition related costs.

(2) This acquisition was partially funded through a 1031 Exchange using $10.7 million of net cash proceeds from the sale of our property located at 8900-8980 Benson Avenue and 5637 Arrow Highway and borrowings under our unsecured revolving credit facility.

(3) The Ontario Airport Commerce Center is an industrial park which includes two properties located at 1900 Proforma Avenue and 1910-1920 Archibald Avenue. This acquisition was partially funded through a 1031 Exchange using $10.3 million of net cash proceeds from the sale of our property located at 700 Allen Avenue and 1851 Flower Street, borrowings under our unsecured revolving credit facility and available cash on hand. On May 9, 2018, we sold the property located at 1910-1920 Archibald Avenue (see Note 11).

(4) This acquisition was funded with available cash on hand.

(5) This acquisition was partially funded through a 1031 Exchange using $4.2 million of net cash proceeds from the sale of our property located at 200-220 South Grand Avenue and borrowings under our unsecured revolving credit facility.

(6) This acquisition was funded with available cash on hand and borrowings under our unsecured revolving credit facility.

(7) This acquisition was partially funded through a 1031 Exchange using $1.6 million of net cash proceeds from the sale of our property located at 6770 Central Avenue—Building B and borrowings under our unsecured revolving credit facility.

(8) We acquired 1998 Surveyor Avenue as an under-construction building for a cost of $5.8 million and the assumption of the seller’s fixed-price construction contracts with approximately $4.4 million of remaining costs. At completion, the property will be one single-tenant building containing 56,306 rentable square feet.

The following table summarizes the fair value of amounts allocated to each major class of asset and liability for the acquisitions noted in the table above, as of the date of each acquisition (in thousands):

	2018 Acquisitions
Assets:	
Land	$ 229,331
Buildings and improvements	154,096
Tenant improvements	1,533
Acquired lease intangible assets[(1)]	19,406
Other acquired assets[(2)]	103
Total assets acquired	404,469
Liabilities:	
Acquired lease intangible liabilities[(3)]	39,467
Other assumed liabilities[(2)]	1,460
Total liabilities assumed	40,927
Net assets acquired	$ 363,542

(1) Acquired lease intangible assets is comprised of $19.3 million of in-place lease intangibles with a weighted average amortization period of 18.3 years and $0.1 million of above-market lease intangibles with a weighted average amortization period of 3.7 years.
(2) Includes other working capital assets acquired and liabilities assumed, at the time of acquisition.
(3) Represents below-market lease intangibles with a weighted average amortization period of 27.6 years.

4. Intangible Assets

The following table summarizes our acquired lease intangible assets, including the value of in-place leases and above-market tenant leases, and our acquired lease intangible liabilities, including below-market tenant leases and above-market ground leases (in thousands):

	September 30, 2018	December 31, 2017
Acquired Lease Intangible Assets:		
In-place lease intangibles	$ 113,505	$ 95,750
Accumulated amortization	(64,556)	(51,735)
In-place lease intangibles, net	$ 48,949	$ 44,015
Above-market tenant leases	$ 10,704	$ 10,718
Accumulated amortization	(6,251)	(5,494)
Above-market tenant leases, net	$ 4,453	$ 5,224
Acquired lease intangible assets, net	$ 53,402	$ 49,239
Acquired Lease Intangible Liabilities:		
Below-market tenant leases	$ (64,078)	$ (24,843)
Accumulated accretion	11,914	6,925
Below-market tenant leases, net	$ (52,164)	$ (17,918)
Above-market ground lease	$ (290)	$ (290)
Accumulated accretion	165	141
Above-market ground lease, net	$ (125)	$ (149)
Acquired lease intangible liabilities, net	$ (52,289)	$ (18,067)

20

The following table summarizes the amortization related to our acquired lease intangible assets and liabilities for the reported periods noted below (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
In-place lease intangibles[1]	$4,115	$4,708	$13,982	$10,812
Net below-market tenant leases[2]	$(1,615)	$(877)	$(4,330)	$(1,179)
Above-market ground lease[3]	$(8)	$(8)	$(24)	$(24)

(1) The amortization of in-place lease intangibles is recorded to depreciation and amortization expense in the consolidated statements of operations for the periods presented.

(2) The amortization of net below-market tenant leases is recorded as an increase to rental revenues in the consolidated statements of operations for the periods presented.

(3) The accretion of the above-market ground lease is recorded as a decrease to property expenses in the consolidated statements of operations for the periods presented.

5. Notes Payable

The following table summarizes the balance of our indebtedness as of September 30, 2018 and December 31, 2017 (in thousands):

	September 30, 2018	December 31, 2017
Principal amount	$761,154	$671,658
Less: unamortized discount and debt issuance costs[1]	(3,936)	(2,717)
Carrying value	$757,218	$668,941

(1) Excludes unamortized debt issuance costs related to our unsecured revolving credit facility, which are presented in the line item “Deferred loan costs, net” in the consolidated balance sheets.

21

The following table summarizes the components and significant terms of our indebtedness as of September 30, 2018, and December 31, 2017 (dollars in thousands):

	September 30, 2018		December 31, 2017				
	Principal Amount	Unamortized Discount and Debt Issuance Costs	Principal Amount	Unamortized Discount and Debt Issuance Costs	Contractual Maturity Date	Stated Interest Rate[1]	Effective Interest Rate [2]
Secured Debt							
$60M Term Loan[3]	$58,499	$ (242)	$58,891	$ (125)	8/1/2023 [4]	LIBOR+1.70%	3.70 %
Gilbert/La Palma[5]	2,655	(131)	2,767	(138)	3/1/2031	5.125 %	5.44 %
Unsecured Debt							
$100M Term Loan Facility	100,000	(280)	100,000	(343)	2/14/2022	LIBOR+1.20% [6]	3.18 % [7]
Revolving Credit Facility	—	—	60,000	—	2/12/2021 [8]	LIBOR+1.10% [6][9]	3.36 %
$225M Term Loan Facility	225,000	(1,569)	225,000	(1,398)	1/14/2023	LIBOR+1.20% [6]	2.74 % [10]
$150M Term Loan Facility	150,000	(1,069)	—	—	5/22/2025	LIBOR+1.50% [6]	3.87 %
$100M Notes	100,000	(519)	100,000	(576)	8/6/2025	4.290 %	4.37 %
$125M Notes	125,000	(126)	125,000	(137)	7/13/2027	3.930 %	3.94 %
Total	$761,154	$ (3,936)	$671,658	$ (2,717)			

(1) Reflects the contractual interest rate under the terms of the loan, as of September 30, 2018.

(2) Reflects the effective interest rate as of September 30, 2018, which includes the effect of the amortization of discounts and debt issuance costs and the effect of interest rate swaps that are effective as of September 30, 2018.

(3) This term loan was modified on June 27, 2018, as further described below under “Modification of $60 Million Term Loan”. This term loan is secured by six properties. As of September 30, 2018, the interest rate on this variable-rate term loan has been effectively fixed through the use of two interest rate swaps. See Note 7 for details.

(4) One 24-month extension available at the borrower’s option.

(5) Monthly payments of interest and principal are based on a 20-year amortization table.

(6) The LIBOR margin will range from 1.20% to 1.70% per annum for the $100.0 million term loan facility, 1.10% to 1.50% per annum for the unsecured revolving credit facility, 1.20% to 1.70% per annum for the $225.0 million term loan facility and 1.50% to 2.20% per annum for the $150.0 million term loan facility, depending on the ratio of our outstanding consolidated indebtedness to the value of our consolidated gross asset value, or leverage ratio, which is measured on a quarterly basis.

(7) As of September 30, 2018, interest on the $100.0 million term loan facility has been effectively fixed through the use of two interest rate swaps. See Note 7 for details.

(8) Two additional six-month extensions are available at the borrower’s option.

(9) The unsecured revolving credit facility is subject to an applicable facility fee which is calculated as a percentage of the total lenders’ commitment amount, regardless of usage. The applicable facility fee will range from 0.15% to 0.30% per annum depending upon our leverage ratio.

(10) As of September 30, 2018, interest on the $225.0 million term loan facility has been effectively fixed through the use of two interest rate swaps. See Note 7 for details.

The following table summarizes the contractual debt maturities and scheduled amortization payments, excluding debt discounts and debt issuance costs, as of September 30, 2018, and does not consider extension options available to us as noted in the table above (in thousands):

October 1, 2018 - December 31, 2018	$38
2019	158
2020	166
2021	566
2022	100,967
Thereafter	659,259
Total	$761,154

Fourth Amendment to Credit Agreement

On January 16, 2018, we entered into the Fourth Amendment to Credit Agreement (the “Fourth Amendment”) to amend our Credit Agreement, dated as of January 14, 2016 (as amended from time to time) for our $225.0 million unsecured term loan facility (the “$225 Million Term Loan Facility”).

Amounts outstanding under the $225 Million Term Loan Facility bear interest at a rate equal to, at our option, either (i) LIBOR plus an applicable margin that is based upon our leverage ratio or (ii) the Base Rate, as defined in the $225 Million Term Loan Facility, plus an applicable margin that is based on our leverage ratio. The Fourth Amendment decreases the applicable margin for LIBOR-based borrowings from a range of 1.50% to 2.25% per annum to a range of 1.20% to 1.70% per annum and decreases the applicable margin for Base Rate-based borrowings from a range of 0.50% to 1.25% per annum to a range of 0.20% to 0.70% per annum.

If we obtain one additional investment grade rating by one or more of Standard & Poor's Financial Services (“S&P”) or Moody's Investor Services (“Moody’s”) to complement our current investment grade Fitch rating, we may elect to convert the pricing structure under the $225 Million Term Loan Facility to be based on such rating. Under this pricing structure, the Fourth Amendment decreases the applicable margin for LIBOR-based borrowings from a range of 1.40% to 2.35% per annum to a range of 0.90% to 1.75% per annum and decreases the applicable margin for Base Rate-based borrowings from a range of 0.40% to 1.35% per annum to a range of 0.00% to 0.75% per annum.

$150 Million Term Loan Facility

On May 22, 2018, we entered into a credit agreement for a senior unsecured term loan facility (the “$150 Million Term Loan Facility”) that initially permits aggregate borrowings of up to $150.0 million, the total of which we borrowed the same day at closing. Under the terms of the $150 Million Term Loan Facility, we may request additional incremental term loans in an aggregate amount not to exceed $100.0 million. Any increase in borrowings is subject to the satisfaction of specified conditions and the identification of lenders willing to make available such additional amounts. The maturity date of the $150 Million Term Loan Facility is May 22, 2025.

Interest on the $150 Million Term Loan Facility is generally to be paid based upon, at our option, either (i) LIBOR plus an applicable Eurodollar rate margin or (ii) the Base Rate (which is defined as the highest of (a) the federal funds rate plus 0.50%, (b) the administrative agent’s prime rate or (c) the Eurodollar Rate plus 1.00%), plus an applicable base rate margin. The applicable Eurodollar rate margin will range from 1.50% to 2.20% per annum for LIBOR-based borrowings and the applicable base rate margin will range from 0.50% to 1.20% per annum for Base Rate-based loans, depending on our leverage ratio.

If we obtain one additional investment grade rating from one or more of S&P or Moody's to complement our current investment grade Fitch rating, we may elect to convert the pricing structure under the $150 Million Term Loan Facility to be based on such rating. Under this pricing structure, the applicable Eurodollar rate margin will range from 1.40% to 2.35% per annum and the applicable base rate margin will range from 0.40% to 1.35% per annum.

We have the option to voluntarily prepay any amounts borrowed under the $150 Million Term Loan Facility in whole or in part at any time, subject to certain notice requirements. To the extent that we prepay all or any portion of a loan prior to May 22, 2020, we will pay a prepayment premium equal to (i) if such prepayment occurs prior to May 22, 2019, 2.00% of the principal amount so prepaid, and (ii) if such prepayment occurs on or after May 22, 2019, but prior to May 22, 2020, 1.00% of

23

the principal amount so prepaid. Amounts borrowed under the $150 Million Term Loan Facility and repaid or prepaid may not be reborrowed.

The $150 Million Term Loan Facility contains usual and customary events of default including defaults in the payment of principal, interest or fees, defaults in compliance with the covenants set forth in the credit agreement and other loan documentation, cross-defaults to certain other indebtedness, and bankruptcy and other insolvency defaults. If an event of default occurs and is continuing under the $150 Million Term Loan Facility, all outstanding principal amounts, together with all accrued unpaid interest and other amounts owing in respect thereof, may be declared immediately due and payable.

Modification of $60 Million Term Loan

On June 27, 2018, we entered into the Second Modification Agreement (the "Modification Agreement") to amend our Term Loan Agreement, dated as of July 24, 2013 (as amended from time to time) for our $60.0 million term loan (the "$60 Million Term Loan")

The Modification Agreement, among other things, (i) extends the maturity date of the $60 Million Term Loan from August 1, 2019, to August 1, 2023, (ii) decreases the interest rate from LIBOR plus 1.90% per annum to LIBOR plus 1.70% per annum, (iii) provides for one 24-month extension option, subject to certain terms and conditions, and (iv) amends the repayment schedule of the $60 Million Term Loan by adding 36 months of interest only payments, followed by equal monthly payments of principal ($65,250), plus accrued interest until maturity.

Credit Facility

We have a $450.0 million senior unsecured credit facility (the "Credit Facility"), comprised of a $350.0 million unsecured revolving credit facility (the "Revolver") and a $100.0 million unsecured term loan facility (the "$100 Million Term Loan Facility"). The Revolver is scheduled to mature on February 12, 2021, and has two six-month extension options available, and the $100 Million Term Loan Facility is scheduled to mature on February 14, 2022. Under the terms of the Credit Facility, we may request additional lender commitments up to an additional aggregate $550.0 million, which may be comprised of additional revolving commitments under the Revolver, an increase to the $100 Million Term Loan Facility, additional term loan tranches or any combination of the foregoing.

Interest on the Credit Facility is generally to be paid based upon, at our option, either (i) LIBOR plus an applicable margin that is based upon our leverage ratio or (ii) the Base Rate (which is defined as the highest of (a) the federal funds rate plus 0.50%, (b) the administrative agent's prime rate or (c) the Eurodollar Rate plus 1.00%) plus an applicable margin that is based on our leverage ratio. The margins for the Revolver range in amount from 1.10% to 1.50% per annum for LIBOR-based loans and 0.10% to 0.50% per annum for Base Rate-based loans, depending on our leverage ratio. The margins for the $100 Million Term Facility range in amount from 1.20% to 1.70% per annum for LIBOR-based loans and 0.20% to 0.70% per annum for Base Rate-based loans, depending on our leverage ratio.

If we attain one additional investment grade rating by one or more of S&P or Moody's to complement our current investment grade Fitch rating, we may elect to convert the pricing structure under the Credit Facility to be based on such rating. In that event, the margins for the Revolver will range in amount from 0.825% to 1.55% per annum for LIBOR-based loans and 0.00% to 0.55% per annum for Base Rate-based loans, depending on such rating, and the margins for the $100 Million Term Loan Facility will range in amount from 0.90% to 1.75% per annum for LIBOR-based loans and 0.00% to 0.75% per annum for Base Rate-based loans, depending on such rating.

In addition to the interest payable on amounts outstanding under the Revolver, we are required to pay an applicable facility fee, based upon our leverage ratio, on each lender's commitment amount under the Revolver, regardless of usage. The applicable facility fee will range in amount from 0.15% to 0.30% per annum, depending on our leverage ratio. In the event that we convert the pricing structure to be based on an investment-grade rating, the applicable facility fee will range in amount from 0.125% to 0.30% per annum, depending on such rating.

The Credit Facility is guaranteed by the Company and by substantially all of the current and to-be-formed subsidiaries of the Operating Partnership that own an unencumbered property. The Credit Facility is not secured by the Company's properties or by equity interests in the subsidiaries that hold such properties.

The Revolver and the $100 Million Term Loan Facility may be voluntarily prepaid in whole or in part at any time without premium or penalty. Amounts borrowed under the $100 Million Term Loan Facility and repaid or prepaid may not be reborrowed.

24

The Credit Facility contains usual and customary events of default including defaults in the payment of principal, interest or fees, defaults in compliance with the covenants set forth in the Credit Facility and other loan documentation, cross-defaults to certain other indebtedness, and bankruptcy and other insolvency defaults. If an event of default occurs and is continuing under the Credit Facility, the unpaid principal amount of all outstanding loans, together with all accrued unpaid interest and other amounts owing in respect thereof, may be declared immediately due and payable.

On September 30, 2018, we did not have any borrowings outstanding under the Revolver, leaving $350.0 million available for future borrowings.

Debt Covenants

The Credit Facility, the $225 Million Term Loan Facility, the $150 Million Term Loan Facility, the $100 million unsecured guaranteed senior notes (the “$100 Million Notes”) and the $125 million unsecured guaranteed senior notes (the “$125 Million Notes”) all include a series of financial and other covenants that we must comply with, including the following covenants which are tested on a quarterly basis:

- Maintaining a ratio of total indebtedness to total asset value of not more than 60%;
- For the Credit Facility, the $225 Million Term Loan Facility and the $150 Million Term Loan Facility, maintaining a ratio of secured debt to total asset value of not more than 45%;
- For the $100 Million Notes and the $125 Million Notes, maintaining a ratio of secured debt to total asset value of not more than 40%;
- Maintaining a ratio of total secured recourse debt to total asset value of not more than 15%;
- Maintaining a minimum tangible net worth of at least the sum of (i) $760,740,750, and (ii) an amount equal to at least 75% of the net equity proceeds received by the Company after September 30, 2016;
- Maintaining a ratio of adjusted EBITDA (as defined in each of the loan agreements) to fixed charges of at least 1.5 to 1.0;
- Maintaining a ratio of total unsecured debt to total unencumbered asset value of not more than 60%; and
- Maintaining a ratio of unencumbered NOI (as defined in each of the loan agreements) to unsecured interest expense of at least 1.75 to 1.00.

The Credit Facility, the $225 Million Term Loan Facility, the $150 Million Term Loan Facility, the $100 Million Notes and the $125 Million Notes also provide that our distributions may not exceed the greater of (i) 95.0% of our funds from operations or (ii) the amount required for us to qualify and maintain our status as a REIT and avoid the payment of federal or state income or excise tax in any 12-month period.

Additionally, subject to the terms of the $100 Million Notes and the $125 Million Notes (together the “Notes”), upon certain events of default, including, but not limited to, (i) a default in the payment of any principal, make-whole payment amount, or interest under the Notes, (ii) a default in the payment of certain of our other indebtedness, (iii) a default in compliance with the covenants set forth in the Notes agreement, and (iv) bankruptcy and other insolvency defaults, the principal and accrued and unpaid interest and the make-whole payment amount on the outstanding Notes will become due and payable at the option of the purchasers.

The $60 Million Term Loan contains a financial covenant that is tested on a quarterly basis, which requires us to maintain a minimum Debt Service Coverage Ratio (as defined in the term loan agreement) of at least 1.10 to 1.00.

We were in compliance with all of our required quarterly debt covenants as of September 30, 2018.

6. Operating Leases

We lease space to tenants primarily under non-cancelable operating leases that generally contain provisions for a base rent plus reimbursement for certain operating expenses. Operating expense reimbursements are reflected in the consolidated statements of operations as tenant reimbursements.

Future minimum base rent under operating leases as of September 30, 2018, is summarized as follows (in thousands):

25

Twelve months ended September 30:	
2019	$168,276
2020	145,541
2021	111,805
2022	77,779
2023	58,081
Thereafter	210,050
Total	$771,532

The future minimum base rent in the table above excludes tenant reimbursements, amortization of adjustments for deferred rent receivables and the amortization of above/below-market lease intangibles.

7. Interest Rate Swaps

Risk Management Objective of Using Derivatives

We are exposed to certain risks arising from both our business operations and economic conditions. We principally manage our exposures to a wide variety of business and operational risks through management of our core business activities. We manage economic risks, including interest rate, liquidity, and credit risk primarily by managing the amount, sources and duration of our debt funding and through the use of derivative financial instruments. Specifically, we enter into derivative financial instruments to manage exposures that arise from business activities that result in the payment of future known and uncertain cash amounts, the value of which are determined by interest rates. Our derivative financial instruments are used to manage differences in the amount, timing and duration of our known or expected cash payments principally related to our borrowings.

Derivative Instruments

Our objectives in using interest rate derivatives are to add stability to interest expense and to manage exposure to interest rate movements. To accomplish this objective, we primarily use interest rate swaps as part of our interest rate risk management strategy. Interest rate swaps designated as cash flow hedges involve the receipt of variable amounts from a counterparty in exchange for us making fixed-rate payments over the life of the agreements without exchange of the underlying notional value. We do not use derivatives for trading or speculative purposes.

The change in fair value of derivatives designated and qualifying as cash flow hedges is initially recorded in accumulated other comprehensive income/(loss) ("AOCI") and is subsequently reclassified from AOCI into earnings in the period that the hedged forecasted transaction affects earnings.

The following table sets forth a summary of our interest rate swaps at September 30, 2018 and December 31, 2017 (dollars in thousands):

				Current Notional Value[1]		Fair Value of Interest Rate Derivative Assets /(Derivative Liabilities)[2]	
Derivative Instrument	Effective Date	Maturity Date	LIBOR Interest Strike Rate	September 30, 2018	December 31, 2017	September 30, 2018	December 31, 2017
Interest Rate Swap	1/15/2015	2/15/2019	1.826%	$30,000	$ 30,000	$61	$ (11)
Interest Rate Swap	7/15/2015	2/15/2019	2.010%	$28,304	$ 28,891	$37	$ (70)
Interest Rate Swap	8/14/2015	12/14/2018	1.790%	$50,000	$ 50,000	$49	$ (18)
Interest Rate Swap	2/16/2016	12/14/2018	2.005%	$50,000	$ 50,000	$27	$ (120)
Interest Rate Swap	2/14/2018	1/14/2022	1.349%	$125,000	$ —	$6,037	$ 3,582
Interest Rate Swap	8/14/2018	1/14/2022	1.406%	$100,000	$ —	$4,673	$ 2,521
Interest Rate Swap	12/14/2018	8/14/2021	1.764%	$—	$ —	$2,967	$ 1,090

(1) Represents the notional value of swaps that are effective as of the balance sheet date presented.

(2) The fair value of derivative assets are included in the line item “Interest rate swap asset” in the accompanying consolidated balance sheets and the fair value of (derivative liabilities) are included in the line item “Interest rate swap liability” in the accompanying consolidated balance sheets.

The following table sets forth the impact of our interest rate swaps on our consolidated statements of operations for the periods presented (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Interest Rate Swaps in Cash Flow Hedging Relationships:				
Amount of gain (loss) recognized in AOCI on derivatives	$1,212	$382	$7,382	$(672)
Amount of gain (loss) reclassified from AOCI into earnings under “Interest expense”	$397	$(280)	$505	$(1,090)
Total interest expense presented in the Consolidated Statement of Operations in which the effects of cash flow hedges are recorded (line item “Interest expense”)	$6,456	$6,271	$18,760	$14,571

During the next twelve months, we estimate that an additional $3.7 million will be reclassified from AOCI into earnings as a decrease to interest expense.

Offsetting Derivatives

We enter into master netting arrangements, which reduce credit risk by permitting net settlement of transactions with the same counterparty. Derivative instruments that are subject to master netting arrangements and qualify for net presentation in the consolidated balance sheets are presented on a gross basis in the consolidated balance sheets as of September 30, 2018 and December 31, 2017.

The following tables present information about the potential effects of netting if we were to offset our interest rate swap assets and interest rate swap liabilities in the accompanying consolidated balance sheets as of September 30, 2018 and December 31, 2017 (in thousands).

				Gross Amounts Not Offset in the Balance Sheet		
Offsetting of Derivative Assets	Gross Amounts of Recognized Assets	Gross Amounts Offset in the Balance Sheet	Net Amounts of Assets Presented in the Balance Sheet	Financial Instruments	Cash Collateral Received	Net Amount
September 30, 2018						
Interest rate swaps	13,851	—	13,851	—	—	13,851
December 31, 2017						
Interest rate swaps	7,193	—	7,193	(219)	—	6,974

27

Offsetting of Derivative Liabilities	Gross Amounts of Recognized Liabilities	Gross Amounts Offset in the Balance Sheet	Net Amounts of Assets Presented in the Balance Sheet	Gross Amounts Not Offset in the Balance Sheet		Net Amount
				Financial Instruments	Cash Collateral Received	
September 30, 2018						
Interest rate swaps	—	—	—	—	—	—
December 31, 2017						
Interest rate swaps	219	—	219	(219)	—	—

Credit-risk-related Contingent Features

Certain of our agreements with our derivative counterparties contain a provision where if we default on any of our indebtedness, including default where repayment of the indebtedness has not been accelerated by the lender within a specified time period, then we could also be declared in default on its derivative obligations.

Certain of our agreements with our derivative counterparties contain provisions where if a merger or acquisition occurs that materially changes our creditworthiness in an adverse manner, we may be required to fully collateralize our obligations under the derivative instrument.

8. Fair Value Measurements

We have adopted FASB Accounting Standards Codification Topic 820: Fair Value Measurements and Disclosure ("ASC 820"). ASC 820 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. ASC 820 applies to reported balances that are required or permitted to be measured at fair value under existing accounting pronouncements; accordingly, the standard does not require any new fair value measurements of reported balances.

ASC 820 emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, ASC 820 establishes a fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entity's own assumptions about market participant assumptions (unobservable inputs classified within Level 3 of the hierarchy).

Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access. Level 2 inputs are inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs may include quoted prices for similar assets and liabilities in active markets, as well as inputs that are observable for the asset or liability (other than quoted prices), such as interest rates and yield curves that are observable at commonly quoted intervals. Level 3 inputs are unobservable inputs for the asset or liability, which are typically based on an entity's own assumptions, as there is little, if any, related market activity. In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

Recurring Measurements – Interest Rate Swaps

Currently, we use interest rate swap agreements to manage our interest rate risk. The valuation of these instruments is determined using widely accepted valuation techniques including discounted cash flow analysis on the expected cash

flows of each derivative. This analysis reflects the contractual terms of the derivatives, including the period to maturity, and uses observable market-based inputs, including interest rate curves.

To comply with the provisions of ASC 820, we incorporate credit valuation adjustments to appropriately reflect both our own nonperformance risk and the respective counterparty's nonperformance risk in the fair value measurements. In adjusting the fair value of our derivative contracts for the effect of nonperformance risk, we have considered the impact of netting and any applicable credit enhancements, such as collateral postings, thresholds, mutual puts, and guarantees.

Although we have determined that the majority of the inputs used to value our derivatives fall within Level 2 of the fair value hierarchy, the credit valuation adjustments associated with our derivatives utilize Level 3 inputs, such as estimates of current credit spreads to evaluate the likelihood of default by ourselves and our counterparties. However, as of September 30, 2018, we have assessed the significance of the impact of the credit valuation adjustments on the overall valuation of our derivative positions and have determined that the credit valuation adjustments are not significant to the overall valuation of its derivatives. As a result, we have determined that its derivative valuations in their entirety are classified in Level 2 of the fair value hierarchy.

The table below sets forth the estimated fair value of our interest rate swaps as of September 30, 2018 and December 31, 2017, which we measure on a recurring basis by level within the fair value hierarchy (in thousands).

	Fair Value Measurement Using			
	Total Fair Value	Quoted Price in Active Markets for Identical Assets and Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
September 30, 2018				
Interest Rate Swap Asset	$13,851	$ —	$ 13,851	$ —
Interest Rate Swap Liability	$—	$ —	$ —	$ —
December 31, 2017				
Interest Rate Swap Asset	$7,193	$ —	$ 7,193	$ —
Interest Rate Swap Liability	$(219)	$ —	$ (219)	$ —

Financial Instruments Disclosed at Fair Value

The carrying amounts of cash and cash equivalents, rents and other receivables, other assets, accounts payable, accrued expenses and other liabilities, and tenant security deposits approximate fair value because of their short-term nature.

The fair value of our notes payable was estimated by calculating the present value of principal and interest payments, using discount rates that best reflect current market rates for financings with similar characteristics and credit quality, and assuming each loan is outstanding through its respective contractual maturity date.

The table below sets forth the carrying value and the estimated fair value of our notes payable as of September 30, 2018 and December 31, 2017 (in thousands):

	Fair Value Measurement Using				
Liabilities	Total Fair Value	Quoted Price in Active Markets for Identical	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Carrying Value

		Assets and Liabilities (Level 1)			
Notes Payable at:					
September 30, 2018	$752,722	$ —	$ —	$ 752,722	$757,218
December 31, 2017	$673,377	$ —	$ —	$ 673,377	$668,941

29

9. Related Party Transactions

Howard Schwimmer

We engage in transactions with Howard Schwimmer, our Co-Chief Executive Officer, earning management fees and leasing commissions from entities controlled individually by Mr. Schwimmer. Fees and commissions earned from these entities are included in “Management, leasing and development services” in the consolidated statements of operations. We recorded $0.1 million and $0.1 million for the three months ended September 30, 2018 and 2017, respectively, and $0.3 million and $0.3 million for the nine months ended September 30, 2018 and 2017, respectively, in management, leasing and development services revenue.

10. Commitments and Contingencies

Legal

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

Environmental

We generally will perform environmental site assessments at properties we are considering acquiring. After the acquisition of such properties, we continue to monitor the properties for the presence of hazardous or toxic substances. From time to time, we acquire properties with known adverse environmental conditions. If at the time of acquisition, losses associated with environmental remediation obligations are probable and can be reasonably estimated, we record a liability.

On February 25, 2014, we acquired the property located at West 228th Street. Before purchasing the property during the due diligence phase, we engaged a third party environmental consultant to perform various environmental site assessments to determine the presence of any environmental contaminants that might warrant remediation efforts. Based on their investigation, they determined that hazardous substances existed at the property and that additional assessment and remediation work would likely be required to satisfy regulatory requirements. The total remediation costs were estimated to be $1.3 million, which includes remediation, processing and oversight costs.

To address the estimated costs associated with the environmental issues at the West 228th Street property, we entered into an Environmental Holdback Escrow Agreement (the “Holdback Agreement”) with the former owner, whereby $1.4 million was placed into an escrow account to be used to pay remediation costs. To fund the $1.4 million, the escrow holder withheld $1.3 million of the purchase price, which would have otherwise been paid to the seller at closing, and the Company funded an additional $0.1 million. According to the Holdback Agreement, the seller has no liability or responsibility to pay for remediation costs in excess of $1.3 million.

As of September 30, 2018, and December 31, 2017, we had a $1.1 million and $1.1 million contingent liability recorded in our consolidated balance sheets included in the line item “Accounts payable and accrued expenses,” reflecting the estimated remaining cost to remediate environmental liabilities at West 228th Street that existed prior to the acquisition date. As of September 30, 2018, and December 31, 2017, we also had a $1.1 million and $1.1 million corresponding indemnification asset recorded in our consolidated balance sheets included in the line item “Other assets,” reflecting the estimated costs we expect the former owner to cover pursuant to the Holdback Agreement.

We expect that the resolution of the environmental matters relating to the above will not have a material impact on our consolidated financial condition, results of operations or cash flows. However, we cannot assure you that we have identified all environmental liabilities at our properties, that all necessary remediation actions have been or will be undertaken at our properties or that we will be indemnified, in full or at all, in the event that such environmental liabilities arise. Furthermore, we cannot assure you that future changes to environmental laws or regulations and their application will not give rise to loss contingencies for future environmental remediation.

Rent Expense

As of September 30, 2018, we lease a parcel of land that is currently being sub-leased to a tenant for a parking lot. The ground lease is scheduled to expire on June 1, 2062. We recognized rental expense for our ground lease in the amount of $36 thousand and $36 thousand for the three months ended September 30, 2018 and 2017, respectively, and $0.1 million and $0.1 million for the nine months ended September 30, 2018 and 2017, respectively. As part of conducting our day-to-day business, we also lease office space under operating leases. We recognized rental expense for our office space leases in the amount of $0.2 million and $0.1 million for the three months ended September 30, 2018 and 2017, respectively, and $0.5 million and $0.3 million for the nine months ended September 30, 2018 and 2017, respectively.

The future minimum commitment under our ground lease and office space leases as of September 30, 2018, is as follows (in thousands):

	Office Leases	Ground Lease
October 1, 2018 - December 31, 2018	$223	$36
2019	660	144
2020	257	144
2021	167	144
2022	—	144
Thereafter	—	5,676
Total	$1,307	$6,288

Tenant and Construction Related Commitments

As of September 30, 2018, we had commitments of approximately $25.5 million for tenant improvement and construction work under the terms of leases with certain of our tenants and contractual agreements with our construction vendors.

Concentrations of Credit Risk

We have deposited cash with financial institutions that are insured by the Federal Deposit Insurance Corporation up to $250,000 per institution. Although we have deposits at institutions in excess of federally insured limits as of September 30, 2018, we do not believe we are exposed to significant credit risk due to the financial position of the institutions in which those deposits are held.

As of September 30, 2018, all of our properties are located in the Southern California infill markets. The ability of the tenants to honor the terms of their respective leases is dependent upon the economic, regulatory and social factors affecting the markets in which the tenants operate.

During the nine months ended September 30, 2018, no single tenant accounted for more than 5% of our total consolidated rental revenues.

11. Dispositions and Real Estate Held for Sale

Dispositions

The following table summarizes the properties we sold during the nine months ended September 30, 2018:

Property	Submarket	Date of Disposition	Rentable Square Feet	Contractual Sales Price[1] (in thousands)	Gain Recorded (in thousands)
8900-8980 Benson Avenue and 5637 Arrow Highway	Inland Empire West	1/2/2018	88,016	$ 11,440	$ 4,029
700 Allen Avenue and 1851 Flower Street	Los Angeles - San Fernando Valley	1/17/2018	25,168	$ 10,900	$ 4,753
200-220 South Grand Avenue	Orange County - Airport	3/7/2018	27,200	$ 4,515	$ 1,201
6770 Central Avenue—Building B	Inland Empire West	4/9/2018	11,808	$ 1,676	$ 1,113
1910-1920 Archibald Avenue	Inland Empire West	5/9/2018	78,243	$ 9,050	$ 495
Total			230,435	$ 37,581	$ 11,591

(1) Represents the gross contractual sales price before commissions, prorations and other closing costs.

Real Estate Held for Sale

As of December 31, 2017, our properties located at (i) 700 Allen Avenue and 1830 Flower Street and (ii) 8900-8980 Benson Avenue and 5637 Arrow Highway were classified as held for sale. We did not have any properties classified as held for sale as of September 30, 2018.

The following table summarizes the major classes of assets and liabilities associated with real estate properties classified as held for sale (in thousands):

	December 31, 2017
Land	$ 5,671
Buildings and improvements	7,180
Tenant improvements	429
Construction in progress	16
Real estate held for sale	13,296
Accumulated depreciation	(1,609)
Real estate held for sale, net	11,687
Acquired lease intangible assets, net	71
Other assets associated with real estate held for sale	678
Total assets associated with real estate held for sale, net	$ 12,436
Tenant security deposits	$ 193
Other liabilities associated with real estate held for sale	50
Total liabilities associated with real estate held for sale	$ 243

12. Equity

Common Stock

On June 13, 2018, we established a new at-the-market equity offering program (the "$400 Million ATM Program") pursuant to which we may sell from time to time up to an aggregate of $400.0 million of our common stock through sales agents. The $400 Million ATM Program replaces our previous $300 million at-the-market equity offering program which was established on September 21, 2017 (the "Prior ATM Program"). All $300.0 million of shares of our common stock under the Prior ATM Program were sold prior to establishing the $400 Million ATM Program.

During the nine months ended September 30, 2018, we sold a total of 14,081,074 shares of our common stock under the $400 Million ATM Program and the Prior ATM Program, at a weighted average price of $30.70 per share, for gross proceeds of $432.3 million, and net proceeds of $425.8 million, after deducting the sales agents' fee. As of September 30, 2018, we had the capacity to issue up to an additional $196.8 million of common stock under the $400 Million ATM Program. Actual sales going forward, if any, will depend on a variety of factors, including among others, market conditions, the trading price of our common stock, determinations by us of the appropriate sources of funding for us and potential uses of funding available to us.

Noncontrolling Interests

Noncontrolling interests in our Operating Partnership relate to interests in the Operating Partnership that are not owned by us. As of September 30, 2018, noncontrolling interests consisted of 1,845,565 OP Units and 157,539 fully-vested LTIP units and represented approximately 2.1% of our Operating Partnership. OP Units and shares of our common stock have essentially the same economic characteristics, as they share equally in the total net income or loss and distributions of our Operating Partnership. Investors who own OP Units have the right to cause our Operating Partnership to redeem any or all of their units in our Operating Partnership for an amount of cash per unit equal to the then current market value of one share of common stock, or, at our election, shares of our common stock on a one-for-one basis.

During the nine months ended September 30, 2018, 60,175 OP Units were converted into an equivalent number of shares of common stock, resulting in the reclassification of $0.6 million of noncontrolling interest to Rexford Industrial Realty, Inc.'s stockholders' equity.

Amended and Restated 2013 Incentive Award Plan

On June 11, 2018, our stockholders approved the Amended and Restated Rexford Industrial Realty, Inc. and Rexford Industrial Realty, L.P. 2013 Incentive Award Plan (the "Plan"), superseding and replacing the Rexford Industrial Realty, Inc. and Rexford Industrial Realty, L.P. 2013 Incentive Award Plan (the "Prior Plan"). Pursuant to the Plan, we may continue to make grants of stock options, restricted stock, dividend equivalents, stock payments, restricted stock units, performance shares, LTIP units of partnership interest in our Operating Partnership ("LTIP units"), performance units in our Operating Partnership ("Performance Units"), and other stock based and cash awards to our non-employee directors, employees and consultants. The aggregate number of shares of our common stock, LTIP units and Performance Units that may be issued or transferred pursuant to the Plan is 1,770,000, plus any shares that have not been issued under the Prior Plan, including shares subject to outstanding awards under the Prior Plan that are not issued or delivered to a participant for any reason or that are forfeited by a participant prior to vesting. As of September 30, 2018, a total of 2,162,877 shares of common stock, LTIP units and Performance Units remain available for issuance.

Shares of our restricted common stock generally may not be sold, pledged, assigned or transferred in any manner other than by will or the laws of descent and distribution or, subject to the consent of the administrator of the Plan, a domestic relations order, unless and until all restrictions applicable to such shares have lapsed. Such restrictions generally expire upon vesting. Shares of our restricted common stock are participating securities and have full voting rights and nonforfeitable rights to dividends.

LTIP units and Performance Units are each a class of limited partnership units in the Operating Partnership. Initially, LTIP units and Performance Units do not have full parity with OP Units with respect to liquidating distributions. However, upon the occurrence of certain events described in the Operating Partnership's partnership agreement, the LTIP units and Performance Units can over time achieve full parity with the OP Units for all purposes. If such parity is reached, vested LTIP units and Performance Units may be converted into an equal number of OP Units, and, upon conversion, enjoy all rights of OP Units. LTIP Units, whether vested or not, receive the same quarterly per-unit

distributions as OP Units, which equal the per-

33

share distributions on shares of our common stock. Performance Units that have not vested receive a quarterly per-unit distribution equal to 10% of the distributions paid on OP Units.

The following table sets forth our share-based award activity for the nine months ended September 30, 2018:

	Unvested Awards		
	Restricted Common Stock	LTIP Units	Performance Units
Balance at January 1, 2018	190,695	293,485	703,248
Granted	103,443	57,443	—
Forfeited	(13,031)	—	—
Vested[(1)]	(71,893)	(45,034)	—
Balance at September 30, 2018	209,214	305,894	703,248

(1) During the nine months ended September 30, 2018, 20,663 shares of the Company's common stock were tendered in accordance with the terms of the Plan to satisfy minimum statutory tax withholding requirements associated with the vesting of restricted shares of common stock.

The following table sets forth the vesting schedule of all unvested share-based awards outstanding as of September 30, 2018:

	Unvested Awards		
	Restricted Common Stock	LTIP Units	Performance Units[(1)]
October 1, 2018 - December 31, 2018	9,933	111,721	315,998
2019	82,678	114,818	199,000
2020	55,622	73,151	188,250
2021	39,409	3,102	—
2022	21,572	3,102	—
Total	209,214	305,894	703,248

(1) Represents the maximum number of Performance Units that would become earned and vested on December 14, 2018, December 28, 2019 and December 14, 2020, in the event that the specified maximum total shareholder return ("TSR") goals are achieved over the three-year performance period from December 15, 2015 through December 14, 2018, the three-year performance period from December 29, 2016 through December 28, 2019, and the three-year performance period from December 15, 2017 through December 14, 2020, respectively. The number of Performance Units that ultimately vest will be based on both the Company's absolute TSR and the Company's TSR performance relative to a peer group over each three-year performance period. The maximum number of Performance Units will be earned only if the Company both (i) achieves 50% or higher absolute TSR, inclusive of all dividends paid, over each three-year performance period with respect to the awards vesting on December 14, 2018 and December 28, 2019, and achieves 36% or higher absolute TSR, inclusive of all dividends paid, over the three-year performance period with respect to the awards vesting on December 14, 2020, and (ii) finishes in the 75th or greater percentile of the peer group for TSR over each three-year performance period.

The following table sets forth the amounts expensed and capitalized for all share-based awards for the reported periods presented below (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Expensed share-based compensation[1]	$2,243	$1,329	$7,866	$4,070
Capitalized share-based compensation[2]	73	7	183	120
Total share-based compensation	$2,316	$1,336	$8,049	$4,190

(1) Amounts expensed are included in “General and administrative” and “Property expenses” in the accompanying consolidated statements of operations.

(2) Amounts capitalized, which relate to employees who provide construction and leasing services, are included in “Building and improvements” and “Deferred leasing costs, net” in the consolidated balance sheets.

As of September 30, 2018, total unrecognized compensation cost related to all unvested share-based awards was $9.8 million and is expected to be recognized over a weighted average remaining period of 25 months.

Changes in Accumulated Other Comprehensive Income

The following table summarizes the changes in our AOCI balance for the nine months ended September 30, 2018 and 2017, which consists solely of adjustments related to our cash flow hedges (in thousands):

	Nine Months Ended September 30,	
	2018	2017
Accumulated other comprehensive income - beginning balance	$6,799	$3,445
Other comprehensive income (loss) before reclassifications	7,382	(672)
Amounts reclassified from accumulated other comprehensive income to interest expense	(505)	1,090
Net current period other comprehensive income (loss)	6,877	418
Less other comprehensive (income) loss attributable to noncontrolling interests	(118)	7
Other comprehensive income (loss) attributable to common stockholders	6,759	425
Accumulated other comprehensive income - ending balance	$13,558	$3,870

13. Earnings Per Share

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Numerator:				
Net income	$8,965	$ 2,009	$31,868	$ 27,585
Less: Preferred stock dividends	(2,423)	(1,322)	(7,270)	(3,966)
Less: Net income attributable to noncontrolling interests	(141)	(21)	(588)	(684)
Less: Net income attributable to participating securities	(94)	(80)	(285)	(327)
Net income attributable to common stockholders	$6,307	$ 586	$23,725	$ 22,608
Denominator:				
Weighted average shares of common stock outstanding – basic	91,463,594	72,621,219	84,407,429	68,984,047
Effect of dilutive securities - performance units	481,612	446,862	518,043	380,808
Weighted average shares of common stock outstanding – diluted	91,945,206	73,068,081	84,925,472	69,364,855
Earnings per share — Basic				
Net income attributable to common stockholders	$0.07	$ 0.01	$0.28	$ 0.33
Earnings per share — Diluted				
Net income attributable to common stockholders	$0.07	$ 0.01	$0.28	$ 0.33

Unvested share-based payment awards that contain non-forfeitable rights to dividends, whether paid or unpaid, are accounted for as participating securities. As such, unvested shares of restricted stock, unvested LTIP Units and unvested Performance Units are considered participating securities. Participating securities are included in the computation of basic EPS pursuant to the two-class method. The two-class method determines EPS for each class of common stock and each participating security according to dividends declared (or accumulated) and their respective participation rights in undistributed earnings. Participating securities are also included in the computation of diluted EPS using the more dilutive of the two-class method or treasury stock method for unvested shares of restricted stock and LTIP Units, and by determining if certain market conditions have been met at the reporting date for unvested Performance Units.

The effect of including unvested shares of restricted stock and unvested LTIP Units using the treasury stock method was excluded from our calculation of weighted average shares of common stock outstanding – diluted, as their inclusion would have been anti-dilutive.

Performance Units, which are subject to vesting based on the Company achieving certain TSR levels over a three-year performance period, are included as contingently issuable shares in the calculation of diluted EPS when TSR has been achieved at or above the threshold levels specified in the award agreements, assuming the reporting period is the end of the performance period, and the effect is dilutive.

We also consider the effect of other potentially dilutive securities, including OP Units, which may be redeemed for shares of our common stock under certain circumstances, and include them in our computation of diluted EPS when their inclusion is dilutive.

14. Subsequent Events

Acquisitions

On October 17, 2018, we acquired the property located at 1332-1340 Rocky Point Drive in Oceanside, California for a contract price of $10.2 million. The property consists of one single-tenant building with 73,747 rentable square feet.

Dividends Declared

On October 29, 2018, our board of directors declared a quarterly cash dividend of $0.16 per share of common stock and a quarterly cash distribution of $0.16 per OP Unit, to be paid on January 15, 2019, to holders of record as of December 31, 2018. Also, on October 29, 2018, our board of directors declared a quarterly cash dividend of $0.367188 per share of our 5.875% Series A Cumulative Redeemable Preferred Stock and $0.367188 per share of our 5.875% Series B Cumulative Redeemable Preferred Stock, to be paid on December 31, 2018, to preferred stockholders of record as of December 14, 2018.

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

The following discussion should be read in conjunction with the consolidated financial statements and the related notes thereto that appear in Part I, Item 1 "Financial Statements" of this Quarterly Report on Form 10-Q. The terms "Company," "we," "us," and "our" refer to Rexford Industrial Realty, Inc. and its consolidated subsidiaries except where the context otherwise requires.

Forward-Looking Statements

We make statements in this quarterly report that are forward-looking statements, which are usually identified by the use of words such as "anticipates," "believes," "expects," "intends," "may," "might," "plans," "estimates," "projects," "seeks," "result" and variations of such words or similar expressions. Our forward-looking statements reflect our current views about our plans, intentions, expectations, strategies and prospects, which are based on the information currently available to us and on assumptions we have made. Although we believe that our plans, intentions, expectations, strategies and prospects as reflected in or suggested by our forward-looking statements are reasonable, we can give no assurance that our plans, intentions, expectations, strategies or prospects will be attained or achieved and you should not place undue reliance on these forward-looking statements. Furthermore, actual results may differ materially from those described in the forward-looking statements and may be affected by a variety of risks and factors including, without limitation:

- the competitive environment in which we operate;
- real estate risks, including fluctuations in real estate values and the general economic climate in local markets and competition for tenants in such markets;
- decreased rental rates or increasing vacancy rates;
- potential defaults on or non-renewal of leases by tenants;
- potential bankruptcy or insolvency of tenants;
- acquisition risks, including failure of such acquisitions to perform in accordance with expectations;
- the timing of acquisitions and dispositions;
- potential natural disasters such as earthquakes, wildfires or floods;
- the consequence of any future security alerts and/or terrorist attacks;
- national, international, regional and local economic conditions;
- the general level of interest rates;
- potential changes in the law or governmental regulations that affect us and interpretations of those laws and regulations, including changes in real estate and zoning or real estate investment trust ("REIT") tax laws, and potential increases in real property tax rates;
- financing risks, including the risks that our cash flows from operations may be insufficient to meet required payments of principal and interest and we may be unable to refinance our existing debt upon maturity or obtain new financing on attractive terms or at all;
- lack of or insufficient amounts of insurance;
- our failure to complete acquisitions;
- our failure to successfully integrate acquired properties;
- our ability to qualify and maintain our qualification as a REIT;
- our ability to maintain our current investment grade rating by Fitch;
- litigation, including costs associated with prosecuting or defending pending or threatened claims and any adverse outcomes; and
- possible environmental liabilities, including costs, fines or penalties that may be incurred due to necessary remediation of contamination of properties presently owned or previously owned by us.

Accordingly, there is no assurance that our expectations will be realized. Except as otherwise required by the federal securities laws, we disclaim any obligations or undertaking to publicly release any updates or revisions to any forward-looking statement contained herein (or elsewhere) to reflect any change in our expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based. The reader should

review carefully our financial statements and the notes thereto, as well as the section entitled "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2017.

Company Overview

Rexford Industrial Realty, Inc. is a self-administered and self-managed full-service REIT focused on owning and operating industrial properties in Southern California infill markets. We were formed as a Maryland corporation on January 18, 2013, and Rexford Industrial Realty, L.P. (the "Operating Partnership"), of which we are the sole general partner, was formed as a Maryland limited partnership on January 18, 2013. Through our controlling interest in our Operating Partnership and its subsidiaries, we acquire, own, improve, develop, lease and manage industrial real estate principally located in Southern California infill markets, and, from time to time, acquire or provide mortgage debt secured by industrial property. We are organized and conduct our operations to qualify as a REIT under the Internal Revenue Code of 1986 (the "Code"), as amended, and generally are not subject to federal taxes on our income to the extent we distribute our income to our shareholders and maintain our qualification as a REIT.

As of September 30, 2018, our consolidated portfolio consisted of 167 properties with approximately 20.5 million rentable square feet. In addition, we currently manage an additional 20 properties with approximately 1.2 million rentable square feet.

Our goal is to generate attractive risk-adjusted returns for our stockholders by providing superior access to industrial property investments and mortgage debt secured by industrial property in high-barrier Southern California infill markets. Our target markets provide us with opportunities to acquire both stabilized properties generating favorable cash flow, as well as properties where we can enhance returns through value-add renovations and redevelopment. Scarcity of available space and high barriers limiting new construction all contribute to create superior long-term supply/demand fundamentals within our target infill Southern California industrial property markets. With our vertically integrated operating platform and extensive value-add investment and management capabilities, we believe we are in a position to take advantage of the opportunities in our markets to achieve our objectives.

2018 Year to Date Highlights

Acquisitions

- During the first quarter of 2018, we completed the acquisition of four properties with a combined 0.4 million rentable square feet, for a total gross purchase price of $52.7 million.
- During the second quarter of 2018, we completed the acquisition of 13 properties with a combined 1.6 million rentable square feet, for a total gross purchase price of $274.8 million.
- During the third quarter of 2018, we completed the acquisition of three properties with a combined 0.2 million rentable square feet, for a total gross purchase price of $33.6 million.
- Subsequent to September 30, 2018, we completed the acquisition of one property with 0.1 million rentable square feet, for a gross purchase price of $10.2 million.

Repositioning

- During the first quarter of 2018, we completed the repositioning and lease-up of 43,927 rentable square feet of space at 3233 Mission Oaks Boulevard.
- During the third quarter of 2018, we completed the repositioning of four of our properties located at 301-445 Figueroa Street, 28903 Avenue Paine, 14748-14750 Nelson Avenue and 15401 Figueroa Street, with a combined 0.5 million rentable square feet. As of September 30, 2018, 301-445 Figueroa Street has been stabilized at 100% occupancy, 28903 Avenue Paine is 100% leased to a single-tenant with a lease commencement date of December 31, 2018, and 14748-14750 Nelson Avenue is 76% occupied. During the third quarter of 2018, we also pre-leased our 56,306 square foot single-tenant development property located at 1998 Surveyor Avenue. The lease is expected to commence in January 2019 following the completion of construction.

Dispositions

- During the first quarter of 2018, we sold three properties with a combined 0.1 million rentable square feet, for a total gross sales price of $26.9 million and total net cash proceeds of $25.2 million.
- During the second quarter of 2018, we sold two properties with a combined 0.1 million rentable square feet, for a total gross sales price of $10.7 million and total net cash proceeds of $10.3 million.

Financing

- In January 2018, we amended our $225 million unsecured term loan facility, which reduced the applicable margin for LIBOR-based borrowings from a range of 1.50% to 2.25% per annum to a range of 1.20% to 1.70% per annum.
- In May 2018, we closed on a seven-year $150 million senior unsecured term loan facility that matures May 22, 2025. The term loan facility bears interest at LIBOR plus an applicable Eurodollar rate margin that will range from 1.50% to 2.20% per annum depending on our leverage ratio.
- In June 2018, we amended our $60 million term loan, which extended the maturity date from August 1, 2019 to August 1, 2023, and decreased the interest rate from LIBOR plus 1.90% per annum to LIBOR plus 1.70% per annum.

Equity

- During the first quarter of 2018, we sold 2,085,663 shares of common stock under our at-the-market equity offering program for gross proceeds of $58.5 million, or approximately $28.02 per share.
- During the second quarter of 2018, we sold 10,358,256 shares of common stock under our at-the-market equity offering programs for gross proceeds of $321.8 million, or approximately $31.07 per share.
- During the third quarter of 2018, we sold 1,637,155 shares of common stock under our at-the-market equity offering program for gross proceeds of $52.0 million, or approximately $31.74 per share.

Factors That May Influence Future Results of Operations

Market Fundamentals

Our operating results depend upon the infill Southern California industrial real estate market.

The infill Southern California industrial real estate sector has continued to exhibit strong fundamentals. These high-barrier infill markets are characterized by a relative scarcity of available product, operating at above 98% occupancy, coupled with limited ability to introduce new supply due to high land and development costs and a dearth of developable land in markets experiencing a net reduction in supply as more industrial property is converted to non-industrial uses than can be delivered. Consequently, available industrial supply continues to decrease in many of our target infill submarkets, landlord concessions are at cyclically low levels and construction deliveries are falling short of demand. Meanwhile, underlying tenant demand within our infill target markets continues to demonstrate growth, illustrated or driven by strong re-leasing spreads, an expanding regional economy, substantial growth in e-commerce transaction and delivery volumes, as well as further compression of delivery time-frames to consumers and to businesses, increasing the significance of last-mile facilities for timely fulfillment. Despite potential concerns related to global growth, tax reform and changes to trade and tariff policies and the impact of rising interest rates, we continue to observe a number of positive trends within our target infill markets. Based on current observations, we expect these positive trends will continue through the remainder of 2018.

In Los Angeles County, strong market fundamentals continued into the third quarter of 2018. High tenant demand kept vacancy at historically low levels and average asking lease rates reached a new record high. Current market conditions indicate rents are likely to continue their upward trend through the remainder of 2018, as occupancy remains at near capacity levels and new development remains limited by a lack of land availability and increases in land and development costs.

In Orange County, market fundamentals continued to be favorable during the third quarter of 2018. With steady tenant demand and a continued low availability of industrial product in this region, average asking lease rents reached a record high and vacancy remained unchanged quarter-over-quarter. Current regional market conditions indicate the potential for continued rental growth through the remainder of 2018.

In San Diego, new pre-leased construction deliveries drove net absorption and average asking leasing rates to record highs and caused overall vacancy to decrease quarter-over-quarter.

In Ventura County, vacancy and asking lease rates increased slightly quarter-over-quarter.

Lastly, in the Inland Empire, new industrial product continues to be absorbed well in the market. In the Inland Empire West, which contains the infill markets in which we operate, vacancy remained low and asking lease rates increased slightly quarter-over-quarter. We expect the outlook for the Inland Empire West to be positive through the remainder of 2018. We generally do not focus on properties located within the Inland Empire East sub-market where the development and construction pipeline for new supply is substantial.

Acquisitions and Value-Add Repositioning of Properties

The Company’s growth strategy comprises acquiring leased, stabilized properties as well as properties with value-add opportunities to improve functionality and to deploy our value-driven asset management programs in order to increase cash flow and value. Additionally, from time to time, we may acquire land parcels or properties with excess land where we may construct new buildings, although we don’t anticipate this to be a substantial part of our operations. Acquisitions may comprise single property investments as well as the purchase of portfolios of properties, with transaction values ranging from sub-$10 million dollar single-property investments to portfolios potentially valued in the billions of dollars. The Company’s geographic focus remains infill Southern California. However, from time-to-time, portfolios could be acquired comprising a critical mass of infill Southern California industrial property that could include some assets located in markets outside of infill Southern California. In general, to the extent non-infill-Southern California assets were to be acquired as part of a larger portfolio, the Company may underwrite such investments with the potential to dispose such assets over a certain period of time in order to maximize its core focus on infill Southern California, while endeavoring to take appropriate steps to satisfy REIT safe harbor requirements to avoid prohibited transactions under REIT tax laws.

A key component of our growth strategy is to acquire properties through off-market and lightly marketed transactions that are often operating at below-market occupancy or below-market rent at the time of acquisition or that have near-term lease roll-over or that provide opportunities to add value through functional or physical repositioning and improvements. Through various redevelopment, repositioning, and professional leasing and marketing strategies, we seek to increase the properties’ functionality and attractiveness to prospective tenants and, over time, to stabilize the

properties at occupancy rates that meet or exceed market rates.

A repositioning can consist of a range of improvements to a property. This may include a complete structural renovation of a property whereby we convert large underutilized spaces into a series of smaller and more functional spaces, or it may include the creation of additional square footage, the modernization of the property site, the elimination of functional obsolescence, the addition or enhancement of loading areas and truck access, the enhancement of fire-life-safety systems or other accretive improvements. Because each repositioning effort is unique and determined based on the property, targeted tenants and overall trends in the general market and specific submarket, the timing and effect of the repositioning on our rental

revenue and occupancy levels will vary, and, as a result, will affect the comparison of our results of operations from period to period with limited predictability.

As of September 30, 2018, eight of our properties were in various stages of repositioning or development and three of our properties were in the lease-up stage. In addition, we anticipate beginning repositioning work on one additional property in early 2019. The table below sets forth a summary of these properties, as well as the three projects that were stabilized during the current year. In addition to the properties in the table below, we also have a range of smaller spaces in value-add repositioning or renovation, that due to their smaller size and relatively nominal amount of down-time, are not presented below, however, in the aggregate, may be substantial.

Property (Submarket)	Market	Total Property Rentable Square Feet	Vacant Rentable Square Feet Under Repositioning/Lease-up	Estimated New Development Rentable Square Feet	Estimated Construction Period[1] Start	Completion	Total Property Leased % at 9/30/18
Current Repositioning:							
28901-28903 Avenue Paine (SF Valley)	LA	—	—	115,817	1Q-2017	3Q-2019	—%
2722 Fairview Street (OC Airport)	OC	116,575	58,802	—	1Q-2018	4Q-2018	50%
851 Lawrence Drive (Ventura)[2]	VC	49,976	49,976	39,294 [2]	2Q-2018	3Q-2019	—%
1580 West Carson Street (South Bay)	LA	43,787	43,787	—	2Q-2018	4Q-2018	—%
1998 Surveyor Avenue (Ventura)[3]	VC	—	—	56,306 [3]	2Q-2018	1Q-2019	100% [3]
9615 Norwalk Boulevard (Mid-Counties)[4]	LA	38,362	12,000	189,808 [4]	3Q-2018	2Q-2020	69%
29003 Avenue Sherman (SF Valley)	LA	68,123	49,166	—	3Q-2018	2Q-2019	28%
3233 Mission Oaks Boulevard - Unit 3233 (Ventura)	VC	461,210	109,129	—	2Q-2017	4Q-2018	73%
Total		778,033	322,860	401,225			
Lease-up Stage:							
14748-14750 Nelson Avenue - (San Gabriel Valley)	LA	201,990	47,590	—	3Q-2016	3Q-2018	76%
28901-28903 Avenue Paine (SF Valley)	LA	111,935	111,935	—	1Q-2017	3Q-2018	100% [5]
15401 Figueroa Street (South Bay)	LA	38,584	38,584	—	2Q-2018	3Q-2018	—%
Total		352,509	198,109	—			
Future Repositioning:							
	LA	108,500	—	—	1Q-2019	TBD	89%

16121 Carmenita Road (Mid-Counties)							
Total Current Repositioning, Lease-up Stage and Future Repositioning			520,969	401,225			
Stabilized:[6]							
3233 Mission Oaks Boulevard - Unit H (Ventura)	VC	461,210	—	—	--	--	73%
1601 Alton Parkway (OC Airport)	OC	124,988	15,874	—	--	--	87%
301-445 Figueroa Street (South Bay)	LA	133,650	—	—	--	--	100%

(1) The estimated construction period is subject to change as a result of a number of factors including but not limited to permit requirements, delays in construction, changes in scope, and other unforeseen circumstances.

(2) We expect to demolish the existing 49,976 rentable square foot building and construct a new 89,270 rentable square foot multi-unit building.

(3) We acquired 1998 Surveyor Avenue as an under-construction building for a cost of $5.8 million and the assumption of the seller’s fixed-price construction contracts which had $4.4 million of remaining costs at acquisition. At completion, the property will be one single-tenant building containing 56,306 rentable square feet. As of September 30, 2018, the property has been pre-leased with an estimated lease commencement date of January 15, 2019.

43

(4) 9615 Norwalk Boulevard includes 10.26 acres of partially paved storage-yard/industrial land and three buildings totaling 38,362 rentable square feet. A tenant is currently leasing the 26,362 rentable square foot building on a month-to-month basis and the land through a lease that expires on June 30, 2019, for $66,000 of base rent per month. We expect to demolish the occupied 26,362 rentable square foot building and the two vacant buildings totaling 12,000 rentable square feet prior to constructing a new 201,808 rentable square foot building.

(5) As of September 30, 2018, the repositioning portion of the property located at 28903 Avenue Paine has been leased to a single-tenant with a lease commencement date of December 31, 2018.

(6) We consider a repositioning property to be stabilized at the earlier of the following: (i) upon reaching 90% occupancy or (ii) one year from the date of completion of repositioning construction work.

Properties that are nonoperational as a result of repositioning or redevelopment activity may qualify for varying levels of interest, insurance and real estate tax capitalization during the development and construction period. An increase in our repositioning and redevelopment activities resulting from value-add acquisitions could cause an increase in the asset balances qualifying for interest, insurance and tax capitalization in future periods. We capitalized $0.7 million and $1.6 million of interest expense and $0.2 million and $0.7 million of insurance and real estate tax expenses during the three and nine months ended September 30, 2018, respectively, related to our repositioning and redevelopment projects.

Rental Revenues

Our operating results depend primarily upon generating rental revenue from the properties in our portfolio. The amount of rental revenue generated by these properties is affected by our ability to maintain or increase occupancy levels and rental rates at our properties, which will depend upon our ability to lease vacant space and re-lease expiring space at favorable rates.

Occupancy Rates

As of September 30, 2018, our consolidated portfolio, inclusive of space in repositioning as described in the subsequent paragraph, was approximately 95.1% occupied, while our stabilized consolidated portfolio exclusive of such space was approximately 97.6% occupied. We believe the opportunity to increase occupancy at our properties will be an important driver of future revenue growth. An opportunity to drive this growth will derive from the lease-up of recently completed repositioning projects and the completion and lease-up of repositioning and development projects that are currently under construction.

As summarized in the table under “Acquisitions and Value-Add Repositioning of Properties” above, as of September 30, 2018, 11 of our properties with a combined 0.5 million vacant rentable square feet, were in various stages of redevelopment, repositioning or lease-up. Vacant repositioning space and lease-up space at these 11 properties are concentrated in our Los Angeles, Orange County and Ventura markets, and represent 2.5% of our total consolidated portfolio square footage as of September 30, 2018. Including vacant repositioning space and lease-up space at these 11 properties, our weighted average occupancy rate as of September 30, 2018, in Los Angeles, Orange County and Ventura was 95.1%, 95.1% and 89.0%, respectively. Excluding vacant repositioning space and lease-up space at these 11 properties, our weighted average occupancy rate as of September 30, 2018, in these markets was 98.0%, 97.3% and 97.7%, respectively. We believe that a significant portion of our long-term future growth will come from the completion of these projects currently under repositioning, as well as through the identification or acquisition of new opportunities for redevelopment and repositioning, whether in our existing portfolio or through new investments, which may vary from period to period subject to market conditions.

The occupancy rate of properties not undergoing repositioning is affected by regional and local economic conditions in our Southern California infill markets. In recent years, the Los Angeles, Orange and San Diego county markets have continued to show historically low vacancy and positive absorption, resulting from high tenant demand combined with low product availability. Accordingly, our properties in these markets have exhibited a similar trend. We expect general market conditions to remain positive throughout the remainder of 2018, and believe the opportunity to increase occupancy and rental rates at our properties will be an important driver of future revenue growth.

44

Leasing Activity and Rental Rates

The following tables set forth our leasing activity for new and renewal leases for the nine months ended September 30, 2018:

Quarter	New Leases Number of Leases	Rentable Square Feet	Weighted Average Lease Term (in years)	Effective Rent Per Square Foot[1]	GAAP Leasing Spreads[2][4]	Cash Leasing Spreads[3][4]
Q1-2018	47	281,844	4.8	$ 11.29	32.0 %	18.1 %
Q2-2018	61	300,591	4.5	$ 12.22	28.3 %	19.2 %
Q3-2018	48	583,257	5.2	$ 11.49	46.9 %	34.1 %
Total/Weighted Average	156	1,165,692	4.9	$ 11.63	36.5 %	24.2 %

Quarter	Renewals Number of Leases	Rentable Square Feet	Weighted Average Lease Term (in years)	Effective Rent Per Square Foot[1]	GAAP Leasing Spreads[2][5]	Cash Leasing Spreads[3][5]	Expiring Leases Number of Leases	Expiring Leases Rentable Square Feet[6]	Retention %[7] Rentable Square Feet
Q1-2018	70	566,551	2.8	$ 10.66	23.1 %	13.8 %	119	913,468	68.4 %
Q2-2018	67	542,902	4.0	$ 10.69	37.5 %	25.2 %	108	833,946	70.7 %
Q3-2018	58	360,430	3.2	$ 14.80	25.2 %	14.8 %	105	782,403	55.0 %
Total/Weighted Average	195	1,469,883	3.4	$ 11.69	28.4 %	17.8 %	332	2,529,817	65.0 %

(1) Effective rent per square foot is the average base rent calculated in accordance with GAAP, over the term of the lease, expressed in dollars per square foot per year. Includes all new and renewal leases that were executed during the quarter.

(2) Calculated as the change between GAAP rents for new or renewal leases and the expiring GAAP rents on the expiring leases for the same space.

(3) Calculated as the change between starting cash rents for new or renewal leases and the expiring cash rents on the expiring leases for the same space.

(4) The GAAP and cash re-leasing spreads for new leases executed during the nine months ended September 30, 2018, exclude 56 leases aggregating 684,052 rentable square feet for which there was no comparable lease data. Of these 56 excluded leases, 23 leases aggregating 426,123 rentable square feet are leases of recently repositioned space. Comparable leases generally exclude: (i) space that has never been occupied under our ownership, (ii) recently repositioned/redeveloped space, (iii) space that has been vacant for over one year or (iv) space with lease terms shorter than six months.

(5) The GAAP and cash re-leasing rent spreads for renewal leases executed during the nine months ended September 30, 2018, exclude nine leases for 84,517 rentable square feet for which there was no comparable lease data. Comparable leases generally exclude: (i) space with different lease structures or (ii) space with lease terms shorter than six months.

(6) Includes seven leases totaling 181,512 rentable square feet that expired during the nine months ended September 30, 2018, for which the space was placed into repositioning after each tenant vacated.

(7) Retention is calculated as renewal lease square footage plus relocation/expansion square footage, divided by the square footage of leases expiring during the period. Retention excludes expiring leases associated with space that is placed into repositioning after the tenant vacates.

Our leasing activity is impacted both by our redevelopment and repositioning efforts, as well as by market conditions. While we reposition a property, its space may become unavailable for leasing until completion of our repositioning efforts. During the nine months ended September 30, 2018, we stabilized 3233 Mission Oaks Boulevard - Unit H and

301-445 Figueroa Street with a combined 177,577 rentable square feet, and leased or pre-leased an additional 322,641 rentable square feet at 14748-14750 Nelson Avenue, 28903 Avenue Paine and 1998 Surveyor Avenue. As of the date of this filing, we have eight repositioning and development projects with estimated construction completion periods ranging from the fourth quarter of

45

2018 to the second quarter of 2020 and three properties in the lease-up stage with space available for lease. We expect these properties to have positive impacts on our leasing activity and revenue generation as we complete our value-add repositioning plans and place these properties in service.

Scheduled Lease Expirations

Our ability to re-lease space subject to expiring leases is affected by economic and competitive conditions in our markets and by the relative desirability of our individual properties, which may impact our results of operations. The following table sets forth a summary schedule of lease expirations for leases in place as of September 30, 2018, for each of the 10 full and partial calendar years beginning with 2018 and thereafter, plus space that is available and under current repositioning.

Year of Lease Expiration	Number of Leases Expiring	Total Rentable Square Feet[1]	Percentage of Total Owned Square Feet		Annualized Base Rent[2]	Percentage of Total Annualized Base Rent[3]		Annualized Base Rent per Square Foot[4]
Vacant[5]	—	678,856	3.3	%	$ —	—	%	$ —
Current Repositioning[6]	—	322,860	1.6	%	$ —	—	%	$ —
MTM Tenants[7]	76	139,384	0.7	%	$ 1,803	1.0	%	$ 12.93
Remainder of 2018	74	556,933	2.7	%	$ 5,690	3.2	%	$ 10.22
2019	315	2,822,599	13.8	%	$ 26,525	14.8	%	$ 9.40
2020	332	4,127,843	20.1	%	$ 35,948	20.0	%	$ 8.71
2021	275	4,433,008	21.6	%	$ 38,790	21.6	%	$ 8.75
2022	121	2,110,388	10.3	%	$ 18,820	10.5	%	$ 8.92
2023	112	2,024,792	9.9	%	$ 20,946	11.7	%	$ 10.34
2024	17	770,826	3.8	%	$ 7,465	4.2	%	$ 9.68
2025	11	269,578	1.3	%	$ 2,985	1.7	%	$ 11.07
2026	6	273,904	1.2	%	$ 3,244	1.8	%	$ 11.85
2027	6	220,311	1.1	%	$ 2,092	1.2	%	$ 9.49
Thereafter	11	1,753,875	8.6	%	$ 14,893	8.3	%	$ 8.49
Total Consolidated Portfolio	1,356	20,505,157	100.0	%	$ 179,201	100.0	%	$ 9.19

(1) Represents the contracted square footage upon expiration.

(2) Calculated as monthly contracted base rent (before rent abatements) per the terms of such lease, as of September 30, 2018, multiplied by 12. Excludes billboard and antenna revenue. Amounts in thousands.

(3) Calculated as annualized base rent set forth in this table divided by annualized base rent for the total portfolio as of September 30, 2018.

(4) Calculated as annualized base rent for such leases divided by the occupied square feet for such leases as of September 30, 2018.

(5) Represents vacant space (not under repositioning) as of September 30, 2018. Includes new leases aggregating 186,483 rentable square feet that have been signed but had not yet commenced as of September 30, 2018.

(6) Represents vacant space at eight of our properties that were classified as current repositioning as of September 30, 2018. Refer to the table under "Acquisitions and Value-Add Repositioning of Properties" for a summary of these properties. Excludes stabilized properties and properties in lease-up.

(7) Represents tenants under month-to-month ("MTM") leases or having holdover tenancy. Of the 76 MTM leases, 67 MTM leases aggregating 63,490 rentable square feet are at our property located at 14723-14825 Oxnard Street, where due to number and the small size of spaces, we typically only enter into MTM leases.

As of September 30, 2018, in addition to 0.7 million rentable square feet of currently available space in our portfolio and 0.3 million rentable square feet of vacant space under current repositioning, leases representing 2.7% and 13.8% of the aggregate rentable square footage of our portfolio are scheduled to expire during the remainder of 2018 and 2019, respectively. During the nine months ended September 30, 2018, we renewed 195 leases for 1,469,883 rentable square feet, resulting in a 65.0% retention rate. Our retention rate during the period was impacted by our strategy to

roll certain tenants at below-market rents and to replace them with higher quality tenants paying higher rents with minimal down time. During the nine months ended September 30, 2018, new and renewal leases had a weighted average term of 4.9 and 3.4 years, respectively, and we expect future new and renewal leases to have similar terms.

The leases scheduled to expire during the remainder of 2018 and 2019 represent approximately 3.2% and 14.8% respectively, of the total annualized base rent for our portfolio as of September 30, 2018. We estimate that, on a weighted average basis, in-place rents of leases scheduled to expire during the remainder of 2018 and 2019 are currently below current market asking rents, although individual units or properties within any particular submarket may currently be leased either above, below, or at the current market asking rates within that submarket. As described in the above Market Fundamentals section, we expect market dynamics to remain strong and that these positive trends will provide a favorable environment for additional increases in lease renewal rates. Accordingly, we expect the remainder of 2018 will show positive renewal rates and leasing spreads. We also currently do not see any reason not to expect that 2019 lease expirations will show positive growth upon renewal; however, it is difficult to predict market conditions that far into the future.

Property Expenses

Our property expenses generally consist of utilities, real estate taxes, insurance, site repair and maintenance costs, and the allocation of overhead costs. For the majority of our properties, our property expenses are recovered, in part, by either the triple net provisions or modified gross expense reimbursements in tenant leases. The majority of our leases also comprise contractual three percent annual rental rate increases meant, in part, to help mitigate potential increases in property expenses over time. However, the terms of our leases vary, and, in some instances, we may absorb property expenses. Our overall financial results will be impacted by the extent to which we are able to pass-through property expenses to our tenants.

Taxable REIT Subsidiary

As of September 30, 2018, our Operating Partnership indirectly and wholly owns Rexford Industrial Realty and Management, Inc., which we refer to as the services company. We have elected, together with our services company, to treat our services company as a taxable REIT subsidiary for federal income tax purposes. A taxable REIT subsidiary generally may provide non-customary and other services to our tenants and engage in activities that we may not engage in directly without adversely affecting our qualification as a REIT, provided a taxable REIT subsidiary may not operate or manage a lodging facility or health care facility or provide rights to any brand name under which any lodging facility or health care facility is operated. We may form additional taxable REIT subsidiaries in the future, and our Operating Partnership may contribute some or all of its interests in certain wholly owned subsidiaries or their assets to our services company. Any income earned by our taxable REIT subsidiaries will not be included in our taxable income for purposes of the 75% or 95% gross income tests, except to the extent such income is distributed to us as a dividend, in which case such dividend income will qualify under the 95%, but not the 75%, gross income test. Because a taxable REIT subsidiary is subject to federal income tax, and state and local income tax (where applicable) as a regular corporation, the income earned by our taxable REIT subsidiaries generally will be subject to an additional level of tax as compared to the income earned by our other subsidiaries. Our taxable REIT subsidiary is a C-corporation subject to federal and state income tax, however it has a cumulative unrecognized net operation loss carryforward and therefore there is no income tax provision for the nine months ended September 30, 2018 and 2017.

Critical Accounting Policies

In our 2017 Annual Report on Form 10-K, we identified certain critical accounting policies that affect certain of our more significant estimates and assumptions used in preparing our consolidated financial statements. We have not made any material changes to our critical accounting policies during the period covered by this report.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions in certain circumstances that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses for the reporting periods. Actual amounts may differ from these estimates and assumptions. Management evaluates these estimates on an ongoing basis, based upon information currently available and on various assumptions that it believes are reasonable as of the date hereof. In addition, other companies in similar businesses may use different estimation policies and methodologies, which may affect the comparability of our results of operations and financial condition to those of other companies. See Note 2 to our consolidated financial statements for a discussion of our accounting policies.

Results of Operations

Our consolidated results of operations are often not comparable from period to period due to the effect of property acquisitions and dispositions completed during the comparative reporting periods. Our “Total Portfolio” represents all of the properties owned during the reported periods. To eliminate the effect of changes in our Total Portfolio due to acquisitions and dispositions and to highlight the operating results of our on-going business, we have separately presented the results of our “Same Properties Portfolio.”

For the three and nine months ended September 30, 2018 and 2017, our Same Properties Portfolio includes all properties in our industrial portfolio that were wholly-owned by us as of January 1, 2017, and still owned by us as of September 30, 2018, which consisted of 127 properties aggregating approximately 14.2 million rentable square feet. Results for our Same Properties Portfolio exclude any properties that were acquired or sold during the period from January 1, 2017 through September 30, 2018, interest income, interest expense and corporate general and administrative expenses. In addition to the properties included in our Same Properties Portfolio, our Total Portfolio includes the 41 properties aggregating approximately 6.5 million rentable square feet that were purchased between January 1, 2017 and September 30, 2018, and the 11 properties aggregating approximately 1.0 million rentable square feet that were sold between January 1, 2017 and September 30, 2018.
As of September 30, 2018 and 2017, our Same Properties Portfolio occupancy was approximately 96.8% and 93.1%, respectively. For the three months ended September 30, 2018 and 2017, our Same Properties Portfolio weighted average occupancy was approximately 96.4% and 92.6%, respectively. Comparatively, for the nine months ended September 30, 2018 and 2017, our Same Properties Portfolio weighted average occupancy was approximately 95.7% and 93.2%, respectively.

Comparison of the Three Months Ended September 30, 2018 to the Three Months Ended September 30, 2017
The following table summarizes the historical results of operations for our Same Properties Portfolio and Total Portfolio for the three months ended September 30, 2018 and 2017 (dollars in thousands):

	Same Properties Portfolio Three Months Ended September 30,		Increase/(Decrease)	% Change	Total Portfolio Three Months Ended September 30,		Increase/(Decrease)	% Change
	2018	2017			2018	2017		
RENTAL REVENUES								
Rental income	$32,158	$29,465	$ 2,693	9.1 %	$45,661	$36,748	$ 8,913	24.3 %
Tenant reimbursements	5,577	4,821	756	15.7 %	8,508	6,279	2,229	35.5 %
Other income	241	146	95	65.1 %	300	203	97	47.8 %
TOTAL RENTAL REVENUES	37,976	34,432	3,544	10.3 %	54,469	43,230	11,239	26.0 %
Management, leasing and development services	—	—	—	— %	116	109	7	6.4 %
Interest income	—	—	—	— %	609	—	609	— %
TOTAL REVENUES	37,976	34,432	3,544	10.3 %	55,194	43,339	11,855	27.4 %
EXPENSES								
Property expenses	9,170	8,851	319	3.6 %	13,294	11,229	2,065	18.4 %
General and administrative	—	—	—	— %	6,229	5,843	386	6.6 %
Depreciation and amortization	12,139	12,318	(179)	(1.5)%	20,144	17,971	2,173	12.1 %
TOTAL OPERATING EXPENSES	21,309	21,169	140	0.7 %	39,667	35,043	4,624	13.2 %
OTHER EXPENSES								
Acquisition expenses	—	—	—	— %	106	16	90	562.5%
Interest expense	—	—	—	— %	6,456	6,271	185	3.0 %
TOTAL OTHER EXPENSES	—	—	—	— %	6,562	6,287	275	4.4 %
TOTAL EXPENSES	21,309	21,169	140	0.7 %	46,229	41,330	4,899	11.9 %
NET INCOME	$16,667	$13,263	$ 3,404		$8,965	$2,009	$ 6,956	

Rental Income

Our Same Properties Portfolio and Total Portfolio rental income increased by $2.7 million, or 9.1%, and $8.9 million, or 24.3%, respectively, during the three months ended September 30, 2018, compared to the three months ended September 30, 2017. The increase in our Same Properties Portfolio rental income is primarily due to the increase in the weighted average occupancy of the portfolio for comparable periods, which was partially driven by the completion of repositioning and development work and subsequent lease-up of space at six of these properties between July 1, 2017 and September 30, 2018, and the increase in average rental rates on new and renewal leases. Our Total Portfolio rental income was also positively impacted by the incremental revenues from the 41 properties we acquired between January 1, 2017, and September 30, 2018.

Tenant Reimbursements

Our Same Properties Portfolio and Total Portfolio tenant reimbursements revenue increased by $0.8 million, or 15.7%, and $2.2 million, or 35.5%, respectively, during the three months ended September 30, 2018, compared to the three months ended September 30, 2017. The increase in our Same Properties Portfolio tenant reimbursements is primarily due to an increase in recoverable operating expenses for comparable periods, timing differences in completing prior year recoverable expense reconciliations for comparable periods and an increase in the weighted average occupancy for comparable periods, which was partially driven by the completion of repositioning and development work and subsequent lease-up of space at six of these properties between July 1, 2017 and September 30, 2018. Our Total Portfolio tenant reimbursements revenue was also impacted by the incremental reimbursements from the 41 properties we acquired between January 1, 2017 and September 30, 2018.

Other Income

Our Same Properties Portfolio and Total Portfolio other income increased by $0.1 million, or 65.1%, and $0.1 million, or 47.8%, respectively, during the three months ended September 30, 2018, compared to the three months ended September 30, 2017, primarily due an increase in tenant legal fee reimbursement income and late fee income.

Management, Leasing and Development Services

Our Total Portfolio management, leasing and development services revenue increased by $7 thousand, or 6.4%, during the three months ended September 30, 2018, compared to the three months ended September 30, 2017.

Interest Income

Interest income increased from zero to $0.6 million during the three months ended September 30, 2018, compared to the three months ended September 30, 2017, due to the investment of excess cash in money market accounts during the current period.

Property Expenses

Our Same Properties Portfolio and Total Portfolio property expenses increased by $0.3 million, or 3.6%, and $2.1 million, or 18.4%, respectively, during the three months ended September 30, 2018, compared to the three months ended September 30, 2017. The increase in our Same Properties Portfolio property expenses is primarily due to an increase in real estate tax expense and an increase in allocated overhead costs, partially offset by a decrease in repairs and maintenance expense. Our Total Portfolio property expenses was also impacted by incremental expenses from the 41 properties we acquired between January 1, 2017, and September 30, 2018.

General and Administrative

Our Total Portfolio general and administrative expenses increased by $0.4 million, or 6.6%, during the three months ended September 30, 2018, compared to the three months ended September 30, 2017, primarily due an increase in non-cash equity compensation expense related to equity grants made in December 2017, and increases in non-employee director fees and professional tax service expense, partially offset by a decrease in accrued bonus expense due to an adjustment in the third quarter of 2017 to increase year-to-date performance-based bonus accruals for our named executive officers, and a decrease in other professional fees.

Depreciation and Amortization

Our Same Properties Portfolio depreciation and amortization expense decreased by $0.2 million, or 1.5%, during the three months ended September 30, 2018, compared to the three months ended September 30, 2017, primarily due to acquisition-related tenant improvements and in-place lease intangibles becoming fully depreciated at certain of our properties subsequent to July 1, 2017, partially offset by an increase in depreciation expense related to capital improvements placed into service subsequent to July 1, 2017. Our Total Portfolio depreciation and amortization expense increased $2.2 million, or 12.1%, during the three months ended September 30, 2018, compared to the three months ended September 30, 2017, primarily due to the incremental expense from the 41 properties we acquired between January 1, 2017, and September 30, 2018, partially offset by the decrease in our Same Properties Portfolio depreciation and amortization expense noted above.

Acquisition Expenses

Our Total Portfolio acquisition expenses increased by $0.1 million, or 562.5%, during the three months ended September 30, 2018, compared to the three months ended September 30, 2017, due to an increase in acquisition related costs incurred that did not result in completed transactions.

Interest Expense

Our Total Portfolio interest expense increased by $0.2 million, or 3.0%, during the three months ended September 30, 2018, compared to the three months ended September 30, 2017. The increase in interest expense is primarily comprised of the following: (i) a $1.4 million increase related to the $150.0 million term loan facility borrowing we made in May 2018 and (ii) a $0.2 million increase related to the $125.0 million of 3.93% fixed rate senior notes we issued in July 2017. These increases were partially offset by the following: (i) a $1.1 million decrease in interest related to a reduction of outstanding borrowings on our unsecured revolving credit facility and (ii) a $0.3 million increase in capitalized interest related to our repositioning and development properties.

Comparison of the Nine Months Ended September 30, 2018 to the Nine Months Ended September 30, 2017

The following table summarizes the historical results of operations for our Same Properties Portfolio and Total Portfolio for the nine months ended September 30, 2018 and 2017 (dollars in thousands):

	Same Properties Portfolio				Total Portfolio			
	Nine Months Ended September 30,		Increase/(Decrease)	%	Nine Months Ended September 30,		Increase/(Decrease)	%
	2018	2017		Change	2018	2017		Change
RENTAL REVENUES								
Rental income	$95,036	$87,039	$ 7,997	9.2 %	$130,139	$97,494	$ 32,645	33.5 %
Tenant reimbursements	15,980	14,708	1,272	8.6 %	23,733	16,606	7,127	42.9 %
Other income	568	468	100	21.4 %	646	550	96	17.5 %
TOTAL RENTAL REVENUES	111,584	102,215	9,369	9.2 %	154,518	114,650	39,868	34.8 %
Management, leasing and development services	—	—	—	— %	359	380	(21)	(5.5)%
Interest income	—	—	—	— %	609	445	164	36.9 %
TOTAL REVENUES	111,584	102,215	9,369	9.2 %	155,486	115,475	40,011	34.6 %
EXPENSES								
Property expenses	27,282	26,161	1,121	4.3 %	38,029	29,987	8,042	26.8 %
General and administrative	—	—	—	— %	18,897	16,052	2,845	17.7 %
Depreciation and amortization	36,830	37,714	(884)	(2.3)%	59,371	46,085	13,286	28.8 %
TOTAL OPERATING EXPENSES	64,112	63,875	237	0.4 %	116,297	92,124	24,173	26.2 %
OTHER EXPENSES								
Acquisition expenses	—	—	—	— %	152	421	(269)	(63.9)%
Interest expense	—	—	—	— %	18,760	14,571	4,189	28.7 %
TOTAL OTHER EXPENSES	—	—	—	— %	18,912	14,992	3,920	26.1 %
TOTAL EXPENSES	64,112	63,875	237	0.4 %	135,209	107,116	28,093	26.2 %
Equity in income from unconsolidated real estate entities	—	—	—		—	11	(11)	
Loss on extinguishment of debt	—	—	—		—	(22)	22	
Gain on sale of real estate	—	—	—		11,591	19,237	(7,646)	
NET INCOME	$47,472	$38,340	$ 9,132		$31,868	$27,585	$ 4,283	

Rental Income

Our Same Properties Portfolio and Total Portfolio rental income increased by $8.0 million, or 9.2%, and $32.6 million, or 33.5%, respectively, during the nine months ended September 30, 2018, compared to the nine months ended September 30, 2017. The increase in our Same Properties Portfolio rental income is primarily due to the increase in the weighted average occupancy of the portfolio for comparable periods, which was driven by the completion of repositioning and development work and subsequent lease-up of space at eight of these properties between January 1, 2017, and September 30, 2018, and the increase in average rental rates on new and renewal leases. Our Total Portfolio rental income was also positively impacted by the incremental revenues from the 41 properties we acquired between January 1, 2017, and September 30, 2018.

51

Tenant Reimbursements
Our Same Properties Portfolio and Total Portfolio tenant reimbursements revenue increased by $1.3 million, or 8.6%, and $7.1 million, or 42.9%, respectively, during the nine months ended September 30, 2018, compared to the nine months ended September 30, 2017. The increase in our Same Properties Portfolio tenant reimbursements is primarily due to an increase in recoverable operating expenses for comparable periods and an increase in the weighted average occupancy for comparable periods, which was partially driven by the completion of repositioning and development work and subsequent lease-up of space at eight of these properties between January 1, 2017 and September 30, 2018. Our Total Portfolio tenant reimbursements revenue was also impacted by the incremental reimbursements from the 41 properties we acquired between January 1, 2017 and September 30, 2018.
Other Income
Our Same Properties Portfolio other income increased by $0.1 million, or 21.4%, and our Total Portfolio other income decreased by $0.1 million, or 17.5%, during the nine months ended September 30, 2018, compared to the nine months ended September 30, 2017, primarily due an increase in tenant legal fee reimbursement income.
Management, Leasing and Development Services
Our Total Portfolio management, leasing and development services revenue decreased by $21 thousand, or 5.5%, during the nine months ended September 30, 2018, compared to the nine months ended September 30, 2017.
Interest Income
Interest income of $0.6 million for the nine months ended September 30, 2018, was earned from the investment of excess cash in money market accounts. Interest income of $0.4 million for the nine months ended September 30, 2017, relates to a $6.0 million mortgage loan that we made on July 1, 2016, which was subsequently repaid on June 23, 2017. The loan was secured by an industrial property located in Rancho Cucamonga, California and bore interest at 10.0% per annum.
Property Expenses
Our Same Properties Portfolio and Total Portfolio property expenses increased by $1.1 million, or 4.3%, and $8.0 million, or 26.8%, respectively, during the nine months ended September 30, 2018, compared to the nine months ended September 30, 2017. The increase in our Same Properties Portfolio property expenses is primarily due to an increase in real estate tax expense and an increase in insurance expense due to a new earthquake policy we obtained in June 2017, partially offset by a decrease in allocated overhead costs. Our Total Portfolio property expenses was also impacted by incremental expenses from the 41 properties we acquired between January 1, 2017, and September 30, 2018.
General and Administrative
Our Total Portfolio general and administrative expenses increased $2.8 million, or 17.7%, during the nine months ended September 30, 2018, compared to the nine months ended September 30, 2017, primarily due an increase in non-cash equity compensation expense related to equity grants made in December 2017, an increase in accrued bonus expense, an increase in other various corporate expenses, an increase in legal expense and an increase in professional audit and tax services expense.
Depreciation and Amortization
Our Same Properties Portfolio depreciation and amortization expense decreased by $0.9 million, or 2.3%, during the nine months ended September 30, 2018, compared to the nine months ended September 30, 2017, primarily due to acquisition-related tenant improvements and in-place lease intangibles becoming fully depreciated at certain of our properties subsequent to January 1, 2017, partially offset by an increase in depreciation expense related to capital improvements placed into service subsequent to January 1, 2017. Our Total Portfolio depreciation and amortization expense increased $13.3 million, or 28.8%, during the nine months ended September 30, 2018, compared to the nine months ended September 30, 2017, primarily due to the incremental expense from the 41 properties we acquired between January 1, 2017, and September 30, 2018, and an increase in depreciation expense related to capital improvements, partially offset by the decrease in our Same Properties Portfolio depreciation and amortization expense noted above.

Acquisition Expenses

Our Total Portfolio acquisition expenses decreased by $0.3 million, or 63.9%, during the nine months ended September 30, 2018, compared to the nine months ended September 30, 2017, primarily due to the write-off of $0.3 million of transaction costs in connection with the termination of a ground lease in March 2017.

Interest Expense

Our Total Portfolio interest expense increased by $4.2 million, or 28.7%, during the nine months ended September 30, 2018, compared to the nine months ended September 30, 2017. The increase in interest expense is primarily comprised of the following: (i) a $2.6 million increase related to the issuance of $125.0 million of 3.93% fixed rate senior notes in July 2017, and (ii) a $2.0 million increase related to the $150.0 million term loan facility borrowing we made in May 2018. These increases were partially offset by the following: (i) a $0.3 million increase in capitalized interest related to our repositioning and redevelopment properties and (ii) a $0.2 million decrease in interest related to a reduction of outstanding borrowings on our unsecured revolving credit facility.

Equity in Income from Unconsolidated Real Estate Entities

Equity in income from unconsolidated real estate entities of $11 thousand for the nine months ended September 30, 2017, represents the final liquidating distribution we received in connection with the winding down of our joint venture.

Loss on Extinguishment of Debt

On March 20, 2017, we repaid the mortgage loan secured by the property located at 1065 E. Walnut Avenue in advance of the maturity date of February 1, 2019. The loss on extinguishment of debt of $22 thousand for the nine months ended September 30, 2017, represents $0.2 million of prepayment penalties, partially offset by the $0.2 million write-off of the unamortized loan premium.

Gain on Sale of Real Estate

For the nine months ended September 30, 2018, we recognized a total gain on sale of real estate of $11.6 million from the disposition of five properties that were sold for an aggregate gross sales price of $37.6 million. For the nine months ended September 30, 2017, we recognized a gain on sale of real estate of $19.2 million from the disposition of three properties that were sold for an aggregate gross sales price of $65.6 million.

Non-GAAP Supplemental Measure: Funds From Operations

We calculate funds from operations ("FFO") attributable to common stockholder in accordance with the standards established by the National Association of Real Estate Investment Trusts ("NAREIT"). FFO represents net income (loss) (computed in accordance with accounting principles generally accepted in the United States ("GAAP")), excluding gains (or losses) from sales of depreciable operating property, impairment losses, real estate related depreciation and amortization (excluding amortization of deferred financing costs) and after adjustments for unconsolidated joint ventures.

Management uses FFO as a supplemental performance measure because, in excluding real estate related depreciation and amortization, gains and losses from property dispositions, and asset impairments, it provides a performance measure that, when compared year over year, captures trends in occupancy rates, rental rates and operating costs. We also believe that, as a widely recognized measure of performance used by other REITs, FFO may be used by investors as a basis to compare our operating performance with that of other REITs.

However, because FFO excludes depreciation and amortization and captures neither the changes in the value of our properties that result from use or market conditions nor the level of capital expenditures and leasing commissions necessary to maintain the operating performance of our properties, all of which have real economic effects and could materially impact our results from operations, the utility of FFO as a measure of our performance is limited. Other equity REITs may not calculate or interpret FFO in accordance with the NAREIT definition as we do, and, accordingly, our FFO may not be comparable to such other REITs' FFO. FFO should not be used as a measure of our liquidity, and is not indicative of funds available for our cash needs, including our ability to pay dividends.

The following table sets forth a reconciliation of net income, the most directly comparable financial measure calculated and presented in accordance with GAAP, to FFO (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Net income	$8,965	$2,009	$31,868	$27,585
Add:				
Depreciation and amortization	20,144	17,971	59,371	46,085
Deduct:				
Gains on sale of real estate	—	—	11,591	19,237
Gain on acquisition of unconsolidated joint venture property	—	—	—	11
Funds From Operations (FFO)	$29,109	$19,980	$79,648	$54,422
Less: preferred stock dividends	(2,423)	(1,322)	(7,270)	(3,966)
Less: FFO attributable to noncontrolling interest[(1)]	(574)	(491)	(1,693)	(1,408)
Less: FFO attributable to participating securities[(2)]	(165)	(133)	(476)	(408)
FFO attributable to common stockholders	$25,947	$18,034	$70,209	$48,640

(1) Noncontrolling interests represent holders of outstanding common units of the Company's operating partnership that are owned by unit holders other than the Company.

(2) Participating securities include unvested shares of restricted stock, unvested LTIP units and unvested performance units.

Non-GAAP Supplemental Measure: NOI and Cash NOI

Net operating income ("NOI") is a non-GAAP measure which includes the revenue and expense directly attributable to our real estate properties. NOI is calculated as total revenue from real estate operations including i) rental income ii) tenant reimbursements, and iii) other income less property expenses (before interest expense, depreciation and amortization).

We use NOI as a supplemental performance measure because, in excluding real estate depreciation and amortization expense, general and administrative expenses, interest expense, gains (or losses) on sale of real estate and other non-operating items, it provides a performance measure that, when compared year over year, captures trends in occupancy rates, rental rates and operating costs. We also believe that NOI will be useful to investors as a basis to compare our operating performance with that of other REITs. However, because NOI excludes depreciation and amortization expense and captures neither the changes in the value of our properties that result from use or market conditions, nor the level of capital expenditures and leasing commissions necessary to maintain the operating performance of our properties (all of which have real economic effect and could materially impact our results from operations), the utility of NOI as a measure of our performance is limited. Other equity REITs may not calculate NOI in a similar manner and, accordingly, our NOI may not be comparable to such other REITs' NOI. Accordingly, NOI should be considered only as a supplement to net income as a measure of our performance. NOI should not be used as a measure of our liquidity, nor is it indicative of funds available to fund our cash needs. NOI should not be used as a substitute for cash flow from operating activities in accordance with GAAP.

NOI on a cash-basis ("Cash NOI") is a non-GAAP measure, which we calculate by adding or subtracting the following items from NOI: i) fair value lease revenue and ii) straight-line rental revenue adjustments. We use Cash NOI, together with NOI, as a supplemental performance measure. Cash NOI should not be used as a measure of our liquidity, nor is it indicative of funds available to fund our cash needs. Cash NOI should not be used as a substitute for cash flow from operating activities computed in accordance with GAAP.

The following table sets forth the revenue and expense items comprising NOI and the adjustments to calculate Cash NOI (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Rental income	$45,661	$36,748	$130,139	$97,494
Tenant reimbursements	8,508	6,279	23,733	16,606
Other income	300	203	646	550
Total operating revenues	54,469	43,230	154,518	114,650
Property expenses	13,294	11,229	38,029	29,987
Net Operating Income	$41,175	$32,001	$116,489	$84,663
Amortization of (below) above market lease intangibles, net	(1,622)	(885)	(4,354)	(1,203)
Straight line rental revenue adjustment	(1,343)	(1,307)	(4,985)	(3,259)
Cash Net Operating Income	$38,210	$29,809	$107,150	$80,201

The following table sets forth a reconciliation of net income, the most directly comparable financial measure calculated and presented in accordance with GAAP, to NOI and Cash NOI (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Net income	$8,965	$2,009	$31,868	$27,585
Add:				
General and administrative	6,229	5,843	18,897	16,052
Depreciation and amortization	20,144	17,971	59,371	46,085
Acquisition expenses	106	16	152	421
Interest expense	6,456	6,271	18,760	14,571
Loss on extinguishment of debt	—	—	—	22
Deduct:				
Management, leasing and development services	116	109	359	380
Interest income	609	—	609	445
Equity in income from unconsolidated real estate entities	—	—	—	11
Gains on sale of real estate	—	—	11,591	19,237
Net Operating Income	$41,175	$32,001	$116,489	$84,663
Amortization of (below) above market lease intangibles, net	(1,622)	(885)	(4,354)	(1,203)
Straight line rental revenue adjustment	(1,343)	(1,307)	(4,985)	(3,259)
Cash Net Operating Income	$38,210	$29,809	$107,150	$80,201

Non-GAAP Supplemental Measure: EBITDAre

We calculate earnings before interest expense, income taxes, depreciation and amortization for real estate ("EBITDAre") in accordance with the standards established by NAREIT. EBITDAre is calculated as net income (loss) (computed in accordance with GAAP), before interest expense, income tax expense, depreciation and amortization, gains (or losses) from sales of depreciable operating property, impairment losses and adjustments to reflect our proportionate share of EBITDAre from our unconsolidated joint venture.

We believe that EBITDAre is helpful to investors as a supplemental measure of our operating performance as a real estate company because it is a direct measure of the actual operating results of our properties. We also use this measure in ratios to compare our performance to that of our industry peers. In addition, we believe EBITDAre is frequently used by securities analysts, investors and other interested parties in the evaluation of equity REITs. However, our industry peers may not calculate EBITDAre in accordance with the NAREIT definition as we do and, accordingly, our EBITDAre may not be comparable to our peers' EBITDAre. Accordingly, EBITDAre should be considered only as a supplement to net income (loss) as a measure of our performance.

The following table sets forth a reconciliation of net income, the most directly comparable financial measure calculated and presented in accordance with GAAP, to EBITDAre (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Net income	$8,965	$2,009	$31,868	$27,585
Interest expense	6,456	6,271	18,760	14,571
Depreciation and amortization	20,144	17,971	59,371	46,085
Gains on sale of real estate	—	—	(11,591)	(19,237)
Gain on sale of real estate from unconsolidated joint ventures	—	—	—	(11)
EBITDAre	$35,565	$26,251	$98,408	$68,993

56

Liquidity and Capital Resources

Overview

Our short-term liquidity requirements consist primarily of funds to pay for operating expenses, interest expense, general and administrative expenses, capital expenditures, tenant improvements and leasing commissions, and distributions to our common and preferred stockholders and holders of common units of partnership interests in our Operating Partnership ("OP Units"). We expect to meet our short-term liquidity requirements through available cash on hand, cash flow from operations, by drawing on our unsecured revolving credit facility and by issuing shares of common stock pursuant to our at-the-market equity offering program described below.

Our long-term liquidity needs consist primarily of funds necessary to pay for acquisitions, recurring and non-recurring capital expenditures and scheduled debt maturities. We intend to satisfy our long-term liquidity needs through net cash flow from operations, proceeds from long-term secured and unsecured financings, borrowings available under our unsecured revolving credit facility, the issuance of equity securities, including preferred stock, and proceeds from selective real estate dispositions as we identify capital recycling opportunities.

As of September 30, 2018, our cash and cash equivalents were $183.9 million, and we did not have any borrowings outstanding under our unsecured revolving credit facility, leaving $350.0 million available for future borrowings.

Sources of Liquidity

Cash Flow from Operations

Cash flow from operations is one of our key sources of liquidity and is primarily dependent upon: (i) the occupancy levels and lease rates at our properties, (ii) our ability to collect rent, (iii) the level of operating costs we incur and (iv) our ability to pass through operating expenses to our tenants. We are subject to a number of risks related to general economic and other unpredictable conditions, which have the potential to affect our overall performance and resulting cash flows from operations. However, based on our current portfolio mix and business strategy, we anticipate that we will be able to generate positive cash flows from operations.

ATM Program

On June 13, 2018, we established a new at-the-market equity offering program (the "$400 Million ATM Program") pursuant to which we may sell from time to time up to an aggregate of $400.0 million of our common stock through sales agents. The $400 Million ATM Program replaces our previous $300 million at-the-market equity offering program which was established on September 21, 2017 (the "Prior ATM Program"). All $300.0 million of shares of our common stock under the Prior ATM Program were sold prior to establishing the $400 Million ATM Program.

During the nine months ended September 30, 2018, we sold a total of 14,081,074 shares of our common stock under the $400 Million ATM Program and the Prior ATM Program, at a weighted average price of $30.70 per share, for gross proceeds of $432.3 million, and net proceeds of $425.8 million, after deducting the sales agents' fee. As of September 30, 2018, we had the capacity to issue up to an additional $196.8 million of common stock under the $400 Million ATM Program.

Future sales, if any, will depend on a variety of factors to be determined by us from time to time, including among others, market conditions, the trading price of our common stock and capital needs. We intend to use the net proceeds from the offering of shares under the $400 Million ATM Program, if any, to fund potential acquisition opportunities, repay amounts outstanding from time to time under our unsecured revolving credit facility or other debt financing obligations, to fund our development or redevelopment activities and/or for general corporate purposes.

Equity Offerings

We evaluate the capital markets on an ongoing basis for opportunities to raise capital, and as circumstances warrant, we may issue additional securities, from time to time, to fund acquisitions, for the repayment of long-term debt upon maturity and for other general corporate purposes. Any future issuance, however, is dependent upon market conditions, available pricing and capital needs and there can be no assurance that we will be able to complete any such offerings of securities.

Capital Recycling

We continuously evaluate opportunities for the potential disposition of properties in our portfolio when we believe such disposition is appropriate in view of our business objectives. In evaluating these opportunities, we consider a variety of criteria including, but not limited to, local market conditions and lease rates, asset type and location, as well as potential uses of proceeds and tax considerations. Tax considerations include entering into tax-deferred like-kind exchanges under Section 1031 of the Internal Revenue Code (“1031 Exchange”), when possible, to defer some or all of the taxable gains, if any, on dispositions.

During the nine months ended September 30, 2018, we completed the sale of five of our properties for a total gross sales price of $37.6 million and total net cash proceeds of $35.5 million. Total net cash proceeds of $26.8 million from four of the dispositions were used to partially fund the acquisition of four properties during the nine months ended September 30, 2018, through 1031 Exchange transactions.

We anticipate continuing to selectively and opportunistically dispose of properties, however, the timing of any potential future dispositions will depend on market conditions, asset-specific circumstances or opportunities, and our capital needs. Our ability to dispose of selective properties on advantageous terms, or at all, is dependent upon a number of factors including the availability of credit to potential buyers to purchase properties at prices that we consider acceptable.

Credit Facility

We have a $450.0 million senior unsecured credit facility (the “Credit Facility”), comprised of a $350.0 million unsecured revolving credit facility (the "Revolver") and a $100.0 million unsecured term loan facility (the "$100 Million Term Loan Facility"). The Revolver is scheduled to mature on February 12, 2021 and has two six-month extension options available for a maximum maturity date of February 14, 2022, subject to certain conditions and the payment of an additional fee. The $100 Million Term Loan Facility is scheduled to mature on February 14, 2022. Under the terms of the Credit Facility, we may request additional lender commitments up to an additional aggregate $550.0 million, which may be comprised of additional revolving commitments under the Revolver, an increase to the $100 Million Term Loan Facility, additional term loan tranches or any combination of the foregoing.

Interest on the Credit Facility is generally to be paid based upon, at our option, either (i) LIBOR plus an applicable margin that is based upon our leverage ratio or (ii) the Base Rate (which is defined as the highest of (a) the federal funds rate plus 0.50%, (b) the administrative agent’s prime rate or (c) the Eurodollar Rate plus 1.00%) plus an applicable margin that is based on our leverage ratio. The margins for the Revolver range in amount from 1.10% to 1.50% per annum for LIBOR-based loans and 0.10% to 0.50% per annum for Base Rate-based loans, depending on our leverage ratio. The margins for the $100 Million Term Loan Facility range in amount from 1.20% to 1.70% per annum for LIBOR-based loans and 0.20% to 0.70% per annum for Base Rate-based loans, depending on our leverage ratio.

If we attain one additional investment grade rating by one or more of Standard & Poor’s (“S&P”) or Moody’s Investor Services (“Moody’s”) to complement our current investment grade Fitch rating, we may elect to convert the pricing structure under the Credit Facility to be based on such rating. In that event, the margins for the Revolver will range in amount from 0.825% to 1.550% per annum for LIBOR-based loans and 0.00% to 0.55% per annum for Base Rate-based loans, depending on such rating, and the margins for the $100 Million Term Loan Facility will range in amount from 0.90% to 1.75% per annum for LIBOR-based loans and 0.00% to 0.75% per annum for Base Rate-based loans, depending on such ratings.

In addition to the interest payable on amounts outstanding under the Revolver, we are required to pay an applicable facility fee, based upon our leverage ratio, on the aggregate amount of each lender's Revolving Credit Commitment (whether or not such Revolving Credit Commitment is drawn), as defined in the Credit Facility. The applicable facility fee will range in amount from 0.15% to 0.30% per annum, depending on our leverage ratio. In the event that we convert the pricing structure to be based on an investment-grade rating, the applicable facility fee will range in amount from 0.125% to 0.30% per annum, depending on such rating.

The Credit Facility is guaranteed by the Company and by substantially all of the current and to-be-formed subsidiaries of the Operating Partnership that own an unencumbered property. The Credit Facility is not secured by the Company’s properties or by equity interests in the subsidiaries that hold such properties.

The Revolver and the $100 Million Term Loan Facility may be voluntarily prepaid in whole or in part at any time without premium or penalty. Amounts borrowed under the $100 Million Term Loan Facility and repaid or prepaid may not be reborrowed.
The Credit Facility contains usual and customary events of default including defaults in the payment of principal, interest or fees, defaults in compliance with the covenants set forth in the Credit Facility and other loan documentation, cross-defaults to certain other indebtedness, and bankruptcy and other insolvency defaults. If an event of default occurs and is

continuing under the Credit Facility, the unpaid principal amount of all outstanding loans, together with all accrued unpaid interest and other amounts owing in respect thereof, may be declared immediately due and payable.
As of the filing date of this Quarterly Report on Form 10-Q, we did not have any borrowings outstanding under the Revolver, leaving $350.0 million available for future borrowings.
$150 Million Term Loan Facility
On May 22, 2018, we entered into a credit agreement for a senior unsecured term loan facility (the “$150 Million Term Loan Facility”) that initially permits aggregate borrowings of up to $150.0 million, the total of which we borrowed the same day at closing. The net proceeds were used to partially pay down the outstanding balance of the Revolver and to fund acquisitions. Under the terms of the $150 Million Term Loan Facility, we may request additional incremental term loans in an aggregate amount not to exceed $100.0 million. Any increase in borrowings is subject to the satisfaction of specified conditions and the identification of lenders willing to make available such additional amounts. The maturity date of the $150 Million Term Loan Facility is May 22, 2025.
Interest on the $150 Million Term Loan Facility is generally to be paid based upon, at our option, either (i) LIBOR plus an applicable Eurodollar rate margin or (ii) the Base Rate (which is defined as the highest of (a) the federal funds rate plus 0.50%, (b) the administrative agent’s prime rate or (c) the Eurodollar Rate plus 1.00%), plus an applicable base rate margin. The applicable Eurodollar rate margin will range from 1.50% to 2.20% per annum and the applicable base rate margin will range from 0.50% to 1.20% per annum, depending on our leverage ratio.
If we obtain one additional investment grade rating from one or more of S&P or Moody's to complement our current investment grade Fitch rating, we may elect to convert the pricing structure under the $150 Million Term Loan Facility to be based on such rating. Under this pricing structure, the applicable Eurodollar rate margin will range from 1.40% to 2.35% per annum and the applicable base rate margin will range from 0.40% to 1.35% per annum.

We have the option to voluntarily prepay any amounts borrowed under the $150 Million Term Loan Facility in whole or in part at any time, subject to certain notice requirements. To the extent that we prepay all or any portion of a loan prior to May 22, 2020, we will pay a prepayment premium equal to (i) if such prepayment occurs prior to May 22, 2019, 2.00% of the principal amount so prepaid, and (ii) if such prepayment occurs on or after May 22, 2019, but prior to May 22, 2020, 1.00% of the principal amount so prepaid. Amounts borrowed under the $150 Million Term Loan Facility and repaid or prepaid may not be reborrowed.
Investment Grade Rating
In October 2018, Fitch Ratings upgraded our investment grade credit rating to BBB from BBB- with a stable outlook on the Revolver, the $100 Million Term Loan Facility, the $150 Million Term Loan Facility, our $225 million term loan facility, our $100 million unsecured guaranteed senior notes and our $125 million unsecured guaranteed senior notes. They also upgraded our investment grade credit rating to BB+ from BB on our 5.875% Series A Cumulative Redeemable Preferred Stock and assigned a BB+ rating on our 5.875% Series B Cumulative Redeemable Preferred Stock. Our credit ratings are based on our operating performance, liquidity and leverage ratios, overall financial position and other factors employed by the credit rating agencies in their rating analysis of us, and, although it is our intent to maintain our investment grade credit rating, there can be no assurance that we will be able to maintain our current credit ratings. In the event our current credit ratings are downgraded, it may become difficult or more expensive to obtain additional financing or refinance existing indebtedness as maturities become due.
Uses of Liquidity
Acquisitions
One of our most significant liquidity needs has historically been for the acquisition of real estate properties. Year to date, we have acquired 21 properties with a combined 2.3 million rentable square feet for a total gross purchase price of $371.3 million, and we are actively monitoring a volume of properties in our markets that we believe represent attractive potential investment opportunities to continue to grow our business. As of the filing date of this Quarterly Report on Form 10-Q, we have approximately $193.8 million of acquisitions under contract or letter of intent. While the actual number of acquisitions that we complete will be dependent upon a number of factors, in the short term, we expect to fund our acquisitions through available cash on hand, cash flows from operations, borrowings available under the Revolver, recycling capital through property dispositions and, in the long term, through the issuance of equity securities or proceeds from long-term secured and unsecured financings.

Recurring and Nonrecurring Capital Expenditures

Capital expenditures are considered part of both our short-term and long-term liquidity requirements. As discussed above under — Factors that May Influence Future Results —Acquisitions and Value-Add Repositioning of Properties, as of September 30, 2018, 12 of our properties were in various stages of current and future repositioning or lease-up. We currently estimate that approximately $46.2 million of capital will be required over the next seven quarters (4Q-2018 through 2Q-2020) to complete the redevelopment and repositioning of these properties. This estimate, however, is based on our current construction plans and budgets, both of which are subject to change as a result of a number of factors. If we are unable to complete construction on schedule or within budget, we could incur increased construction costs and experience potential delays in leasing the properties. We expect to fund these projects through a combination of cash flow from operations, the issuance of common stock under the $400 Million ATM Program and borrowings available under the Revolver.

The following table sets forth certain information regarding non-recurring and recurring capital expenditures at the properties in our portfolio as follows (dollars in thousands):

	Nine Months Ended September 30, 2018		
	Total	Square Feet[1]	Per Square Foot[2]
Non-Recurring Capital Expenditures[3]	$34,923	13,732,012	$ 2.54
Recurring Capital Expenditures[4]	3,218	19,512,895	$ 0.16
Total Capital Expenditures	$38,141		

(1) For non-recurring capital expenditures, reflects the aggregate square footage of the properties in which we incurred such capital expenditures. For recurring capital expenditures, reflects the weighted average square footage of our consolidated portfolio during the period.

(2) Per square foot amounts are calculated by dividing the aggregate capital expenditure costs by the square footage as defined in (1) above.

(3) Non-recurring capital expenditures are expenditures made in respect of a property for improvement to the appearance of such property or any other major upgrade or renovation of such property, and further includes capital expenditures for seismic upgrades, or capital expenditures for deferred maintenance existing at the time such property was acquired.

(4) Recurring capital expenditures are expenditures made in respect of a property for maintenance of such property and replacement of items due to ordinary wear and tear including, but not limited to, expenditures made for maintenance of parking lots, roofing materials, mechanical systems, HVAC systems and other structural systems.

Commitments and Contractual Obligations

The following table sets forth our principal obligations and commitments as of September 30, 2018, including (i) scheduled principal payments and debt maturities, (ii) periodic interest payments related to our outstanding indebtedness and interest rate swaps, (iii) office and ground lease payments and (iv) other contractual obligations (in thousands):

	Payments by Period						
	Total	Remainder of 2018	2019	2020	2021	2022	Thereafter
Principal payments and debt maturities	$761,154	$ 38	$158	$166	$566	$100,967	$659,259
Interest payments - fixed-rate debt[1]	75,188	1,261	9,333	9,325	9,316	9,307	36,646
Interest payments - variable-rate debt[2]	85,831	4,233	16,690	16,715	16,898	16,071	15,224
Office lease payments	1,307	223	660	257	167	—	—
Ground lease payments	6,288	36	144	144	144	144	5,676
Contractual obligations[3]	25,468	25,468	—	—	—	—	—
Total	$955,236	$ 31,259	$26,985	$26,607	$27,091	$126,489	$716,805

(1) Reflects scheduled interest payments on our fixed rate debt, including the $100 million unsecured guaranteed senior notes, the $125 million unsecured guaranteed senior notes and the Gilbert/La Palma mortgage loan.

(2) Reflects an estimate of interest payments due on variable rate debt, including the impact of interest rate swaps. For variable rate debt where interest is paid based on LIBOR plus an applicable LIBOR margin, we used the applicable LIBOR margin in effect as of September 30, 2018, and the one-month LIBOR rate of 2.26056%, as of September 30, 2018. Furthermore, it is assumed that any maturity extension options available are not exercised.

(3) Includes total commitments for tenant improvement and construction work related to obligations under certain tenant leases and vendor contracts. We anticipate these obligations to be paid as incurred through the remainder of 2018 and 2019, however, as the timing of these obligations is subject to a number of factors, for purposes of this table, we have included the full amount under "Remainder of 2018".

Dividends and Distributions

In order to maintain our qualification as a REIT, we are required to distribute annually at least 90% of our REIT taxable income, determined without regard to the dividends paid deduction and excluding any net capital gains. To satisfy the requirements to qualify as a REIT and generally not be subject to U.S. federal income tax, we intend to distribute a percentage of our cash flow on a quarterly basis to holders of our common stock. In addition, we intend to make distribution payments to holders of OP Units and dividend payments to holders of our preferred stock.

On October 29, 2018, our board of directors declared a quarterly cash dividend of $0.16 per share of common stock and a quarterly cash distribution of $0.16 per OP Unit, to be paid on January 15, 2019, to holders of record as of December 31, 2018. Also, on October 29, 2018, our board of directors declared a quarterly cash dividend of $0.367188 per share of our 5.875% Series A Cumulative Redeemable Preferred Stock and $0.367188 per share of our 5.875% Series B Cumulative Redeemable Preferred Stock, to be paid on December 31, 2018, to preferred stockholders of record as of December 14, 2018.

Consolidated Debt

The following table sets forth certain information with respect to our consolidated debt outstanding as of September 30, 2018:

	Maturity Date	Stated Interest Rate	Effective Interest Rate[1]	Principal Balance (in thousands)[2]	Maturity Date of Effective Swaps
Secured Debt:					
$60M Term Loan	8/1/2023[3]	LIBOR+1.70%	3.616 % [4]	$ 58,499	2/15/2019
Gilbert/La Palma	3/1/2031	5.125%	5.125 %	2,655	
Unsecured Debt:					
Revolver[5]	2/12/2021[6]	LIBOR +1.10%[7]	3.361 %	—	
$100M Term Loan Facility	2/14/2022	LIBOR +1.20%[7]	3.098 % [8]	100,000	12/14/2018; 8/14/2021[8]
$225M Term Loan Facility	1/14/2023	LIBOR +1.20%[7]	2.574 % [9]	225,000	1/14/2022
$150M Term Loan Facility	5/22/2025	LIBOR +1.50%[7]	3.761 %	150,000	
$100M Senior Notes	8/6/2025	4.290%	4.290 %	100,000	
$125M Senior Notes	7/13/2027	3.930%	3.930 %	125,000	
Total Consolidated			3.414 %	$ 761,154	

(1) Includes the effect of interest rate swaps that were effective as of September 30, 2018. Assumes a 1-month LIBOR rate of 2.26056% as of September 30, 2018, as applicable. Excludes the effect of amortization of debt issuance costs, discounts and the facility fee on the Revolver.

(2) Excludes unamortized debt issuance costs and discounts aggregating $3.9 million as of September 30, 2018.

(3) One 24-month extension is available if certain conditions are satisfied.

(4) As of September 30, 2018, $58.3 million of this term loan has been effectively fixed at 3.615% through the use of two interest rate swaps as follows: (i) $30 million at 3.526% with an effective date of January 15, 2015 and (ii) $28.3 million at 3.71% with an effective date of July 15, 2015.

(5) The Revolver is subject to an applicable facility fee which is calculated as a percentage of the total lenders' commitment amount, regardless of usage. The applicable facility fee will range from 0.15% to 0.30% depending upon our leverage ratio.

(6) Two additional six-month extensions available at the borrower's option.

(7) The LIBOR margin will range from 1.10% to 1.50% per annum for the Revolver, 1.20% to 1.70% per annum for the $100 Million Term Loan Facility, 1.20% to 1.70% per annum for the $225 million term loan facility and 1.50% to 2.20% per annum for the $150 Million Term Loan Facility, depending on our leverage ratio, which is the ratio of our outstanding consolidated indebtedness to the value of our consolidated gross asset value. This leverage ratio is measured on a quarterly basis, and as a result, the effective interest rate will fluctuate from period to period.

(8) As of September 30, 2018, the $100 Million Term Loan Facility has been effectively fixed at 1.8975% plus the applicable LIBOR margin through the use of two interest rate swaps as follows: (i) $50 million with a strike rate of 1.79% and an effective date of August 14, 2015, and (ii) $50 million with a strike rate of 2.005% and an effective date of February 16, 2016, plus the applicable LIBOR margin. We have an interest rate swap that will effectively fix the $100 Million Term Loan Facility at 1.764% plus an applicable LIBOR margin from December 14, 2018 (the expiration date of the current swaps) through August 14, 2021.

(9) As of September 30, 2018, the $225 million term loan facility has been effectively fixed at 1.374% plus the applicable LIBOR margin through the use of two interest rate swaps as follows: (i) $125 million with a strike rate of 1.349% and an effective date of February 14, 2018, and (ii) $100 million with a strike rate of 1.406% and an effective date of August 14, 2018, plus the applicable LIBOR margin.

The following table summarizes the composition of our consolidated debt between fixed-rate and variable-rate and secured and unsecured debt as of September 30, 2018:

	Average Term Remaining (in years)	Stated Interest Rate	Effective Interest Rate(1)	Principal Balance (in thousands)(2)	% of Total
Fixed vs. Variable:					
Fixed	5.6	3.33%	3.33%	$ 610,959	80%
Variable	6.6	LIBOR + 1.50%	3.76%	$ 150,195	20%
Secured vs. Unsecured:					
Secured	5.2		3.68%	$ 61,154	8%
Unsecured	5.8		3.39%	$ 700,000	92%

(1) Includes the effect of interest rate swaps that were effective as of September 30, 2018. Excludes the effect of amortization of debt issuance costs, discounts/premiums and the facility fee on the Revolver. Assumes a 1-month LIBOR rate of 2.26056% as of September 30, 2018, as applicable.
(2) Excludes unamortized debt issuance costs and discounts aggregating $3.9 million as of September 30, 2018.

At September 30, 2018, we had total consolidated indebtedness of $761.2 million, excluding unamortized debt issuance costs and discounts, with a weighted average interest rate of 3.414% and an average term-to-maturity of 5.8 years. As of September 30, 2018, $611.0 million, or 80% of our outstanding indebtedness had an interest rate that was effectively fixed under either the terms of the loan ($227.7 million) or an interest rate swap ($383.3 million).

At September 30, 2018, we had consolidated indebtedness of $761.2 million, reflecting a net debt to total combined market capitalization of approximately 15.3%. Our total market capitalization is defined as the sum of the market value of our outstanding preferred stock plus the market value of our common stock excluding shares of nonvested restricted stock, plus the aggregate value of common units not owned by us, plus the value of our net debt. Our net debt is defined as our consolidated indebtedness less cash and cash equivalents.

Fourth Amendment to Credit Agreement

On January 16, 2018, we entered into the Fourth Amendment to Credit Agreement (the “Fourth Amendment”) to amend our Credit Agreement, dated as of January 14, 2016 (as amended from time to time) for our $225.0 million unsecured term loan facility (the “$225 Million Term Loan Facility”).

Amounts outstanding under the $225 Million Term Loan Facility bear interest at a rate equal to, at our option, either (i) LIBOR plus an applicable margin that is based upon our leverage ratio or (ii) the Base Rate, as defined in the $225 Million Term Loan Facility, plus an applicable margin that is based on our leverage ratio. The Fourth Amendment decreases the applicable margin for LIBOR-based borrowings from a range of 1.50% to 2.25% per annum to a range of 1.20% to 1.70% per annum and decreases the applicable margin for Base Rate-based borrowings from a range of 0.50% to 1.25% per annum to a range of 0.20% to 0.70% per annum.

If we obtain one additional investment grade rating by one or more of S&P or Moody’s to complement our current investment grade Fitch rating, we may elect to convert the pricing structure under the $225 Million Term Loan Facility to be based on such rating. Under this pricing structure, the Fourth Amendment decreases the applicable margin for LIBOR-based borrowings from a range of 1.40% to 2.35% per annum to a range of 0.90% to 1.75% per annum and decreases the applicable margin for Base Rate-based borrowings from a range of 0.40% to 1.35% per annum to a range of 0.00% to 0.75% per annum.

Modification of $60 Million Term Loan

On June 27, 2018, we entered into the Second Modification Agreement (the “Modification Agreement”) to amend our Term Loan Agreement, dated as of July 24, 2013 (as amended from time to time) for our $60.0 million term loan (the “$60 Million Term Loan”)

The Modification Agreement, among other things, (i) extends the maturity date of the $60 Million Term Loan from August 1, 2019, to August 1, 2023, (ii) decreases the interest rate from LIBOR plus 1.90% per annum to LIBOR plus 1.70% per annum, (iii) provides for one 24-month extension option, subject to certain terms and conditions, and (iv)

amends the repayment schedule of the $60 Million Term Loan by adding 36 months of interest only payments, followed by equal monthly payments of principal ($65,250), plus accrued interest until maturity.

63

Debt Covenants

The Credit Facility, the $225 Million Term Loan Facility, the $150 Million Term Loan Facility, the $100 million unsecured guaranteed senior notes (the "$100 Million Notes"), and the $125 million unsecured guaranteed senior notes (the "$125 Million Notes") all include a series of financial and other covenants that we must comply with, including the following covenants which are tested on a quarterly basis:

- Maintaining a ratio of total indebtedness to total asset value of not more than 60%;
- For the Credit Facility, the $225 Million Term Loan Facility and the $150 Million Term Loan Facility, maintaining a ratio of secured debt to total asset value of not more than 45%;
- For the $100 Million Notes and the $125 Million Notes, maintaining a ratio of secured debt to total asset value of not more than 40%;
- Maintaining a ratio of total secured recourse debt to total asset value of not more than 15%;
- Maintaining a minimum tangible net worth of at least the sum of (i) $760,740,750, and (ii) an amount equal to at least 75% of the net equity proceeds received by the Company after September 30, 2016;
- Maintaining a ratio of adjusted EBITDA (as defined in each of the loan agreements) to fixed charges of at least 1.50 to 1.0;
- Maintaining a ratio of total unsecured debt to total unencumbered asset value of not more than 60%;
- Maintaining a ratio of unencumbered NOI (as defined in each of the loan agreements) to unsecured interest expense of at least 1.75 to 1.0.

The Credit Facility, the $225 Million Term Loan Facility, the $150 Million Term Loan Facility, the $100 Million Notes and the $125 Million Notes also contain limitations on our ability to pay distributions on our common stock. Specifically, our cash dividends may not exceed the greater of (1) 95% of our FFO (as defined in the credit agreement) and (2) the amount required for us to qualify and maintain our REIT status. If an event of default exists, we may only make distributions sufficient to qualify and maintain our REIT status.

Additionally, subject to the terms of the $100 Million Notes and the $125 Million Notes (together the "Notes"), upon certain events of default, including, but not limited to, (i) a default in the payment of any principal, make-whole payment amount, or interest under the Notes, (ii) a default in the payment of certain of our other indebtedness, (iii) a default in compliance with the covenants set forth in the Notes agreement and (iv) bankruptcy and other insolvency defaults, the principal and accrued and unpaid interest and the make-whole payment amount on the outstanding Notes will become due and payable at the option of the purchasers.

The $60 Million Term Loan contains the following financial covenants:

- Maintaining a Debt Service Coverage Ratio (as defined in the term loan agreement) of at least 1.10 to 1.00, to be tested quarterly;
- Maintaining Unencumbered Liquid Assets (as defined in the term loan agreement) of not less than (i) $5 million, or (ii) $8 million if we elect to have Line of Credit Availability (as defined in the term loan agreement) included in the calculation, of which $2 million must be cash or cash equivalents, to be tested annually as of December 31 of each year;
- Maintaining a minimum Fair Market Net Worth (as defined in the term loan agreement) of at least $75 million, to be tested annually as of December 31 of each year.

We were in compliance with all of our quarterly debt covenants as of September 30, 2018.

Off Balance Sheet Arrangements

As of September 30, 2018, we did not have any off-balance sheet arrangements.

Cash Flows
Comparison of the Nine Months Ended September 30, 2018 to the Nine Months Ended September 30, 2017
The following table summarizes the changes in net cash flows associated with our operating, investing, and financing activities for the nine months ended September 30, 2018 and 2017 (in thousands):

	Nine Months Ended September 30,		
	2018	2017	Change
Cash provided by operating activities	$80,945	$58,129	$22,816
Cash used in investing activities	$(368,493)	$(491,948)	$123,455
Cash provided by financing activities	$464,582	$431,212	$33,370

Net cash provided by operating activities. Net cash provided by operating activities increased by $22.8 million to $80.9 million for the nine months ended September 30, 2018, compared to $58.1 million for the nine months ended September 30, 2017. The increase was primarily attributable to incremental cash flows from property acquisitions completed subsequent to January 1, 2017, and the increase in Cash NOI from our Same Properties Portfolio, partially offset by higher cash paid for interest for comparable periods and changes in working capital.
Net cash used in investing activities. Net cash used in investing activities decreased by $123.5 million to $368.5 million for the nine months ended September 30, 2018, compared to $491.9 million for the nine months ended September 30, 2017. The decrease was primarily attributable to a $170.8 million decrease in cash paid for property acquisitions, including related deposits, partially offset by a $29.2 million decrease in net cash proceeds from the sale of properties, a $12.1 million increase in cash paid for construction and repositioning projects for comparable periods, and a $6.0 million decrease in proceeds from repayment of a note receivable in the prior period.
Net cash provided by financing activities. Net cash provided by financing activities increased by $33.4 million to $464.6 million for the nine months ended September 30, 2018, compared to $431.2 million for the nine months ended September 30, 2017. The increase was primarily attributable to the following: (i) an increase of $150.0 million in borrowings on the $150 Million Term Loan Facility, (ii) an increase of $121.4 million in net cash proceeds from the sale of shares of our common stock for comparable periods and (iii) the $9.9 million repayment of one of our secured mortgage loans in March 2017, inclusive of a $0.2 million early prepayment premium. These increases were partially offset by the following: (i) a decrease of $125.0 million of cash proceeds from the issuance of the $125 Million Notes in July 2017, (ii) a decrease of $76.0 million in draws on the Revolver for comparable periods, (iii) an increase of $34.0 million in paydowns on the Revolver for comparable periods, (iv) an increase of $10.0 million in dividends and distributions paid to common stockholders and unit holders resulting from the increase in the number of common shares outstanding and the increase in our quarterly per share cash dividend and (v) an increase of $3.9 million in dividends paid to preferred stockholders due to the issuance of our 5.87% Series B Cumulative Redeemable Preferred Stock in November 2017.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Market risk refers to the risk of loss from adverse changes in market prices and interest rates. A key market risk we face is interest rate risk. We are exposed to interest rate changes primarily as a result of using variable-rate debt to satisfy various short-term and long-term liquidity needs, which have interest rates based upon LIBOR. We use interest rate swaps to manage, or hedge, interest rate risks related to our borrowings. Because actual interest rate movements over time are uncertain, our swaps pose potential interest rate risks, notably if interest rates fall. We also expose ourselves to credit risk, which we attempt to minimize by contracting with highly-rated banking financial counterparties. For a summary of our outstanding variable-rate debt, see Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources. For a summary of our interest rate swaps, see Note 7 to our consolidated financial statements.

As of September 30, 2018, $58.3 million of the $60 Million Term Loan's principal has been effectively fixed at 3.615% through the use of two interest rate swaps, with notional values of $30.0 million and $28.3 million, respectively. The first interest rate swap, which is effective for the period from January 15, 2015 to February 15, 2019, currently fixes the annual interest rate payable at 3.526%. The second interest rate swap, which is an amortizing swap, is effective for the period from July 15, 2015 to February 15, 2019, and currently fixes the annual interest rate payable at 3.71%.

As of September 30, 2018, interest on the $100 Million Term Loan Facility has been effectively fixed through the use of two interest rate swaps, each with a notional value of $50.0 million. The first interest rate swap has an effective date of August 14, 2015, and a maturity date of December 14, 2018, and the second interest rate swap has an effective date of February 16, 2016, and a maturity date of December 14, 2018. The two interest rate swaps currently fix the annual interest rate payable on the $100 Million Term Loan Facility as follows: 1.79% for the first $50.0 million and 2.005% for the second $50.0 million, plus an applicable margin under the terms of the Credit Facility.

On August 11, 2017, we entered into an interest rate swap transaction to manage our exposure to fluctuations in the variable interest rate associated with $100 Million Term Loan Facility. The interest rate swap, which has a notional value of $100.0 million, has an effective date of December 14, 2018, which coincides with the termination date of the two in-place interest rate swaps noted above, and a maturity date of August 14, 2021. Upon termination of the two in-place swaps, the new swap will effectively fix the annual interest rate payable on the $100 Million Term Loan Facility at 1.764% plus an applicable margin under the terms of the Credit Facility.

As of September 30, 2018, interest on the $225 Million Term Loan Facility has been effectively fixed through the use of two interest rate swaps. The first interest rate swap has a notional value of $125.0 million, an effective date of February 14, 2018, a maturity date of January 14, 2022, and currently fixes the annual interest rate payable at 1.349% plus an applicable LIBOR margin under the terms of the $225 Million Term Loan Facility. The second interest rate swap has a notional value of $100.0 million, an effective date of August 14, 2018, a maturity date of January 14, 2022, and currently fixes the annual interest rate payable at 1.406% plus an applicable LIBOR margin under the terms of the $225 Million Term Loan Facility.

At September 30, 2018, we had total consolidated indebtedness, excluding unamortized debt issuance costs and discounts/premiums, of $761.2 million. Of this total amount, $611.0 million, or 80%, had an interest rate that was effectively fixed under the terms of the loan or an interest rate swap. The remaining $150.2 million, or 20%, comprises our variable-rate debt. Based upon the amount of variable-rate debt outstanding as of September 30, 2018, if LIBOR were to increase by 50 basis points, the increase in interest expense on our variable-rate debt would decrease our future earnings and cash flows by approximately $0.8 million annually. If LIBOR were to decrease by 50 basis points, the decrease in interest expense on our variable-rate debt would increase our future earnings and cash flows by approximately $0.8 million annually.

Interest risk amounts are our management's estimates and were determined by considering the effect of hypothetical interest rates on our financial instruments. We calculate interest sensitivity by multiplying the amount of variable rate debt outstanding by the respective change in rate. The sensitivity analysis does not take into consideration possible changes in the balances or fair value of our floating rate debt or the effect of any change in overall economic activity that could occur in that environment. Further, in the event of a change of that magnitude, we may take actions to further mitigate our exposure to the change. However, due to the uncertainty of the specific actions that would be

taken and their possible effects, this analysis assumes no changes in our financial structure.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as defined in Rule 13a-15(e) or Rule 15d-15(e) under the Securities Exchange Act of 1934, as amended, (the "Exchange Act")) that are designed to ensure that information required to be disclosed in our reports under the Exchange Act is processed, recorded, summarized, and reported within the time periods specified in the Security and Exchange Commission's rules and forms and that such information is accumulated and communicated to management, including the Co-Chief Executive Officers and Chief Financial Officer, as appropriate, 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 SEC Rule 13a-15(b), we carried out an evaluation, under the supervision and with the participation of management, including our Co-Chief Executive Officers and Chief Financial Officer, regarding the effectiveness of our disclosure controls and procedures as of September 30, 2018, the end of the period covered by this report.

Based on the foregoing, our Co-Chief Executive Officers and Chief Financial Officer concluded that, as of September 30, 2018, our disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Control Over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting. No changes to our internal control over financial reporting were identified that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Part II. OTHER INFORMATION

Item 1. Legal Proceedings

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

Our subsidiary Rexford Industrial - 1065 Walnut, LLC, may be subject to a potential insurance subrogation related lawsuit arising from the alleged loss of inventory when a broken beam in the ceiling of one of our properties allegedly caused fire sprinkler and water damage. The matter is currently in the investigation stage, and no lawsuit has been filed. The amount sought through insurance subrogation is approximately $3.7 million. Our commercial liability insurer has confirmed that our liability insurance policy limit is sufficient to pay the potential claim and has confirmed that it has no reservation of rights for this claim. Based on the foregoing, we do not believe that this potential claim would reasonably be expected to have a material adverse effect on our business, financial condition or results of operations. While we intend to vigorously defend any claims asserted against us should a lawsuit be filed, we cannot predict their outcome.

Item 1A. Risk Factors

Please refer to our Risk Factors as set forth in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2017. There have been no material changes to the risk factors as set forth in these documents.

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

(a) Unregistered Sales of Equity Securities
None.
(b) Use of Proceeds
None.
(c) Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number (or approximate dollar value) of Shares that May Yet Be Purchased Under the Plans or Programs
July 1, 2018 to July 31, 2018[1]	608	$ 31.04	N/A	N/A
August 1, 2018 to August 31, 2018[1]	357	$ 31.44	N/A	N/A
September 1, 2018 to September 30, 2018	—	$ —	N/A	N/A
	965	$ 31.19	N/A	N/A

(1) In July and August 2018, these shares were tendered by certain of our employees to satisfy minimum statutory tax withholding obligations related to the vesting of restricted shares.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

None.

Item 5. Other Information

None.

Item 6. Exhibits

Exhibit	
3.1	Articles of Amendment and Restatement of Rexford Industrial Realty, Inc. (incorporated by reference to Exhibit 3.1 of Form S-11/A, filed by the registrant on July 15, 2013 (Registration No. 333-188806))
3.2	Rexford Industrial Realty, Inc. Third Amended and Restated Bylaws of Rexford Industrial Realty, Inc. (incorporated by reference to Exhibit 3.1 of Form 8-K, filed by the registrant on May 4, 2018)
3.3	Articles Supplementary designating the Series A Preferred Stock of Rexford Industrial Realty, Inc. (incorporated by reference to Exhibit 3.3 of Form 8-A, filed by the registrant on August 15, 2016)
3.4	Third Amended and Restated Agreement of Limited Partnership of Rexford Industrial Realty, L.P. (incorporated by reference to Exhibit 3.2 of Form 8-K, filed by the registrant on August 16, 2016)
3.5	Articles Supplementary designating the Series B Preferred Stock of Rexford Industrial Realty, Inc. (incorporated by reference to Exhibit 3.3 of Form 8-A12B, filed by the registrant on November 9, 2017)
4.1	Form of Certificate of Common Stock of Rexford Industrial Realty, Inc. (incorporated by reference to Exhibit 4.1 of Form S-11/A, filed by the registrant on July 15, 2013 (Registration No. 333-188806))
4.2	Form of Specimen Certificate of Series A Preferred Stock of Rexford Industrial Realty, Inc. (incorporated by reference to Exhibit 4.1 of Form 8-A, filed by the registrant on August 15, 2016)
4.3	Form of Specimen Certificate of Series B Preferred Stock of Rexford Industrial Realty, Inc. (incorporated by reference to Exhibit 4.1 of Form 8-A12B, filed by the registrant on November 9, 2017)
31.1*	Certification of the Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2*	Certification of the Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.3*	Certification of the Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1*	Certification of Principal Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2*	Certification of Principal Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.3*	Certification of Principal Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.1*	The registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2018, formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Balance Sheets (unaudited), (ii) Consolidated Statements of Operations (unaudited), (iii) Consolidated Statements of Comprehensive Income, (iv) Consolidated Statements of Changes in Equity (unaudited), (v) Consolidated Statements of Cash Flows (unaudited) and (vi) the Notes to the Consolidated Financial Statements (unaudited) that have been detail tagged.

*Filed herein

70

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 authorized.

	Rexford Industrial Realty, Inc.
October 31, 2018	/s/ Michael S. Frankel Michael S. Frankel Co-Chief Executive Officer (Principal Executive Officer)
October 31, 2018	/s/ Howard Schwimmer Howard Schwimmer Co-Chief Executive Officer (Principal Executive Officer)
October 31, 2018	/s/ Adeel Khan Adeel Khan Chief Financial Officer (Principal Financial and Accounting Officer)

71