

QTS Realty Trust, Inc.
Form 10-Q
November 09, 2016
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FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

(Mark One)

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

For the quarterly period ended September 30, 2016

OR

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

For the transition period from _____ to _____

Commission File Number 001-36109

QTS Realty Trust, Inc.

QualityTech, LP

(Exact name of registrant as specified in its charter)

Maryland (QTS Realty Trust, Inc.)	46-2809094
Delaware (QualityTech, LP)	27-0707288
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
12851 Foster Street, Overland Park, Kansas	66213
(Address of principal executive offices)	(Zip Code)

(Registrant's telephone number, including area code) (913) 312-5503

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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

QTS Realty Trust, Inc. Yes No QualityTech, LP Yes No

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

QTS Realty Trust, Inc. Yes No QualityTech, LP Yes 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 definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

QTS Realty Trust, Inc.

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

QualityTech, LP

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

QTS Realty Trust, Inc. Yes No QualityTech, LP Yes No

There were 47,705,495 shares of Class A common stock, \$0.01 par value per share, and 133,000 shares of Class B common stock, \$0.01 par value per share, of QTS Realty Trust, Inc. outstanding on November 4, 2016.

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EXPLANATORY NOTE

This report combines the quarterly reports on Form 10-Q of QTS Realty Trust, Inc. (“QTS”) and QualityTech, LP, a Delaware limited partnership, which is our operating partnership (the “Operating Partnership”). This report also includes the financial statements of QTS and those of the Operating Partnership, although it presents only one set of combined notes for QTS’ financial statements and those of the Operating Partnership.

Substantially all of QTS’ assets are held by, and its operations are conducted through, the Operating Partnership. QTS is the sole general partner of the Operating Partnership, and, as of September 30, 2016, its only material asset consisted of its ownership of approximately 87.6% of the Operating Partnership. Management operates QTS and the Operating Partnership as one business. The management of QTS consists of the same employees as the management of the Operating Partnership. QTS does not conduct business itself, other than acting as the sole general partner of the Operating Partnership and issuing public equity from time to time. QTS has not issued or guaranteed any indebtedness. Except for net proceeds from public equity issuances by QTS, which are contributed to the Operating Partnership in exchange for units of limited partnership interest of the Operating Partnership, the Operating Partnership generates all remaining capital required by our business through its operations, the direct or indirect incurrence of indebtedness, and the issuance of partnership units. Therefore, as general partner with control of the Operating Partnership, QTS consolidates the Operating Partnership for financial reporting purposes.

We believe, therefore, that a combined presentation with respect to QTS and the Operating Partnership, including providing one set of notes for the financial statements of QTS and the Operating Partnership, provides the following benefits:

- enhances investors’ understanding of QTS and the Operating Partnership by enabling investors to view the business as a whole in the same manner as management views and operates the business;
- eliminates duplicative disclosure and provides a more streamlined and readable presentation since a substantial portion of the disclosure in this report applies to both QTS and the Operating Partnership; and
- creates time and cost efficiencies through the preparation of one presentation instead of two separate presentations.

In addition, in light of these combined disclosures, we believe it is important for investors to understand the few differences between QTS and the Operating Partnership in the context of how QTS and the Operating Partnership operate as a consolidated company. With respect to balance sheets, the presentation of stockholders’ equity and partners’ capital are the main areas of difference between the consolidated balance sheets of QTS and those of the Operating Partnership. On the Operating Partnership’s consolidated balance sheets, partners’ capital includes partnership units that are owned by QTS and other partners. On QTS’ consolidated balance sheets, stockholders’ equity includes common stock, additional paid-in capital, accumulated other comprehensive income (loss) and accumulated

dividends in excess of earnings. The remaining equity reflected on QTS's consolidated balance sheet is the portion of net assets that are retained by partners other than QTS, referred to as noncontrolling interests. With respect to statements of operations, the primary difference in QTS' Statements of Operations and Comprehensive Income is that for net income (loss), QTS retains its proportionate share of the net income (loss) based on its ownership of the Operating Partnership, with the remaining balance being retained by the Operating Partnership.

In order to highlight the few differences between QTS and the Operating Partnership, there are sections and disclosure in this report that discuss QTS and the Operating Partnership separately, including separate financial statements, separate controls and procedures sections, separate Exhibit 31 and 32 certifications, and separate presentation of certain accompanying notes to the financial statements, including Note 7 – Partners' Capital, Equity and Incentive Compensation Plans. In the sections that combine disclosure for QTS and the Operating Partnership, this report refers to actions or holdings as being actions or holdings of "we," "our," "us," "our company" and "the Company." Although the Operating Partnership is generally the entity that enters into contracts, holds assets and issues debt, we believe that these general references to "we," "our," "us," "our company" and "the Company" in this context are appropriate because the business is one enterprise operated through the Operating Partnership.

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QTS Realty Trust, Inc.

QualityTech, LP

Form 10-Q

For the Quarterly Period Ended September 30, 2016

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PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements

QTS REALTY TRUST, INC.

INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

BALANCE SHEETS

(in thousands except share data)

	September 30, 2016 (unaudited)	December 31, 2015
ASSETS		
Real Estate Assets		
Land	\$ 73,968	\$ 57,112
Buildings, improvements and equipment	1,449,376	1,180,386
Less: Accumulated depreciation	(295,879)	(239,936)
	1,227,465	997,562
Construction in progress	320,650	345,655
Real Estate Assets, net	1,548,115	1,343,217
Cash and cash equivalents	11,769	8,804
Rents and other receivables, net	34,192	28,233
Acquired intangibles, net	135,306	115,702
Deferred costs, net	35,714	30,042
Prepaid expenses	9,835	6,502
Goodwill	173,843	181,738
Other assets, net	37,813	33,101
TOTAL ASSETS	\$ 1,986,587	\$ 1,747,339
LIABILITIES		
Unsecured credit facility, net	\$ 529,395	\$ 520,956
Senior notes, net of discount and debt issuance costs	291,842	290,852
Capital lease and lease financing obligations	41,825	49,761
Accounts payable and accrued liabilities	84,053	95,924
Dividends and distributions payable	19,653	15,378
Advance rents, security deposits and other liabilities	20,655	18,798
Deferred income taxes	16,018	18,813
Deferred income	18,403	16,991
TOTAL LIABILITIES	1,021,844	1,027,473

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EQUITY

Common stock, \$0.01 par value, 450,133,000 shares authorized, 47,857,646 and 41,225,784 shares issued and outstanding as of September 30, 2016 and December 31, 2015, respectively	479	412
Additional paid-in capital	930,128	670,275
Accumulated dividends in excess of earnings	(85,378)	(52,732)
Total stockholders' equity	845,229	617,955
Noncontrolling interests	119,514	101,911
TOTAL EQUITY	964,743	719,866
TOTAL LIABILITIES AND EQUITY	\$ 1,986,587	\$ 1,747,339

See accompanying notes to financial statements.

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QTS REALTY TRUST, INC.

INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (UNAUDITED)

(in thousands except share and per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Revenues:				
Rental	\$ 77,005	\$ 62,744	\$ 217,101	\$ 164,270
Recoveries from customers	8,703	6,158	20,306	17,404
Cloud and managed services	16,243	18,573	52,148	32,588
Other	1,514	1,415	7,365	4,131
Total revenues	103,465	88,890	296,920	218,393
Operating Expenses:				
Property operating costs	36,288	30,925	100,715	72,292
Real estate taxes and insurance	2,566	1,462	6,326	4,421
Depreciation and amortization	32,699	24,486	91,693	58,791
General and administrative	19,942	19,440	61,836	47,893
Transaction and integration costs	3,465	1,482	9,385	6,256
Total operating expenses	94,960	77,795	269,955	189,653
Operating income	8,505	11,095	26,965	28,740
Other income and expenses:				
Interest income	1	1	3	2
Interest expense	(6,179)	(5,418)	(17,034)	(15,559)
Other expense, net	1	—	1	(83)
Income before taxes	2,328	5,678	9,935	13,100
Tax benefit of taxable REIT subsidiaries	4,210	2,560	9,269	5,695
Net income	6,538	8,238	19,204	18,795
Net income attributable to noncontrolling interests	(808)	(1,229)	(2,485)	(3,072)
Net income attributable to QTS Realty Trust, Inc.	\$ 5,730	\$ 7,009	\$ 16,719	\$ 15,723
Net income per share attributable to common shares:				
Basic	\$ 0.12	\$ 0.17	\$ 0.37	\$ 0.43
Diluted	0.12	0.17	0.36	0.43
Weighted average common shares outstanding:				
Basic	47,854,516	40,994,387	45,651,421	36,354,738
Diluted	55,687,665	48,733,417	53,420,326	44,181,583

See accompanying notes to financial statements.

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QTS REALTY TRUST, INC.

INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENT OF EQUITY

(unaudited and in thousands)

	Common stock Shares	Common stock Amount	Additional paid-in capital	Accumulated dividends in excess of earnings	Total stockholders' equity	Noncontrolling interests	Total
Balance January 1, 2016	41,226	\$ 412	\$ 670,275	\$ (52,732)	\$ 617,955	\$ 101,911	\$ 719,866
Net share activity through equity award plan	307	3	(3)	—	—	(1,251)	(1,251)
Equity-based compensation expense	—	—	6,866	—	6,866	1,021	7,887
Net proceeds from equity offering	6,325	64	252,990	—	253,054	22,781	275,835
Dividends to shareholders	—	—	—	(49,365)	(49,365)	—	(49,365)
Distributions to noncontrolling interests	—	—	—	—	—	(7,433)	(7,433)
Net income	—	—	—	16,719	16,719	2,485	19,204
Balance September 30, 2016	47,858	\$ 479	\$ 930,128	\$ (85,378)	\$ 845,229	\$ 119,514	\$ 964,743

See accompanying notes to financial statements.

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QTS REALTY TRUST, INC.

INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

STATEMENTS OF CASH FLOW

(unaudited and in thousands)

For the nine months ended September 30, 2016 and 2015

	2016	2015
Cash flow from operating activities:		
Net income	\$ 19,204	\$ 18,795
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	89,104	57,347
Amortization of deferred loan costs	2,424	2,372
Amortization of senior notes discount	194	184
Equity-based compensation expense	7,887	5,206
Bad debt expense	1,201	640
Write off of deferred loan costs	—	83
Deferred tax benefit	(9,298)	(5,695)
Changes in operating assets and liabilities		
Rents and other receivables, net	(9,191)	(2,382)
Prepaid expenses	(2,854)	(4,713)
Other assets	(967)	(352)
Accounts payable and accrued liabilities	3,359	(2,427)
Advance rents, security deposits and other liabilities	984	(437)
Deferred income	1,448	3,698
Net cash provided by operating activities	103,495	72,319
Cash flow from investing activities:		
Acquisitions, net of cash acquired	(122,981)	(288,865)
Additions to property and equipment	(197,751)	(252,156)
Net cash used in investing activities	(320,732)	(541,021)
Cash flow from financing activities:		
Credit facility proceeds	267,000	420,162
Debt repayment	(259,002)	(260,000)
Payment of deferred financing costs	(35)	(577)
Payment of cash dividends	(45,371)	(32,756)
Distribution to noncontrolling interests	(7,189)	(6,652)
Payments to net settle equity awards	(1,252)	—
Principal payments on capital lease obligations	(9,612)	(4,415)
Mortgage principal debt repayments	—	(16,600)
Equity proceeds, net of costs	275,663	369,482
Net cash provided by financing activities	220,202	468,644
Net increase (decrease) in cash and cash equivalents	2,965	(58)

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Cash and cash equivalents, beginning of period	8,804	10,788
Cash and cash equivalents, end of period	\$ 11,769	\$ 10,730

See accompanying notes to financial statements.

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QTS REALTY TRUST, INC.

INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

STATEMENTS OF CASH FLOW (continued)

(unaudited and in thousands)

For the nine months ended September 30, 2016 and 2015

	2016	2015
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash paid for interest (excluding deferred financing costs and amounts capitalized)	\$ 18,659	\$ 17,785
Noncash investing and financing activities:		
Accrued capital additions	\$ 40,344	\$ 48,540
Capital lease and lease financing obligations assumed	\$ —	\$ 43,832
Acquisitions, net of cash acquired:		
Land	\$ 7,440	\$ 1,130
Buildings, improvements and equipment	80,390	78,898
Construction in Progress	13,900	12,127
Rents and other receivables, net	(2,033)	13,704
Acquired intangibles	34,281	93,400
Deferred costs	4,391	—
Prepaid expenses	479	1,653
Goodwill	(7,895)	174,697
Other assets	303	633
Capital lease and lease financing obligations	—	(43,832)
Accounts payable and accrued liabilities	(922)	(8,586)
Advance rents, security deposits and other liabilities	(1,343)	(2,468)
Deferred income	35	(10,818)
Deferred income taxes	(6,045)	(21,673)
Total acquisitions, net of cash acquired	\$ 122,981	\$ 288,865

See accompanying notes to financial statements.

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QUALITYTECH, LP

INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

BALANCE SHEETS

(in thousands)

	September 30, 2016 (unaudited)	December 31, 2015
ASSETS		
Real Estate Assets		
Land	\$ 73,968	\$ 57,112
Buildings, improvements and equipment	1,449,376	1,180,386
Less: Accumulated depreciation	(295,879)	(239,936)
	1,227,465	997,562
Construction in progress	320,650	345,655
Real Estate Assets, net	1,548,115	1,343,217
Cash and cash equivalents	11,769	8,804
Rents and other receivables, net	34,192	28,233
Acquired intangibles, net	135,306	115,702
Deferred costs, net	35,714	30,042
Prepaid expenses	9,835	6,502
Goodwill	173,843	181,738
Other assets, net	37,813	33,101
TOTAL ASSETS	\$ 1,986,587	\$ 1,747,339
LIABILITIES		
Unsecured credit facility, net	\$ 529,395	\$ 520,956
Senior notes, net of discount and debt issuance costs	291,842	290,852
Capital lease and lease financing obligations	41,825	49,761
Accounts payable and accrued liabilities	84,053	95,924
Dividends and distributions payable	19,653	15,378
Advance rents, security deposits and other liabilities	20,655	18,798
Deferred income taxes	16,018	18,813
Deferred income	18,403	16,991
TOTAL LIABILITIES	1,021,844	1,027,473
PARTNERS' CAPITAL		
Partners' capital	964,743	719,866
TOTAL LIABILITIES AND PARTNERS' CAPITAL	\$ 1,986,587	\$ 1,747,339

See accompanying notes to financial statements.

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QUALITYTECH, LP

INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (UNAUDITED)

(in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Revenues:				
Rental	\$ 77,005	\$ 62,744	\$ 217,101	\$ 164,270
Recoveries from customers	8,703	6,158	20,306	17,404
Cloud and managed services	16,243	18,573	52,148	32,588
Other	1,514	1,415	7,365	4,131
Total revenues	103,465	88,890	296,920	218,393
Operating Expenses:				
Property operating costs	36,288	30,925	100,715	72,292
Real estate taxes and insurance	2,566	1,462	6,326	4,421
Depreciation and amortization	32,699	24,486	91,693	58,791
General and administrative	19,942	19,440	61,836	47,893
Transaction and integration costs	3,465	1,482	9,385	6,256
Total operating expenses	94,960	77,795	269,955	189,653
Operating income	8,505	11,095	26,965	28,740
Other income and expenses:				
Interest income	1	1	3	2
Interest expense	(6,179)	(5,418)	(17,034)	(15,559)
Other expense, net	1	—	1	(83)
Income before taxes	2,328	5,678	9,935	13,100
Tax benefit of taxable REIT subsidiaries	4,210	2,560	9,269	5,695
Net income	\$ 6,538	\$ 8,238	\$ 19,204	\$ 18,795

See accompanying notes to financial statements.

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QUALITYTECH, LP

INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENT OF PARTNERS' CAPITAL

(unaudited and in thousands)

	Limited Partners' Capital		General Partner's Capital		Total
	Units	Amount	Units	Amount	
Balance January 1, 2016	48,023	\$ 719,866	1	\$ —	\$ 719,866
Net share activity through equity award plan	307	(1,251)	—	—	(1,251)
Equity-based compensation expense	—	7,887	—	—	7,887
Net proceeds from QTS Realty Trust, Inc. equity offering	6,325	275,835	—	—	275,835
Dividends to QTS Realty Trust, Inc.	—	(49,365)	—	—	(49,365)
Partnership distributions	—	(7,433)	—	—	(7,433)
Net income	—	19,204	—	—	19,204
Balance September 30, 2016	54,655	\$ 964,743	1	\$ —	\$ 964,743

See accompanying notes to financial statements.

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QUALITYTECH, LP

INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

STATEMENTS OF CASH FLOW

(unaudited and in thousands)

For the nine months ended September 30, 2016 and 2015

	2016	2015
Cash flow from operating activities:		
Net income	\$ 19,204	\$ 18,795
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	89,104	57,347
Amortization of deferred loan costs	2,424	2,372
Amortization of senior notes discount	194	184
Equity-based compensation expense	7,887	5,206
Bad debt expense	1,201	640
Write off of deferred loan costs	—	83
Deferred tax benefit	(9,298)	(5,695)
Changes in operating assets and liabilities		
Rents and other receivables, net	(9,191)	(2,382)
Prepaid expenses	(2,854)	(4,713)
Other assets	(967)	(352)
Accounts payable and accrued liabilities	3,359	(2,427)
Advance rents, security deposits and other liabilities	984	(437)
Deferred income	1,448	3,698
Net cash provided by operating activities	103,495	72,319
Cash flow from investing activities:		
Acquisitions, net of cash acquired	(122,981)	(288,865)
Additions to property and equipment	(197,751)	(252,156)
Net cash used in investing activities	(320,732)	(541,021)
Cash flow from financing activities:		
Credit facility proceeds	267,000	420,162
Debt repayment	(259,002)	(260,000)
Payment of deferred financing costs	(35)	(577)
Payment of cash dividends	(45,371)	(32,756)
Partnership distributions	(7,189)	(6,652)
Payments to net settle equity awards	(1,252)	—
Principal payments on capital lease obligations	(9,612)	(4,415)
Mortgage principal debt repayments	—	(16,600)
Equity proceeds, net of costs	275,663	369,482
Net cash provided by financing activities	220,202	468,644
Net increase (decrease) in cash and cash equivalents	2,965	(58)

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Cash and cash equivalents, beginning of period	8,804	10,788
Cash and cash equivalents, end of period	\$ 11,769	\$ 10,730
See accompanying notes to financial statements.		

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QUALITYTECH, LP

INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

STATEMENTS OF CASH FLOW (continued)

(unaudited and in thousands)

For the nine months ended September 30, 2016 and 2015

	2016	2015
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash paid for interest (excluding deferred financing costs and amounts capitalized)	\$ 18,659	\$ 17,785
Noncash investing and financing activities:		
Accrued capital additions	\$ 40,344	\$ 48,540
Capital lease and lease financing obligations assumed	\$ —	\$ 43,832
Acquisitions, net of cash acquired:		
Land	\$ 7,440	\$ 1,130
Buildings, improvements and equipment	80,390	78,898
Construction in Progress	13,900	12,127
Rents and other receivables, net	(2,033)	13,704
Acquired intangibles	34,281	93,400
Deferred costs	4,391	—
Prepaid expenses	479	1,653
Goodwill	(7,895)	174,697
Other assets	303	633
Capital lease and lease financing obligations	—	(43,832)
Accounts payable and accrued liabilities	(922)	(8,586)
Advance rents, security deposits and other liabilities	(1,343)	(2,468)
Deferred income	35	(10,818)
Deferred income taxes	(6,045)	(21,673)
Total acquisitions, net of cash acquired	\$ 122,981	\$ 288,865

See accompanying notes to financial statements.

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QTS REALTY TRUST, INC.

QUALITYTECH, LP

NOTES TO UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Description of Business

QTS Realty Trust, Inc. (“QTS”) through its controlling interest in QualityTech, LP (the “Operating Partnership” and collectively with QTS and their subsidiaries, the “Company”) and the subsidiaries of the Operating Partnership, is engaged in the business of owning, acquiring, redeveloping and managing multi-tenant data centers. The Company’s portfolio consists of 24 wholly-owned and leased properties with data centers located throughout the United States, Canada, Europe and Asia.

QTS was formed as a Maryland corporation on May 17, 2013 and completed its initial public offering of 14,087,500 shares of Class A common stock, \$0.01 par value per share (the “IPO”), on October 15, 2013. QTS elected to be taxed as a real estate investment trust (“REIT”), for U.S. federal income tax purposes, commencing with its taxable year ended December 31, 2013. As a REIT, QTS generally is not required to pay federal corporate income taxes on its taxable income to the extent it is currently distributed to its stockholders.

As of September 30, 2016, QTS owned approximately 87.6% of the interests in the Operating Partnership. Substantially all of QTS’ assets are held by, and QTS’ operations are conducted through, the Operating Partnership.

2. Summary of Significant Accounting Policies

Basis of Presentation – The accompanying financial statements have been prepared by management in accordance with accounting principles generally accepted in the United States (“U.S. GAAP”). In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included.

The accompanying financial statements are presented for both QTS Realty Trust, Inc. and QualityTech, LP. References to “QTS” mean QTS Realty Trust, Inc. and its controlled subsidiaries and references to the “Operating Partnership” mean QualityTech, LP and its controlled subsidiaries.

In 2016, the Company adopted ASU 2015-02, Amendments to the Consolidation Analysis. This standard amends certain guidance applicable to the consolidation of various legal entities, including variable interest entities (“VIE”). The Company evaluated the application of the ASU and concluded that no change was required to its accounting for its interest in the Operating Partnership. However, under the new guidance, the Operating Partnership now meets the definition and criteria of a VIE and the Company is the primary beneficiary of the VIE. As discussed below, the Company’s only material asset is its ownership interest in the Operating Partnership, and consequently, all of its assets and liabilities represent those assets and liabilities of the Operating Partnership. The Company’s debt is an obligation of the Operating Partnership where the creditors may have recourse, under certain circumstances, against the credit of the Company.

QTS is the sole general partner of the Operating Partnership, and its only material asset consists of its ownership interest in the Operating Partnership. Management operates QTS and the Operating Partnership as one business. The management of QTS consists of the same employees as the management of the Operating Partnership. QTS does not conduct business itself, other than acting as the sole general partner of the Operating Partnership and issuing public equity from time to time. QTS has not issued or guaranteed any indebtedness. Except for net proceeds from public equity issuances by QTS, which are contributed to the Operating Partnership in exchange for units of limited partnership interest of the Operating Partnership, the Operating Partnership generates all remaining capital required by the business through its operations, the direct or indirect incurrence of indebtedness, and the issuance of partnership units.

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The Company believes, therefore, that providing one set of notes for the financial statements of QTS and the Operating Partnership provides the following benefits:

- enhances investors' understanding of QTS and the Operating Partnership by enabling investors to view the business as a whole in the same manner as management views and operates the business;
- eliminates duplicative disclosure and provides a more streamlined and readable presentation since a substantial portion of the disclosure applies to both QTS and the Operating Partnership; and
- creates time and cost efficiencies through the preparation of one set of notes instead of two separate sets of notes.

In addition, in light of these combined notes, the Company believes it is important for investors to understand the few differences between QTS and the Operating Partnership in the context of how QTS and the Operating Partnership operate as a consolidated company. With respect to balance sheets, the presentation of stockholders' equity and partners' capital are the main areas of difference between the consolidated balance sheets of QTS and those of the Operating Partnership. On the Operating Partnership's consolidated balance sheets, partners' capital includes partnership units that are owned by QTS and other partners. On QTS' consolidated balance sheets, stockholders' equity includes common stock, additional paid in capital, accumulated other comprehensive income (loss) and accumulated dividends in excess of earnings. The remaining equity reflected on QTS's consolidated balance sheet is the portion of net assets that are retained by partners other than QTS, referred to as noncontrolling interests. With respect to statements of operations, the primary difference in QTS' Statements of Operations and Comprehensive Income is that for net income (loss), QTS retains its proportionate share of the net income (loss) based on its ownership of the Operating Partnership, with the remaining balance being retained by the Operating Partnership. These combined notes refer to actions or holdings as being actions or holdings of "the Company." Although the Operating Partnership is generally the entity that enters into contracts, holds assets and issues debt, management believes that these general references to "the Company" in this context is appropriate because the business is one enterprise operated through the Operating Partnership.

As discussed above, QTS owns no operating assets and has no operations independent of the Operating Partnership and its subsidiaries. Also, the Operating Partnership owns no operating assets and has no operations independent of its subsidiaries. Obligations under the 5.875% Senior Notes due 2022 and the unsecured credit facility, both discussed in Note 5, are fully, unconditionally, and jointly and severally guaranteed by the Operating Partnership's existing subsidiaries, other than 1) 2470 Satellite Boulevard, LLC, a subsidiary formed in December 2015 that acquired an office building in Duluth, Georgia and has de minimis operations, and 2) QTS Finance Corporation, the co-issuer of the 5.875% Senior Notes due 2022. As such, condensed consolidating financial information for the guarantors is not being presented in the notes to the interim condensed consolidated financial statements. However, the indenture governing the 5.875% Senior Notes due 2022 restricts the ability of the Operating Partnership to make distributions to QTS, subject to certain exceptions, including distributions required in order for QTS to maintain its status as a real estate investment trust under the Internal Revenue Code of 1986, as amended.

The interim condensed consolidated financial statements of QTS Realty Trust, Inc. for the three and nine months ended September 30, 2016 and 2015, and as of September 30, 2016 and December 31, 2015 present the accounts of QTS Realty Trust, Inc. and its majority owned subsidiaries. This includes the operating results of the Operating Partnership for all periods presented.

Use of Estimates – The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant items subject to such estimates and assumptions include the useful lives of fixed assets, allowances for doubtful accounts and deferred tax assets and the valuation of derivatives, real estate assets, acquired intangible assets and certain accruals.

Principles of Consolidation – The consolidated financial statements of QTS Realty Trust, Inc. include the accounts of QTS Realty Trust, Inc. and its majority-owned subsidiaries. The consolidated financial statements of QualityTech, LP include the accounts of QualityTech, LP and its subsidiaries. All significant intercompany accounts and transactions have been eliminated in the consolidated financial statements.

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Reclassifications – The consolidated balance sheet at December 31, 2015 reflects a reclassification of \$3.1 million from Deferred Costs, net to Unsecured Credit Facility, net, and \$7.1 million from Deferred Costs, net to Senior Notes, net of discount and debt issuance costs as required by the Company’s adoption of ASU 2015-03, “Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs.”

Real Estate Assets – Real estate assets are reported at cost. All capital improvements for the income-producing properties that extend their useful lives are capitalized to individual property improvements and depreciated over their estimated useful lives. Depreciation is generally provided on a straight-line basis over 40 years from the date the property was placed in service. Property improvements are depreciated on a straight-line basis over the life of the respective improvement ranging from 20 to 40 years from the date the components were placed in service. Leasehold improvements are depreciated over the lesser of 20 years or through the end of the respective life of the lease. Repairs and maintenance costs are expensed as incurred. For the three months ended September 30, 2016, depreciation expense related to real estate assets and non-real estate assets was \$20.4 million and \$3.4 million, respectively, for a total of \$23.8 million. For the three months ended September 30, 2015, depreciation expense related to real estate assets and non-real estate assets was \$15.2 million and \$2.7 million, respectively, for a total of \$17.9 million. For the nine months ended September 30, 2016, depreciation expense related to real estate assets and non-real estate assets was \$57.6 million and \$9.5 million, respectively, for a total of \$67.1 million. For the nine months ended September 30, 2015, depreciation expense related to real estate assets and non-real estate assets was \$38.5 million and \$6.2 million, respectively, for a total of \$44.7 million. The Company capitalizes certain development costs, including internal costs incurred in connection with development. The capitalization of costs during the construction period (including interest and related loan fees, property taxes and other direct and indirect costs) begins when development efforts commence and ends when the asset is ready for its intended use. Capitalization of such costs, excluding interest, aggregated to \$2.8 million and \$2.7 million for the three months ended September 30, 2016 and 2015, respectively, and \$9.1 million and \$8.6 million for the nine months ended September 30, 2016 and 2015, respectively. Interest is capitalized during the period of development by first applying the Company’s actual borrowing rate on the related asset and second, to the extent necessary, by applying the Company’s weighted average effective borrowing rate to the actual development and other costs expended during the construction period. Interest is capitalized until the property is ready for its intended use. Interest costs capitalized totaled \$2.5 million and \$2.7 million for the three months ended September 30, 2016 and 2015 respectively, and \$8.4 million and \$7.1 million for the nine months ended September 30, 2016 and 2015, respectively.

Acquisitions – Acquisitions of real estate and other entities are either accounted for as asset acquisitions or business combinations depending on facts and circumstances. Purchase accounting is applied to the assets and liabilities related to all real estate investments acquired in accordance with the accounting requirements of ASC 805, Business Combinations, which requires the recording of net assets of acquired businesses at fair value. The fair value of the consideration transferred is allocated to the acquired tangible assets, consisting primarily of land, building and improvements, and identified intangible assets and liabilities, consisting of the value of above-market and below-market leases, value of in-place leases, value of customer relationships, trade names, software intangibles and capital leases. The excess of the fair value of liabilities assumed, common stock issued and cash paid over the fair value of identifiable assets acquired is allocated to goodwill, which is not amortized by the Company.

In developing estimates of fair value of acquired assets and assumed liabilities, management analyzed a variety of factors including market data, estimated future cash flows of the acquired operations, industry growth rates, current replacement cost for fixed assets and market rate assumptions for contractual obligations. Such a valuation requires management to make significant estimates and assumptions, particularly with respect to the intangible assets.

Acquired in-place leases are amortized on a straight-line basis over the remaining life of the underlying leases. Amortization of acquired in place lease costs totaled \$1.8 million and \$0.4 million for the three months ended September 30, 2016 and 2015, respectively, and \$3.0 million and \$1.3 million for the nine months ended September 30, 2016 and 2015, respectively. This amortization expense is accounted for as real estate amortization expense.

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Acquired customer relationships are amortized on a straight-line basis over the expected life of the customer relationship. Amortization of acquired customer relationships totaled \$2.3 million and \$2.0 million for the three months ended September 30, 2016 and 2015, respectively, and \$7.7 million and \$3.0 million for the nine months ended September 30, 2016 and 2015, respectively. This amortization expense is accounted for as real estate amortization expense. The current period amortization includes a \$1.0 million adjustment related to an increase in the purchase price allocation of the acquired customer relationship intangible recorded in the three months ended March 31, 2016, of which \$0.7 million related to prior reporting periods. See Note 3 for further detail.

Other acquired intangible assets, which includes platform, above or below market leases, and trade name intangibles, are amortized on a straight-line basis over their respective expected lives. Platform and trade name intangibles are amortized as amortization expense. Platform amortization expense was \$0.8 million and \$0.8 million for the three months ended September 30, 2016 and 2015, respectively, and \$2.4 million and \$0.9 million for the nine months ended September 30, 2016 and 2015, respectively. Trade name amortization expense was \$0.3 million and \$0.3 million for the three months ended September 30, 2016 and 2015, respectively, and \$0.8 million and \$0.3 million for the nine months ended September 30, 2016 and 2015, respectively. Above or below market leases are amortized as rent expense in the case of the Company as lessee, which totaled \$0.1 and \$0.2 million for the three and nine months ended September 30, 2016, respectively. Amortization of above or below market leases with the Company as lessee was immaterial for the three and nine months ended September 30, 2015. Above or below market leases are amortized as rental revenue in the case of the Company as lessor, which totaled \$0.2 and \$0.4 million for the three and nine months ended September 30, 2016, respectively. There was no amortization of above or below market leases with the Company as lessor in the three and nine months ended September 30, 2015. The expense associated with trade name intangibles is accounted for as real estate expense, whereas the expense associated with the amortization of platform intangibles is accounted for as non-real estate expense.

See Note 3 for discussion of the final purchase price allocation for the acquisition of Carpathia Hosting, Inc. (“Carpathia”) on June 16, 2015, as well as the preliminary purchase price allocation for the Piscataway, New Jersey facility (the “Piscataway facility”) that the Company acquired on June 6, 2016.

Impairment of Long-Lived and Intangible Assets – The Company reviews its long-lived assets for impairment when events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. Recoverability of assets to be held and used is measured by comparison of the carrying amount to the future net cash flows, undiscounted and without interest, expected to be generated by the asset group. If the net carrying value of the asset exceeds the value of the undiscounted cash flows, the fair value of the asset is assessed and may be considered impaired. An impairment loss is recognized based on the excess of the carrying amount of the impaired asset over its fair value. No impairment losses were recorded for the three and nine months ended September 30, 2016 and 2015, respectively.

The fair value of goodwill is the consideration transferred which is not allocable to identifiable intangible and tangible assets. Goodwill is subject to an annual assessment for impairment, which the Company tests on October 1 each year.

As a result of the Carpathia acquisition, the Company recognized \$173.8 million in goodwill.

Cash and Cash Equivalents – The Company considers all demand deposits and money market accounts purchased with a maturity date of three months or less at the date of purchase to be cash equivalents. The Company’s account balances at one or more institutions periodically exceed the Federal Deposit Insurance Corporation (“FDIC”) insurance coverage and, as a result, there is concentration of credit risk related to amounts on deposit in excess of FDIC coverage. The Company mitigates this risk by depositing a majority of its funds with several major financial institutions. The Company also has not experienced any losses and, therefore, does not believe that the risk is significant.

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Deferred Costs – Deferred costs, net, on the Company’s balance sheets include both financing costs and leasing costs.

As discussed above in Reclassifications, the Company adopted ASU 2015-03 during the three months ended March 31, 2016. Pursuant to this updated guidance, debt issuance costs related to revolving debt arrangements are permitted to be deferred and presented as assets on the balance sheet; however, all other debt issuance costs must be recorded as a direct offset to the associated liability. As such, deferred financing costs on the Company’s consolidated balance sheets represent costs incurred in connection with obtaining only revolving debt arrangements. These costs are amortized over the term of the loan and are included in interest expense. Amortization of debt issuance costs, including those costs presented as offsets to the associated liability in the consolidated balance sheet, was \$0.8 million and \$0.7 million for the three months ended September 30, 2016 and 2015, respectively and \$2.4 million and \$2.1 million for the nine months ended September 30, 2016 and 2015. Deferred financing costs related to revolving debt arrangements, net of accumulated amortization are as follows:

(dollars in thousands)	September 30, 2016 (unaudited)	December 31, 2015
Deferred financing costs	\$ 6,676	\$ 6,652
Accumulated amortization	(1,564)	(389)
Deferred financing costs, net	\$ 5,112	\$ 6,263

Deferred leasing costs consist of external fees and internal costs incurred in the successful negotiations of leases and are deferred and amortized over the terms of the related leases on a straight-line basis. If an applicable lease terminates prior to the expiration of its initial term, the carrying amount of the costs are written off to amortization expense. Amortization of deferred leasing costs totaled \$3.7 million and \$3.1 million for the three months ended September 30, 2016 and 2015, respectively, and \$10.8 million and \$8.6 million for the nine months ended September 30, 2016 and 2015, respectively. Deferred leasing costs, net of accumulated amortization are as follows:

(dollars in thousands)	September 30, 2016 (unaudited)	December 31, 2015
Deferred leasing costs	\$ 45,701	\$ 36,748
Accumulated amortization	(15,099)	(12,970)
Deferred leasing costs, net	\$ 30,602	\$ 23,778

Advance Rents and Security Deposits – Advance rents, typically prepayment of the following month’s rent, consist of payments received from customers prior to the time they are earned and are recognized as revenue in subsequent periods when earned. Security deposits are collected from customers at the lease origination and are generally refunded to customers upon lease expiration.

Deferred Income – Deferred income generally results from non-refundable charges paid by the customer at lease inception to prepare their space for occupancy. The Company records this initial payment, commonly referred to as set-up fees, as a deferred income liability which amortizes into rental revenue over the term of the related lease on a straight-line basis. Deferred income was \$18.4 million and \$17.0 million as of September 30, 2016 and December 31, 2015, respectively. Additionally, \$2.4 million and \$1.5 million of deferred income was amortized into revenue for the three months ended September 30, 2016 and 2015, respectively, and \$6.5 million and \$4.1 million for the nine months ended September 30, 2016 and 2015, respectively.

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Equity-based Compensation – All equity-based compensation is measured at fair value on the grant date or date of modification, as applicable, and recognized in earnings over the requisite service period. Depending upon the settlement terms of the awards, all or a portion of the fair value of equity-based awards may be presented as a liability or as equity in the consolidated balance sheets. Equity-based compensation costs are measured based upon their estimated fair value on the date of grant or modification. Equity-based compensation expense was \$2.6 million and \$2.1 million for the three months ended September 30, 2016 and 2015, respectively, and \$7.9 million and \$5.2 million for the nine months ended September 30, 2016 and 2015, respectively.

Rental Revenue – The Company, as a lessor, has retained substantially all of the risks and benefits of ownership and accounts for its leases as operating leases. For lease agreements that provide for scheduled rent increases, rental income is recognized on a straight-line basis over the non-cancellable term of the leases, which commences when control of the space has been provided to the customer. The amount of the straight-line rent receivable on the balance sheets included in rents and other receivables, net was \$15.9 million and \$9.1 million as of September 30, 2016 and December 31, 2015, respectively. Rental revenue also includes amortization of set-up fees which are amortized over the term of the respective lease as discussed above.

Cloud and Managed Services Revenue – The Company may provide both its cloud product and use of its managed services to its customers on an individual or combined basis. Service fee revenue is recognized as the revenue is earned, which generally coincides with the services being provided.

Allowance for Uncollectible Accounts Receivable – Rents receivable are recognized when due and are carried at cost, less an allowance for doubtful accounts. The Company records a provision for losses on rents receivable equal to the estimated uncollectible accounts, which is based on management's historical experience and a review of the current status of the Company's receivables. As necessary, the Company also establishes an appropriate allowance for doubtful accounts for receivables arising from the straight-lining of rents. The aggregate allowance for doubtful accounts was \$3.7 million and \$5.1 million as of September 30, 2016 and December 31, 2015, respectively.

Capital Leases and Lease Financing Obligations – The Company evaluates leased real estate to determine whether the lease should be classified as a capital or operating lease in accordance with U.S. GAAP.

The Company periodically enters into capital leases for certain equipment. In addition, through its acquisition of Carpathia Hosting, Inc. on June 16, 2015, the Company is now party to capital leases for property and equipment, as well as financing obligations related to a sale-leaseback transaction. The outstanding liabilities for the capital leases were \$20.6 million and \$26.9 million as of September 30, 2016 and December 31, 2015, respectively. The outstanding liabilities for the lease financing obligations were \$21.2 million and \$22.8 million as of September 30, 2016 and December 31, 2015, respectively. The net book value of the assets associated with these leases was approximately \$42.8 million and \$51.0 million as of September 30, 2016 and December 31, 2015, respectively. Depreciation related to the associated assets is included in depreciation and amortization expense in the Statements of Operations and Comprehensive Income.

See Note 3 for further discussion of the acquisition of Carpathia and Note 5 for further discussion of capital leases and lease financing obligations.

Recoveries from Customers – Certain customer leases contain provisions under which the customers reimburse the Company for a portion of the property’s real estate taxes, insurance and other operating expenses, which include certain power and cooling-related charges. The reimbursements are included in revenue as recoveries from customers in the Statements of Operations and Comprehensive Income in the period the applicable expenditures are incurred. Certain customer leases are structured to provide a fixed monthly billing amount that includes an estimate of various operating expenses, with all revenue from such leases included in rental revenues.

Segment Information – The Company manages its business as one operating segment and thus one reportable segment consisting of a portfolio of investments in data centers located primarily in the United States with others in Canada, Europe and Asia.

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Customer Concentrations – As of September 30, 2016, one of the Company’s customers represented 12.8% of its total monthly rental revenue. No other customers exceeded 4% of total monthly rental revenue.

As of September 30, 2016, five of the Company’s customers exceeded 5% of total accounts receivable. In aggregate, these five customers accounted for approximately 41% of total accounts receivable. Two of these five customers individually exceeded 10% of total accounts receivable.

Income Taxes – The Company elected for two of its existing subsidiaries to be taxed as taxable REIT subsidiaries pursuant to the REIT rules of the U.S. Internal Revenue Code.

For the taxable REIT subsidiaries, income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

As of December 31, 2014, one of the taxable REIT subsidiaries’ deferred tax assets were primarily the result of U.S. net operating loss carryforwards. A valuation allowance was recorded against its gross deferred tax asset balance as of December 31, 2014. As a result of the acquisition of Carpathia, the Company determined that it was more likely than not that pre-existing deferred tax assets will be realized by the combined entity, and the valuation allowance was eliminated. The change in the valuation allowance resulting from the change in circumstances was included in income, recognized in deferred income tax benefit in the year ended December 31, 2015.

In addition to the deferred income tax benefit recognized in the prior year in connection with the elimination of the valuation allowance, a deferred tax benefit was recognized in the three and nine months ended September 30, 2016 in connection with recorded operating losses. The taxable REIT subsidiary consolidated group has a net deferred tax liability position primarily due to the customer-based intangibles acquired as part of the Carpathia acquisition.

The Company provides for income taxes during interim periods based on the estimated effective tax rate for the year. The effective tax rate is subject to change in the future due to various factors such as the operating performance of the taxable REIT subsidiary, tax law changes and future business acquisitions. The taxable REIT subsidiary’s effective tax rates were 48.9% and 28.4% for the nine months ended September 30, 2016 and 2015, respectively. The increase in the effective tax rate is primarily due to the elimination of the valuation allowance as a result of the Carpathia acquisition, recorded operating losses of the taxable REIT subsidiary in the current year, and permanent book and tax

differences. Additionally, during the three and nine months ended September 30, 2016 the Company recognized additional tax benefits associated with differences between the 2015 tax provision and the amounts as reflected in the Company's final 2015 tax returns.

Fair Value Measurements – ASC Topic 820, Fair Value Measurements, 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, a fair-value hierarchy is established 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).

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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, foreign exchange 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.

There are no financial assets or liabilities measured at fair value on a recurring basis on the consolidated balance sheets as of September 30, 2016 and December 31, 2015. The Company's purchase price allocations of Carpathia and Piscataway are fair value estimates that utilized Level 3 inputs and are measured on a non-recurring basis. See Note 3 for further detail.

New Accounting Pronouncements

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606), which supersedes the current revenue recognition requirements in ASC 605, Revenue Recognition. Under this new guidance, entities should recognize revenues to depict the transfer of promised goods or services to customers in an amount that reflects the consideration the entity expects to receive in exchange for those goods or services. This ASU also requires enhanced disclosures. In April 2016, the FASB finalized amendments to the guidance on identifying performance obligations and accounting for licenses of intellectual property. In May 2016, the FASB finalized amendments to the guidance related to the assessment of collectibility, the definition of completed contracts at transition, and the measurement of the fair value of non-cash consideration at contract inception. The FASB also added new practical expedients for the presentation of sales taxes collected from customers and the accounting for contract modifications at transition. These amendments are not intended to change the core principles of the standard; however, they are intended to clarify important aspects of the guidance and improve its operability, as well as to address implementation issues. The amendments have the same effective date and transition requirements as the new revenue standard, which is effective for annual and interim periods beginning after December 15, 2017. Early adoption is permitted; however, entities are not permitted to adopt the standard earlier than December 15, 2016, the original effective date. Retrospective and modified retrospective application is allowed. The Company is currently assessing the impact of this standard on its consolidated financial statements.

In April 2015, the FASB issued ASU 2015-03, Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. The amendments in this ASU require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts, and not as a separate deferred charge. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this ASU. In June 2015, the Securities and

Exchange Commission (“SEC”) stated that given the absence of authoritative guidance within this ASU for debt issuance costs related to revolving debt arrangements, the SEC staff would not object to an entity deferring and presenting such costs as an asset and subsequently amortizing them ratably over the term of the revolving debt arrangement. This announcement confirms that revolver arrangement costs are not within the scope of this ASU. The amendments in this ASU are effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. The amendments are required to be applied on a retrospective basis, and upon transition, an entity is required to comply with the applicable disclosures for a change in an accounting principle. The Company adopted this standard in the three months ended March 31, 2016. See Reclassifications in Note 2 for further detail.

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In September 2015, the FASB issued ASU 2015-16, Simplifying the Accounting for Measurement-Period Adjustments, that eliminates the requirement to restate prior period financial statements for measurement period adjustments. The new guidance requires that the cumulative impact of a measurement period adjustment (including the impact on prior periods) be recognized in the reporting period in which the adjustment is identified. The amendments in this ASU are effective for fiscal years beginning after December 15, 2015, including interim periods within those fiscal years, and should be applied prospectively to adjustments to provisional amounts that occur after the effective date with earlier application permitted for financial statements that have not been issued. The Company adopted this standard in the nine months ended September 30, 2016, and the effect is reflected in the financial statements accordingly.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842), which supersedes the current lease guidance in ASC 840, Leases. The core principle of Topic 842 requires lessees to recognize the assets and liabilities that arise from nearly all leases in the statement of financial position. Accounting applied by lessors will remain largely consistent with previous guidance, with additional changes set to align lessor accounting with the revised lessee model and the FASB's revenue recognition guidance in Topic 606. The amendments in this ASU are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. The Company is currently assessing the impact of this standard on its consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, Improvements to Employee Share-Based Payment Accounting, which amends ASC 718, Compensation – Stock Compensation. The ASU includes provisions intended to simplify various aspects related to how share-based payments are accounted for and presented in the financial statements, including simplified income tax accounting for stock-based compensation, enhanced tax withholding rules, accounting policy options with regard to forfeitures and clarified guidance on statement of cash flow presentation. ASU 2016-09 is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. Early adoption is permitted. The Company is currently assessing the impact of this standard on its consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments. The standard provides guidance on eight specific cash flow classification issues including debt prepayment or debt extinguishment costs, contingent consideration payments made after a business combination, and separately identifiable cash flows and application of the predominance principle. The standard will be effective for fiscal years beginning January 1, 2018, and subsequent interim periods. The Company does not expect the provisions of the standard will have a material impact on its consolidated financial statements.

3. Acquisitions

Piscataway Acquisition

On June 6, 2016, the Company completed the acquisition of the Piscataway facility for approximately \$125.8 million (based on the preliminary assessment of the fair value of assets acquired and liabilities assumed). This facility is located in the New York metro area on 38 acres and consists of 360,000 gross square feet, including approximately 89,000 square feet of raised floor, and approximately 18 MW of critical power. The Piscataway facility supports future growth with space for an additional approximately 87,000 square feet of raised floor in the existing structure, as well as capacity for over 8 MW of additional critical power. This acquisition was funded with a draw on the unsecured revolving credit facility.

The Company accounted for this acquisition in accordance with ASC 805, Business Combinations, as a business combination. The Company is generally valuing the assets acquired and liabilities assumed using Level 3 inputs.

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The following table summarizes the consideration for the Piscataway facility and the preliminary allocation of the fair value of assets acquired and liabilities assumed at the acquisition date (unaudited and in thousands). This allocation is subject to change pending the final valuation of these assets and liabilities:

	Piscataway Allocation as of September 30, 2016	Original Allocation Reported as of June 30, 2016	Adjusted Fair Value
Land	\$ 7,440	\$ 7,440	\$ —
Buildings and improvements	80,391	78,370	2,021
Construction in progress	13,900	13,900	—
Acquired intangibles	19,581	21,668	(2,087)
Deferred costs	4,391	4,084	307
Other assets	106	106	—
Total identifiable assets acquired	125,809	125,568	241
Acquired below market lease	809	568	241
Net working capital	2,019	2,019	—
Total liabilities assumed	2,828	2,587	241
Net identifiable assets acquired	\$ 122,981	\$ 122,981	\$ —

Acquired intangibles are amortized as both amortization expense as well as offsets to rental revenue. Based on the preliminary purchase price allocation, amortization expenses relative to acquired in place leases are expected to be approximately \$3.0 million, \$4.0 million, \$2.9 million, \$2.3 million and \$1.7 million for the years ended December 31, 2016 through December 31, 2020, respectively. Additionally, based on the preliminary purchase price allocation, amortization expenses relative to acquired above and below market leases recorded as net offsets to rental revenue are expected to be approximately \$0.9 million, \$1.1 million, \$0.7 million, \$0.5 million and \$0.6 million for the years ended December 31, 2016 through December 31, 2020, respectively.

Carpathia Acquisition

On June 16, 2015, the Company completed the acquisition of 100% of the outstanding stock of Carpathia Hosting, Inc., a Virginia-based colocation, cloud and managed services provider for approximately \$373.6 million (based on the final assessment of the fair value of assets acquired and liabilities assumed). Upon completion of this acquisition, the Company assumed all of the assets and liabilities of Carpathia Acquisition, Inc. Carpathia Acquisition, Inc. and its subsidiaries, including Carpathia, became indirect, wholly-owned subsidiaries of the Company. Carpathia was a provider of colocation, hybrid cloud and Infrastructure-as-a-Service (IaaS) servicing enterprise customers and federal agencies, with a customer base of approximately 230 customers as of June 16, 2015. Carpathia utilized eight domestic

data centers located in Dulles, Virginia; Phoenix, Arizona; San Jose, California; Harrisonburg, Virginia and Ashburn, Virginia; and five international data centers located in Toronto, Canada; Amsterdam, Netherlands; London, United Kingdom; Hong Kong, China and Sydney, Australia. The Company no longer leases the Sydney, Australia data center.

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The Company accounted for this acquisition in accordance with ASC 805, Business Combinations, as a business combination. The Company generally valued the assets acquired and liabilities assumed using Level 3 inputs.

In June 2016, the Company finalized the Carpathia purchase price allocation. The following table summarizes the consideration for the Carpathia acquisition and the final allocation of the fair value of assets acquired and liabilities assumed at the acquisition date (unaudited and in thousands):

	Final Carpathia Allocation as of June 30, 2016
Land	\$ 1,130
Buildings and improvements	78,898
Construction in progress	12,127
Acquired intangibles	108,100
Net working capital	2,851
Total identifiable assets acquired	203,106
Capital lease and lease financing obligations	43,832
Deferred income taxes	35,980
Acquired above market lease	2,453
Total liabilities assumed	82,265
Net identifiable assets acquired	120,841
Goodwill	173,843
Net assets acquired	\$ 294,684

Goodwill recognized in the transaction relates primarily to anticipated operating synergies, Carpathia's in-place workforce and access to Carpathia's customer pipeline. For tax purposes, the Company acquired goodwill with a tax basis of \$16.6 million, which is deductible in subsequent periods. Based on the final purchase price allocation, amortization expenses relative to the intangible assets acquired are expected to be approximately \$12.2 million, \$12.2 million, \$10.1 million, \$8.0 million and \$8.0 million for the years ended December 31, 2016 through December 31, 2020, respectively.

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The following table represents the pro forma condensed consolidated statement of operations of the combined entities for the nine months ended September 30, 2015 (in thousands):

	(Unaudited) Pro Forma Condensed Consolidated Statements of Operations Nine Months Ended September 30, 2015	
Revenue	\$	285,769
Net income	\$	10,901

These amounts have been calculated after applying the Company's accounting policies, and give effect to the Carpathia acquisition.

The unaudited pro forma condensed consolidated financial information is for comparative purposes only and not necessarily indicative of what actual results of operations of the Company would have been had the transaction noted above been consummated on January 1, 2015, nor does it purport to represent the results of operations for future periods.

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4. Real Estate Assets and Construction in Progress

The following is a summary of properties owned or leased by the Company as of September 30, 2016 and December 31, 2015 (in thousands):

As of September 30, 2016 (unaudited):

Property Location	Land	Buildings, Improvements and Equipment	Construction in Progress	Total Cost
Owned Properties				
Suwanee, Georgia (Atlanta-Suwanee)	\$ 3,521	\$ 155,443	\$ 16,130	\$ 175,094
Atlanta, Georgia (Atlanta-Metro)	15,397	432,302	30,338	478,037
Santa Clara, California*	—	97,170	5,731	102,901
Richmond, Virginia	2,180	236,610	68,270	307,060
Sacramento, California	1,481	61,905	222	63,608
Princeton, New Jersey	20,700	32,776	500	53,976
Dallas-Fort Worth, Texas	8,606	152,575	99,637	260,818
Chicago, Illinois	9,400	45,393	74,277	129,070
Miami, Florida	1,777	31,089	74	32,940
Lenexa, Kansas	437	3,733	0	4,170
Duluth, Georgia Office Building	1,899	1,896	1,611	5,406
Piscataway, New Jersey	7,440	81,638	14,726	103,804
	72,838	1,332,530	311,516	1,716,884
Leased Properties				
Leased facilities acquired in 2015 ***	1,130	93,034	6,894	101,058
Jersey City, New Jersey	—	22,853	2,232	25,085
Overland Park, Kansas	—	959	** 8	967
	1,130	116,846	9,134	127,110
	\$ 73,968	\$ 1,449,376	\$ 320,650	\$ 1,843,994

* Owned facility subject to long-term ground sublease.

** This does not include the portion of the business that is used for QTS office space or other real estate not used by customers.

*** Includes 12 facilities. All facilities are leased, including those subject to capital leases.

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As of December 31, 2015:

Property Location	Land	Buildings, Improvements and Equipment	Construction in Progress	Total Cost
Owned Properties				
Suwanee, Georgia (Atlanta-Suwanee)	\$ 3,521	\$ 150,028	\$ 15,330	\$ 168,879
Atlanta, Georgia (Atlanta-Metro)	15,397	406,190	41,835	463,422
Santa Clara, California*	—	94,437	1,379	95,816
Richmond, Virginia	2,180	208,654	85,771	296,605
Sacramento, California	1,481	61,462	73	63,016
Princeton, New Jersey	20,700	32,708	422	53,830
Dallas-Fort Worth, Texas	8,590	71,783	120,331	200,704
Chicago, Illinois	—	—	70,749	70,749
Miami, Florida	1,777	30,554	144	32,475
Lenexa, Kansas	437	3,511	—	3,948
Duluth, Georgia Office Building	1,899	1,920	—	3,819
	55,982	1,061,247	336,034	1,453,263
Leased Properties				
Leased facilities acquired in 2015 ***	1,130	89,989	7,196	98,315
Jersey City, New Jersey	—	28,228	2,421	30,649
Overland Park, Kansas	—	922	** 4	926
	1,130	119,139	9,621	129,890
	\$ 57,112	\$ 1,180,386	\$ 345,655	\$ 1,583,153

* Owned facility subject to long-term ground sublease.

** This does not include the portion of the business that is used for QTS office space or other real estate not used by customers.

*** Includes 13 facilities. All facilities are leased, including those subject to capital leases.

5. Debt

Below is a listing of the Company's outstanding debt, including capital leases and lease financing obligations, as of September 30, 2016 and December 31, 2015 (in thousands):

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	Weighted Average		September	December
	Coupon Interest Rate at	Maturities	30,	31,
	September 30, 2016		2016	2015
			(unaudited)	
Unsecured Credit Facility				
Revolving Credit Facility		December 17,		
	2.07%	2019	\$ 232,000	\$ 224,002
Term Loan I		December 17,		
	2.02%	2020	150,000	150,000
Term Loan II	2.03%	April 27, 2021	150,000	150,000
Senior Notes	5.88%	August 1, 2022	300,000	300,000
Capital Lease and Lease Financing				
Obligations	3.45%	2017 - 2025	41,825	49,761
	3.43%		873,825	873,763
Less discount and net debt issuance				
costs			(10,763)	(12,194)
Total outstanding debt, net			\$ 863,062	\$ 861,569

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Credit Facility and Senior Notes

(a) Unsecured Credit Facility – In October 2015, the Company amended and restated its unsecured credit facility, increasing the total capacity by \$250 million and extending the term. At the same time, the Company terminated its secured credit facility relating to the Richmond data center. The amended unsecured credit facility has a total capacity of \$900 million and includes a \$150 million term loan which matures on December 17, 2020, another \$150 million term loan which matures on April 27, 2021, and a \$600 million revolving credit facility which matures on December 17, 2019, with a one year extension option. Amounts outstanding under the amended unsecured credit facility bear interest at a variable rate equal to, at the Company’s election, LIBOR or a base rate, plus a spread that will vary depending upon the Company’s leverage ratio. For revolving credit loans, the spread ranges from 1.55% to 2.15% for LIBOR loans and 0.55% to 1.15% for base rate loans. For term loans, the spread ranges from 1.50% to 2.10% for LIBOR loans and 0.50% to 1.10% for base rate loans. The amended unsecured credit facility also includes a \$200 million accordion feature.

Under the amended unsecured credit facility, the capacity may be increased from the current capacity of \$900 million to \$1.1 billion subject to certain conditions set forth in the credit agreement, including the consent of the administrative agent and obtaining necessary commitments. The Company is also required to pay a commitment fee to the lenders assessed on the unused portion of the unsecured revolving credit facility. At the Company’s election, the Company can prepay amounts outstanding under the unsecured credit facility, in whole or in part, without penalty or premium.

The unsecured credit facility requires monthly interest payments and requires the Company to comply with various customary affirmative and negative covenants and quarterly financial covenant requirements relating to the debt service coverage ratio, fixed charge ratio, leverage ratio and tangible net worth and various other operational requirements. In connection with the unsecured credit facility, as of September 30, 2016, the Company had an additional \$2.6 million of letters of credit outstanding. The Company entered into two of these letters of credit in June 2016 related to its Chicago facility and recently acquired Piscataway facility in the amounts of \$0.5 million and \$0.1 million, respectively. As of September 30, 2016, borrowings under the unsecured credit facility consisted of \$232.0 million outstanding under the revolving credit facility and \$300.0 million outstanding under the term loans, exclusive of net debt issuance costs of \$2.6 million. As of September 30, 2016, the weighted average interest rate for amounts outstanding under the unsecured credit facility was 2.04%.

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(b) Senior Notes – On July 23, 2014, the Operating Partnership and QTS Finance Corporation, a subsidiary of the Operating Partnership formed solely for the purpose of facilitating the offering of the notes described below (collectively, the “Issuers”), issued \$300 million aggregate principal amount of 5.875% Senior Notes due 2022 (the “Senior Notes”). The Senior Notes have an interest rate of 5.875% per annum, were issued at a price equal to 99.211% of their face value and mature on August 1, 2022. The proceeds from the offering were used to repay amounts outstanding under the unsecured credit facility, including \$75 million outstanding under the term loan. As of September 30, 2016, the discount recorded on the Senior Notes was \$1.8 million and the outstanding net debt issuance costs associated with the Senior Notes were \$6.3 million.

The Senior Notes are unconditionally guaranteed, jointly and severally, on a senior unsecured basis by all of the Operating Partnership’s existing subsidiaries (other than foreign subsidiaries, receivables entities and 2470 Satellite Boulevard, LLC, which is a Delaware limited liability company formed in December 2015 that acquired an office building in Duluth, Georgia and has de minimis operations) and future subsidiaries that guarantee any indebtedness of QTS Realty Trust, Inc., the Issuers or any other subsidiary guarantor. QTS Realty Trust, Inc. does not guarantee the Senior Notes and will not be required to guarantee the Senior Notes except under certain circumstances. The offering was conducted pursuant to Rule 144A of the Securities Act of 1933, as amended, and the Senior Notes were issued pursuant to an indenture, dated as of July 23, 2014, among the Operating Partnership, QTS Finance Corporation, the Company, the guarantors named therein, and Deutsche Bank Trust Company Americas, as trustee (the “Indenture”).

On March 23, 2015, the SEC declared effective the Operating Partnership and QTS Finance Corporation’s registration statement on Form S-4 pursuant to which the issuers exchanged the originally issued Senior Notes for \$300 million of 5.875% Senior Notes due 2022 (the “Exchange Notes”) that are registered under the Securities Act of 1933, as amended. The exchange offer was completed on April 23, 2015, and all outstanding originally issued Senior Notes were tendered. The Exchange Notes did not provide the Company with any additional proceeds and satisfied its obligations under a registration rights agreement entered into in connection with the issuance of the Senior Notes.

The annual remaining principal payment requirements as of September 30, 2016 per the contractual maturities and excluding extension options, capital leases and lease financing obligations, are as follows (unaudited and in thousands):

2016	\$ —
2017	—
2018	—
2019	232,000
2020	150,000
Thereafter	450,000
Total	\$ 832,000

As of September 30, 2016, the Company was in compliance with all of its covenants.

Capital Leases

The Company has historically entered into capital leases for certain equipment. In addition, through its acquisition of Carpathia on June 16, 2015, the Company acquired capital leases of both equipment and certain properties. Total outstanding liabilities for capital leases were \$20.6 million as of September 30, 2016, of which \$12.6 million were assumed through the Carpathia acquisition, all of which was related to the lease of real property. Carpathia had entered into capital lease arrangements for datacenter space under two lease agreements expiring in 2018 and 2019 at its Harrisonburg, Virginia and Ashburn, Virginia locations. Total recurring monthly payments range from approximately \$0.2 million to \$0.5 million during the terms of the leases, in addition to payments made for utilities. Depreciation related to the associated assets for the capital leases is included in depreciation and amortization expense in the Statements of Operations and Comprehensive Income.

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Lease Financing Obligations

Through the acquisition of Carpathia, the Company acquired lease financing obligations totaling \$21.2 million at September 30, 2016, of which \$19.4 million related to a sale-leaseback transaction where Carpathia has continuing involvement. On December 23, 2011, Carpathia sold the shell of a building and the associated land to an unrelated third party. Carpathia leases the property back and is a party to an agreement with the same third party to construct a new building on the adjoining property for use as a data center. Carpathia is primarily responsible for financing the improvements and outfitting the building with the necessary equipment. The third party leases back the new building in stages to Carpathia as the various stages are completed. In accordance with ASC 840-40, Leases, Carpathia has continuing involvement with the related leased assets; therefore, the Company will continue to account for the existing building shell and the associated land as fixed assets and will capitalize the construction costs of the new building. The financing obligation related to the building and equipment was \$17.9 million at September 30, 2016. In addition, due to Carpathia's continuing involvement, it was required to defer a gain on the sale of the assets. The deferred gain was \$1.5 million at September 30, 2016, and is also included in lease financing obligations.

The financing obligation is reduced as rental payments are made on the existing building, which payments started in January 2012. Rental payments, which include amounts attributable to both principal and interest, increased to approximately \$0.2 million per month in March 2013, which is when the newly constructed building was inhabited by Carpathia. Depreciation expense on the related asset is included in depreciation and amortization expense in the Statements of Operations and Comprehensive Income.

The Company, through its acquisition of Carpathia, also has a lease financing agreement in connection with a \$4.8 million tenant improvement allowance on one of its data center lease agreements. The financing requires monthly payments of principal and interest of less than \$0.1 million through February 2019. The outstanding balance on the financing agreement was \$1.8 million as of September 30, 2016. Depreciation expense on the related leasehold improvements is included in depreciation and amortization expense in the Statements of Operations and Comprehensive Income.

The following table summarizes the Company's combined future payment obligations, excluding interest, as of September 30, 2016, on the capital leases and lease financing obligations above (unaudited and in thousands):

2016	\$ 3,117
2017	12,944
2018	9,370
2019	2,844
2020	2,190
Thereafter	11,360
Total	\$ 41,825

6. Commitments and Contingencies

The Company is subject to various routine legal proceedings and other matters in the ordinary course of business. One of the Company's subsidiaries, Carpathia Hosting, LLC ("Carpathia LLC"), was named as a defendant in a lawsuit filed in state court in New York. Carpathia LLC's customer, Portal Healthcare Solutions ("Portal Ascend") allegedly had a security breach between November 2012 and March 2013. Portal Ascend has agreed to indemnify Carpathia LLC in this litigation and has provided legal counsel to defend Carpathia LLC. The plaintiffs have filed a motion to certify the action as a class action. The litigation is in the earliest stages, thus the outcome of this litigation is neither probable nor reasonably estimable.

7. Partners' Capital, Equity and Incentive Compensation Plans

QualityTech, LP

QTS has the full power and authority to do all the things necessary to conduct the business of the Operating Partnership.

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As of September 30, 2016, the Operating Partnership had two classes of limited partnership units outstanding: Class A units of limited partnership interest (“Class A units”) and Class O LTIP units of limited partnership units (“Class O units”). The Operating Partnership previously had outstanding Class RS LTIP units of limited partnership interest (“Class RS units”) which have all been converted to Class A Units during the three months ended September 30, 2016. The Class A Units are now redeemable at any time. The Company may in its sole discretion elect to assume and satisfy the redemption amount with cash or its shares. Class RS units or Class O units were issued upon grants made under the QualityTech, LP 2010 Equity Incentive Plan (the “2010 Equity Incentive Plan”). Class RS units and Class O units may be subject to vesting and are pari passu with Class A units. Each Class RS unit and Class O unit is convertible into Class A units by the Operating Partnership at any time or by the holder at any time following full vesting (if such unit is subject to vesting) based on formulas contained in the partnership agreement.

QTS Realty Trust, Inc.

In connection with its IPO, QTS issued Class A common stock and Class B common stock. Class B common stock entitles the holder to 50 votes per share and was issued to enable the Company’s Chief Executive Officer to exchange 2% of his Operating Partnership units so he may have a vote proportionate to his economic interest in the Company. Also in connection with its IPO, QTS adopted the QTS Realty Trust, Inc. 2013 Equity Incentive plan (the “2013 Equity Incentive Plan”), which authorized 1.75 million shares of Class A common stock to be issued under the plan, including options to purchase Class A common stock, restricted Class A common stock, Class O units, and Class RS units. In May 2015, the total number of shares available for issuance under the 2013 Equity Incentive Plan was increased to 4,750,000.

The following is a summary of award activity under the 2010 Equity Incentive Plan and 2013 Equity Incentive Plan and related information for the nine months ended September 30, 2016 (unaudited):

	2010 Equity Incentive Plan			2013 Equity Incentive Plan						
	Number of Class O units	Weighted average exercise price	Weighted average fair value	Number of Class RS units	Weighted average grant date value	Options	Weighted average exercise price	Weighted average fair value	Restricted Stock	
ing at er 31,	1,292,899	\$ 23.76	\$ 3.68	39,875	\$ 22.18	867,882	\$ 27.80	\$ 5.56	394,908	\$
d/Vested	—	—	—	—	—	229,693	45.78	9.91	236,148	
from	(125,992)	21.45	4.28	—	—	(29,543)	25.70	4.96	(83,139)	(1)
n (2)	—	—	—	(39,875)	22.18	—	—	—	—	
	—	—	—	—	—	(9,735)	32.14	6.95	(85,820)	

d/Expired

ing at
er 30,

1,166,907	\$ 24.00	\$ 3.61	—	\$ —	1,058,297	\$ 31.72	\$ 6.51	462,097	\$
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- (1) This represents the Class A common stock that has been released from restriction and which was not surrendered by the holder to satisfy their statutory minimum federal and state tax obligations associated with the vesting of restricted common stock.
- (2) This represents Class RS units that upon vesting have converted to Operating Partnership units.
- (3) Includes approximately 40,000 restricted Class A common stock surrendered by certain employees to satisfy their statutory minimum federal and state tax obligations associated with the vesting of restricted common stock.

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The assumptions and fair values for restricted stock and options to purchase shares of Class A common stock granted for the nine months ended September 30, 2016 are included in the following table on a per unit basis (unaudited). Class O units and options to purchase shares of Class A common stock were valued using the Black-Scholes model.

	Nine Months Ended September 30, 2016
Fair value of restricted stock granted	\$45.78-\$56.28
Fair value of options granted	\$9.57-\$9.97
Expected term (years)	5.5-5.9
Expected volatility	30.7-31.3%
Expected dividend yield	3.14%
Expected risk-free interest rates	1.42-1.48%

The following table summarizes information about awards outstanding as of September 30, 2016 (unaudited).

	Operating Partnership Awards Outstanding		
	Exercise prices	Awards outstanding	Weighted average remaining vesting period (years)
Class RS Units	\$ —	—	—
Class O Units	\$ 20.00-25.00	1,166,907	0.1
Total Operating Partnership awards outstanding		1,166,907	

	QTS Realty Trust, Inc. Awards Outstanding		
	Exercise prices	Awards outstanding	Weighted average remaining vesting period (years)
Restricted stock	\$ —	462,097	1.8
Options to purchase Class A common stock	\$ 21.00-45.78	1,058,297	1.0
Total QTS Realty Trust, Inc. awards outstanding		1,520,394	

All nonvested LTIP unit awards are valued as of the grant date and generally vest ratably over a defined service period. Certain nonvested LTIP unit awards vest on the earlier of achievement by the Company of various performance goals or specified dates in 2015 and 2016. As of September 30, 2016 there were 0.1 million, 0.5 million and 0.4 million nonvested Class O units, restricted Class A common stock and options to purchase Class A common

stock outstanding, respectively. As of September 30, 2016, there were no Class RS units outstanding. As of September 30, 2016 the Company had \$18.7 million of unrecognized equity-based compensation expense which will be recognized over the remaining vesting period of up to 4 years. The total intrinsic value of the awards outstanding at September 30, 2016 was \$80.1 million.

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Dividends and Distributions

The following tables present quarterly cash dividends and distributions paid to QTS' common stockholders and the Operating Partnership's unit holders for the nine months ended September 30, 2016 and 2015 (unaudited):

Nine Months Ended September 30, 2016

Record Date	Payment Date	Per Common Share and Per Unit Rate	Aggregate Dividend/Distribution Amount (in millions)
June 17, 2016	July 6, 2016	\$ 0.36	\$ 19.7
March 18, 2016	April 5, 2016	0.36	17.4
December 17, 2015	January 6, 2016	0.32	15.4
			\$ 52.5

Nine Months Ended September 30, 2015

Record Date	Payment Date	Per Common Share and Per Unit Rate	Aggregate Dividend/Distribution Amount (in millions)
June 19, 2015	July 8, 2015	\$ 0.32	\$ 15.3
March 20, 2015	April 7, 2015	0.32	13.4
December 19, 2014	January 7, 2015	0.29	10.7
			\$ 39.4

Additionally, on October 5, 2016, the Company paid its regular quarterly cash dividend of \$0.36 per common share and per unit in the Operating Partnership to stockholders and unit holders of record as of the close of business on September 20, 2016.

Equity Issuances

In March 2016, QTS filed an automatic shelf registration statement on Form S-3 with the SEC. Effective upon filing, the shelf provides for the potential sale of an unspecified amount of QTS' Class A common stock, preferred stock, depositary shares representing preferred stock, warrants and rights to purchase QTS common stock or any combination thereof, subject to the ability of QTS to effect offerings on satisfactory terms based on prevailing conditions. Pursuant to this shelf registration, on April 1, 2016, the Company issued 6,325,000 shares of QTS' Class A common stock at a price of \$45.50 per share in an underwritten public offering, including the exercise in full of the underwriters' option to purchase an additional 825,000 shares. The Company used substantially all of the net proceeds of approximately \$276 million to repay amounts outstanding under its unsecured revolving credit facility.

QTS Realty Trust, Inc. Employee Stock Purchase Plan

In June 2015, the Company established the QTS Realty Trust, Inc. Employee Stock Purchase Plan (the “Plan”) to give eligible employees the opportunity to purchase, through payroll deductions, shares of the Company’s Class A common stock in the open market by an independent broker selected by the Company’s Board of Directors (the “Board”) or the plan’s administrator. Eligible employees include employees of the Company and its majority-owned subsidiaries (excluding executives) who have been employed for at least thirty days and who perform at least thirty hours of service per week for the Company. The Plan became effective July 1, 2015 and is administered by the Board or by a committee of one or more persons appointed by the Board. The Company has reserved 250,000 shares for purchase under the Plan and has also agreed to pay the brokerage commissions and fees associated with a Plan participant's purchase of shares. An eligible employee may deduct a minimum of \$40 per month and a maximum of \$2,000 per month towards the purchase of shares. On June 17, 2015, the Company filed a registration statement on Form S-8 to register the 250,000 shares of the Company’s Class A common stock related to the Plan.

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8. Related Party Transactions

The Company periodically executes transactions with entities affiliated with its Chairman and Chief Executive Officer. Such transactions include automobile, furniture and equipment purchases as well as building operating lease payments and receipts, and reimbursement for the use of a private aircraft service by the Company's officers and directors.

The transactions which occurred during the three and nine months ended September 30, 2016 and 2015 are outlined below (unaudited and in thousands):

(dollars in thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Tax, utility, insurance and other reimbursement	\$ 155	\$ 63	\$ 527	\$ 208
Rent expense	254	254	761	761
Capital assets acquired	24	38	191	163
Total	\$ 433	\$ 355	\$ 1,479	\$ 1,132

9. Noncontrolling Interest

Concurrently with the completion of the IPO, QTS consummated a series of transactions pursuant to which QTS became the sole general partner and majority owner of QualityTech, LP, which then became its operating partnership. The previous owners of QualityTech, LP retained 21.2% ownership of the Operating Partnership.

Commencing at any time beginning November 1, 2014, at the election of the holders of the noncontrolling interest, the Class A units are redeemable for cash or, at the election of the Company, common stock of the Company on a one-for-one basis. As a result of these redemptions of Class A units into common stock and the issuance of additional common stock, the noncontrolling ownership interest of QualityTech, LP, was 12.4% at September 30, 2016.

10. Earnings per share of QTS Realty Trust, Inc.

Basic income (loss) per share is calculated by dividing the net income (loss) attributable to common shares by the weighted average number of common shares outstanding during the period. Diluted income (loss) per share adjusts basic income (loss) per share for the effects of potentially dilutive common shares.

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The computation of basic and diluted net income per share is as follows (in thousands, except per share data, and unaudited):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Numerator:				
Net income available to common stockholders - basic	\$ 5,730	\$ 7,009	\$ 16,719	\$ 15,723
Effect of net income attributable to noncontrolling interests	808	1,229	2,485	3,072
Net income available to common stockholders - diluted	\$ 6,538	\$ 8,238	\$ 19,204	\$ 18,795
Denominator:				
Weighted average shares outstanding - basic	47,855	40,994	45,651	36,355
Effect of Class A and Class RS partnership units *	6,767	6,932	6,787	7,103
Effect of Class O units and options to purchase Class A common stock on an "as if" converted basis *	1,066	807	982	724
Weighted average shares outstanding - diluted	55,688	48,733	53,420	44,182
Net income per share attributable to common stockholders - basic	\$ 0.12	\$ 0.17	\$ 0.37	\$ 0.43
Net income per share attributable to common stockholders - diluted	\$ 0.12	\$ 0.17	\$ 0.36	\$ 0.43

* The Class A units, Class RS units and Class O units represent limited partnership interests in the Operating Partnership, and are described in more detail in Note 7.

No securities were antidilutive for the three months ended September 30, 2016 and 2015, or the nine months ended September 30, 2016 and 2015, and as such, no securities were excluded from the computation of diluted net income per share for those periods.

11. Customer Leases, as Lessor

Future minimum lease payments to be received under non-cancelable operating customer leases (inclusive of payments for contracts which have not yet commenced, and exclusive of recoveries of operating costs from customers) are as follows for the years ending December 31 (unaudited and in thousands):

2016 (October - December)	\$ 88,736
2017	299,141
2018	218,803

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2019	142,179
2020	113,147
Thereafter	238,487
Total	\$ 1,100,493

12. Fair Value of Financial Instruments

ASC Topic 825 requires disclosure of fair value information about financial instruments, whether or not recognized in the consolidated balance sheets, for which it is practicable to estimate that value. In cases where quoted market prices are not available, fair values are based upon the application of discount rates to estimated future cash flows based upon market yields or by using other valuation methodologies. Considerable judgment is necessary to interpret market data and develop estimated fair value. Accordingly, fair values are not necessarily indicative of the amounts the Company could realize on disposition of the financial instruments. The use of different market assumptions and/or estimation methodologies may have a material effect on estimated fair value amounts.

Short-term instruments: The carrying amounts of cash and cash equivalents and restricted cash approximate fair value.

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Credit facility and Senior Notes: The Company's unsecured credit facility did not have interest rates which were materially different than current market conditions and therefore, the fair value approximated the carrying value. The fair value of the Company's Senior Notes was estimated using Level 2 "significant other observable inputs," primarily based on quoted market prices for the same or similar issuances. At September 30, 2016, the fair value of the Senior Notes was approximately \$304.9 million.

Other debt instruments: The fair value of the Company's other debt instruments (including capital leases and lease financing obligations) were estimated in the same manner as the unsecured credit facility above. Similarly, each of these instruments did not have interest rates which were materially different than current market conditions and therefore, the fair value of each instrument approximated the respective carrying values.

13. Subsequent Events

On October 5, 2016, the Company paid its regular quarterly cash dividend of \$0.36 per common share and per unit in the Operating Partnership to stockholders and unit holders of record as of the close of business on September 20, 2016.

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

The following discussion and analysis presents the financial condition and results of operations of QTS Realty Trust, Inc. ("QTS"), which includes the operations of QualityTech, LP (the "Operating Partnership"), for the three and nine months ended September 30, 2016 and 2015. You should read the following discussion and analysis in conjunction with QTS' and the Operating Partnership's accompanying consolidated financial statements and related notes contained elsewhere in this Form 10-Q. We believe it is important for investors to understand the few differences between the financial statements of QTS and the Operating Partnership. See "Explanatory Note" for an explanation of these few differences. Since the financial data presented in this Item 2 does not contain any differences between QTS and the Operating Partnership, all periods presented reflect the operating results of the Operating Partnership.

Forward-Looking Statements

Some of the statements contained in this Form 10-Q constitute forward-looking statements within the meaning of the federal securities laws. Forward-looking statements relate to expectations, beliefs, projections, future plans and strategies, anticipated events or trends and similar expressions concerning matters that are not historical facts. In particular, statements pertaining to our capital resources, portfolio performance and results of operations contain forward-looking statements. Likewise, all of our statements regarding anticipated growth in our funds from operations

and anticipated market conditions are forward-looking statements. In some cases, you can identify forward-looking statements by the use of forward-looking terminology such as “may,” “will,” “should,” “expects,” “intends,” “plans,” “anticipates,” “believes,” “estimates,” “predicts,” or “potential” or the negative of these words and phrases or similar words or phrases which are predictions of or indicate future events or trends and which do not relate solely to historical matters. You can also identify forward-looking statements by discussions of strategy, plans or intentions.

The forward-looking statements contained in this Form 10-Q reflect our current views about future events and are subject to numerous known and unknown risks, uncertainties, assumptions and changes in circumstances that may cause our actual results to differ significantly from those expressed in any forward-looking statement. We do not guarantee that the transactions and events described will happen as described (or that they will happen at all). The following factors, among others, could cause actual results and future events to differ materially from those set forth or contemplated in the forward-looking statements:

- * adverse economic or real estate developments in our markets or the technology industry;
- * global, national and local economic conditions;
- * risks related to our international operations;
- * difficulties in identifying properties to acquire and completing acquisitions;

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- * our failure to successfully develop, redevelop and operate acquired properties or lines of business, including data centers acquired in our acquisition of Carpathia Hosting, Inc.;
- * significant increases in construction and development costs;
- * the increasingly competitive environment in which we operate;
- * defaults on, or termination or non-renewal of, leases by customers;
- * increased interest rates and operating costs, including increased energy costs;
- * financing risks, including our failure to obtain necessary outside financing;
- * decreased rental rates or increased vacancy rates;
- * dependence on third parties to provide Internet, telecommunications and network connectivity to our data centers;
- * our failure to qualify and maintain QTS' qualification as a real estate investment trust ("REIT");
- * environmental uncertainties and risks related to natural disasters;
- * financial market fluctuations; and
- * changes in real estate and zoning laws, revaluations for tax purposes and increases in real property tax rates.

While forward-looking statements reflect our good faith beliefs, they are not guarantees of future performance. We disclaim any obligation to publicly update or revise any forward-looking statement to reflect changes in underlying assumptions or factors, of new information, data or methods, future events or other changes. For a further discussion of these and other factors that could cause our future results to differ materially from any forward-looking statements, see the section entitled "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2015 and Item 1A. "Risk Factors" of this Form 10-Q.

Overview

We are a leading provider of secure, compliant data center solutions, hybrid cloud and fully managed services. We refer to our spectrum of core data center products as our “3Cs,” which consist of Custom Data Center (“C1”), Colocation (“C2”) and Cloud and Managed Services (“C3”). Our 3C integrated technology platform provides flexible, scalable, secure IT solutions for web and IT applications. Our Critical Facilities Management (“CFM”) provides increased efficiency and greater performance for third-party data center owners and operators.

We operate a portfolio of 24 data centers located throughout the United States, Canada, Europe and Asia. Within the United States, we are located in some of the top U.S. data center markets plus other high-growth markets. Our data centers are highly specialized, full-service, mission-critical facilities used by our customers to house, power and cool the networking equipment and computer systems that support their most critical business processes. We believe that our data centers are best-in-class and engineered to adhere to the highest specifications commercially available to customers, providing fully redundant, high-density power and cooling sufficient to meet the needs of major national and international companies and organizations. This is in part reflected by our operating track record of “five-nines” (99.999%) reliability and by our diverse customer base of more than 1,000 customers, including financial institutions, healthcare companies, government agencies, communications service providers, software companies and global Internet companies.

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We account for the operations of all of our properties in one reporting segment.

As of September 30, 2016, QTS owned an approximate 87.6% ownership interest in the Operating Partnership. Substantially all of our assets are held by, and our operations are conducted through, the Operating Partnership.

The Operating Partnership is a Delaware limited partnership formed on August 5, 2009 and was QTS' historical predecessor prior to the initial public offering ("IPO"), having operated the Company's business until the IPO.

We believe that QTS has operated and has been organized in conformity with the requirements for qualification and taxation as a REIT commencing with our taxable year ended December 31, 2013. Our qualification as a REIT, and maintenance of such qualification, depends upon our ability to meet, on a continuing basis, various complex requirements under the Internal Revenue Code of 1986, as amended (the "Code") relating to, among other things, the sources of our gross income, the composition and values of our assets, our distributions to our stockholders and the concentration of ownership of our equity shares.

Our Customer Base

We provide data center solutions to a diverse set of customers. Our customer base is comprised of companies of all sizes representing an array of industries, each with unique and varied business models and needs. We serve Fortune 1000 companies as well as small and medium-sized businesses, or SMBs, including financial institutions, healthcare companies, government agencies, communications service providers, software companies and global Internet companies.

Our Custom Data Center, or C1, customers typically are large enterprises with significant IT expertise and specific IT requirements, including financial institutions, "Big Four" accounting firms and the world's largest global Internet companies. Our Colocation, or C2, customers consist of a wide range of organizations, including major healthcare, telecommunications and software and web-based companies. Our C3 Cloud customers include both large organizations and SMBs seeking to reduce their capital expenditures and outsource their IT infrastructure on a flexible basis. Examples of current C3 Cloud customers include a global financial processing company and various U.S. government agencies.

As a result of our diverse customer base, customer concentration in our portfolio is limited. As of September 30, 2016, only three of our more than 1,000 customers individually accounted for more than 3% of our monthly recurring

revenue (“MRR”) (as defined below), with the largest customer accounting for approximately 12.8% of our MRR and the next largest customer accounting for only 3.5% of our MRR. In addition, approximately 60% of our MRR was attributable to customers who use more than one of our 3C products.

Our Portfolio

We develop and operate 24 data centers located throughout the United States, Canada, Europe and Asia, containing an aggregate of approximately 5.3 million gross square feet of space (approximately 91% of which is wholly owned by us), including approximately 2.3 million “basis-of-design” raised floor square feet, which represents the total data center raised floor potential of our existing data center facilities. This represents the maximum amount of space in our existing buildings that could be leased following full build-out, depending on the configuration that we deploy. We build out our data center facilities for both general use (colocation) and for executed leases that require significant amounts of space and power, depending on the needs of each facility at that time. As of September 30, 2016, this space included approximately 1,297,000 raised floor operating net rentable square feet, or NRSF, plus approximately 1.0 million square feet of additional raised floor in our development pipeline, of which approximately 32,000 NRSF is expected to become operational by December 31, 2016. Of the total 1.0 million NRSF in our development pipeline, approximately 38,000 square feet was related to customer leases which had been executed but not yet commenced. Our facilities collectively have access to over 600 megawatts (“MW”) of gross utility power with 550 MW of available utility power. We believe such access to power gives us a competitive advantage in redeveloping data center space, since access to power is usually the most limiting and expensive component in data center redevelopment.

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The following table presents an overview of the portfolio of operating properties that we own or lease, based on information as of September 30, 2016:

Gross Square Feet (2)	Operating Net Rentable Square Feet (Operating NRSF) (3)			Total	% Occupied (7)	Annualized Rent (8)	Available Utility Power (MW) (9)	Basis of De ("BOD") N
	Raised Floor (4)	Office & Other (5)	Supporting Infrastructure (6)					
1,318,353	167,309	51,093	178,854	397,256	90.4 %	\$ 39,348,818	110	557,309
968,695	452,986	36,953	331,426	821,365	96.3 %	\$ 93,228,957	72	527,186
698,000	95,614	6,981	77,425	180,020	95.9 %	\$ 24,009,556	140	275,701
553,930	58,157	2,229	111,405	171,791	100.0%	\$ 9,829,070	22	158,157
369,822	185,422	8,697	107,128	301,247	81.9 %	\$ 57,128,648	36	208,008
317,000	14,000	-	18,579	32,579	1.3 %	\$ 146,327	8	133,000
135,322	55,905	944	45,094	101,943	78.4 %	\$ 22,605,220	11	80,940
122,448	31,503	14,208	41,901	87,612	88.8 %	\$ 12,120,955	7	52,744
92,644	54,595	2,794	23,916	81,305	47.0 %	\$ 12,278,400	8	57,906
360,000	88,820	14,311	91,851	194,982	76.2 %	\$ 9,772,733	111	176,000
30,029	19,887	-	6,592	26,479	66.3 %	\$ 5,105,508	4	19,887
166,478	70,450	5,418	32,992	108,860	84.2 %	\$ 70,891,274	20	94,175
117,406	2,493	49,337	23,482	75,312	60.4 %	\$ 871,845	1	2,493

5,250,127	1,297,141	192,965	1,090,645	2,580,751	88.6 %	\$ 357,337,311	550	2,343,506
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- (1) Represents the year a property was acquired or, in the case of a property under lease, the year our initial lease commenced for the property.
- (2) With respect to our owned properties, gross square feet represents the entire building area. With respect to leased properties, gross square feet represents that portion of the gross square feet subject to our lease. Gross square feet includes 292,086 square feet of our office and support space, which is not included in operating NRSF.
- (3) Represents the total square feet of a building that is currently leased or available for lease plus developed supporting infrastructure, based on engineering drawings and estimates, but does not include space held for redevelopment or space used for our own office space.
- (4) Represents management's estimate of the portion of NRSF of the facility with available power and cooling capacity that is currently leased or readily available to be leased to customers as data center space based on engineering drawings.
- (5) Represents the operating NRSF of the facility other than data center space (typically office and storage space) that is currently leased or available to be leased.
- (6) Represents required data center support space, including mechanical, telecommunications and utility rooms, as well as building common areas.
- (7) Calculated as data center raised floor that is subject to a signed lease for which space is occupied (904,808 square feet as of September 30, 2016) divided by leasable raised floor based on the current configuration of the properties (1,020,901 square feet as of September 30, 2016), expressed as a percentage.
- (8) We define annualized rent as MRR multiplied by 12. We calculate MRR as monthly contractual revenue under executed contracts as of a particular date, which includes revenue from our C1, C2 and C3 rental and cloud and managed services activities, but excludes customer recoveries, deferred set up fees, variable related revenues, non-cash revenues and other one-time revenues. MRR does not include the impact from booked-not-billed contracts as of a particular date, unless otherwise specifically noted. This amount reflects the annualized cash rental payments. It does not reflect the accounting associated with any free rent, rent abatements or future scheduled rent increases and also excludes operating expense and power reimbursements.
- (9) Represents installed utility power and transformation capacity that is available for use by the facility as of September 30, 2016.

* Represents facilities that we lease.

** Subject to long term ground lease

*** Includes 12 facilities. All facilities are leased, including those subject to capital leases.

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Key Operating Metrics

The following sets forth definitions for our key operating metrics. These metrics may differ from similar definitions used by other companies.

Monthly Recurring Revenue (“MRR”). We calculate MRR as monthly contractual revenue under signed leases as of a particular date, which includes revenue from our C1, C2 and C3 rental and cloud and managed services activities, but excludes customer recoveries, deferred set-up fees, variable related revenues, non-cash revenues and other one-time revenues. MRR does not include the impact from booked-not-billed leases as of a particular date, unless otherwise specifically noted.

Annualized Rent. We define annualized rent as MRR multiplied by 12.

Rental Churn. We define rental churn as MRR lost to a customer intending to fully exit the platform compared to total MRR at the beginning of the period.

Leasable Raised Floor. We define leasable raised floor as the amount of raised floor square footage that we have leased plus the available capacity of raised floor square footage that is in a leasable format as of a particular date and according to a particular product configuration. The amount of our leasable raised floor may change even without completion of new redevelopment projects due to changes in our configuration of C1, C2 and C3 product space.

Percentage (%) Occupied. We define percentage occupied as the square footage that is subject to a signed lease for which space is occupied as of a particular date compared to leasable raised floor as of that date, expressed as a percentage.

Booked-not-Billed. We define booked-not-billed as our customer leases that have been signed, but for which lease payments have not yet commenced.

Factors That May Influence Future Results of Operations and Cash Flows

Revenue. Our revenue growth will depend on our ability to maintain the historical occupancy rates of leasable raised floor, lease currently available space, lease new capacity that becomes available as a result of our development and redevelopment activities, attract new customers and continue to meet the ongoing technological requirements of our customers. As of September 30, 2016, we had in place customer leases generating revenue for approximately 89% of our leasable raised floor. Our ability to grow revenue also will be affected by our ability to maintain or increase rental, cloud and managed services rates at our properties. Future economic downturns, regional downturns or downturns in the technology industry could impair our ability to attract new customers or renew existing customers' leases on favorable terms, or at all, and could adversely affect our customers' ability to meet their obligations to us. Negative trends in one or more of these factors could adversely affect our revenue in future periods, which would impact our results of operations and cash flows. We also at times may elect to reclaim space from customers in a negotiated transaction where we believe that we can redevelop and/or re-lease that space at higher rates, which may cause a decrease in revenue until the space is re-leased.

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Leasing Arrangements. As of September 30, 2016, 33% of our MRR came from customers which individually occupied greater than or equal to 6,600 square feet of space (or approximately 1 MW of power). As of September 30, 2016, approximately 40% of our MRR was attributable to the metered power model. Under the metered power model, the customer pays us a fixed monthly rent amount, plus reimbursement of certain other operating costs, including actual costs of sub-metered electricity used to power its data center equipment and an estimate of costs for electricity used to power supporting infrastructure for the data center, expressed as a factor of the customer's actual electricity usage. Fluctuations in our customers' utilization of power and the supplier pricing of power do not significantly impact our results of operations or cash flows under the metered power model. These leases generally have a minimum term of five years. As of September 30, 2016, 67% of our MRR was leased to customers which individually occupied less than 6,600 square feet of space. As of September 30, 2016, approximately 60% of our MRR was attributable to the gross lease model. Under a gross lease, the customer pays us a fixed rent on a monthly basis, and does not separately reimburse us for operating costs, including utilities, maintenance, repair, property taxes and insurance, as reimbursement for these costs is factored into MRR. However, if customers access more utility costs than their leases permit, we are able to charge these customers for overages. For leases under the gross lease model, fluctuations in our customers' utilization of power and the prices our utility providers charge us will impact our results of operations and cash flows. Our leases on a gross lease basis generally have a term of three years or less.

Scheduled Lease Expirations. Our ability to minimize rental churn and customer downgrades at renewal and renew, lease and re-lease expiring space will impact our results of operations and cash flows. Leases which have commenced billing representing approximately 4% and 17% of our total leased raised floor are scheduled to expire during the years ending December 31, 2016 (including all month-to-month leases) and 2017, respectively. These leases also represented approximately 10% and 30%, respectively, of our annualized rent as of September 30, 2016. At expiration, as a general matter, based on current market conditions, we expect that expiring rents will be at or below the then-current market rents.

Acquisitions, Redevelopment and Financing. Our revenue growth also will depend on our ability to acquire and redevelop and subsequently lease data center space at favorable rates. We generally fund the cost of data center acquisition and redevelopment from our net cash provided by operations, revolving credit facility, other unsecured and secured borrowings or the issuance of additional equity. We believe that we have sufficient access to capital from our current cash and cash equivalents, and borrowings under our credit facility to fund our redevelopment projects.

Operating Expenses. Our operating expenses generally consist of direct personnel costs, utilities, property and ad valorem taxes, insurance and site maintenance costs and rental expenses on our ground and building leases. In particular, our buildings require significant power to support the data center operations conducted in them. Although substantially all of our long-term leases—leases with a term greater than three years—contain reimbursements for certain operating expenses, we will not in all instances be reimbursed for all of the property operating expenses we incur. We also incur general and administrative expenses, including expenses relating to senior management, our in-house sales and marketing organization, cloud and managed services support personnel and legal, human resources, accounting and other expenses related to professional services. We also incur additional expenses arising from being a publicly traded company, including employee equity-based compensation. Increases or decreases in our operating expenses will impact our results of operations and cash flows. We expect to incur additional operating expenses as we continue to expand.

General Leasing Activity

During the three and nine months ended September 30, 2016, we entered into customer leases representing approximately \$1.2 million and \$3.0 million of incremental MRR, net of downgrades (and representing approximately \$14.5 million and \$36.4 million of incremental annualized rent, net of downgrades) at \$714 and \$583 per square foot, respectively. In addition, \$4.3 million and \$11.7 million of leasing commissions was associated with new and renewal leasing activity for the three and nine months ended September 30, 2016.

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During the three and nine months ended September 30, 2016, we renewed leases with a total annualized rent of \$10.7 million and \$33.7 million at an average rent per square foot of \$1,204 and \$956, respectively, which was 0.8% higher and 1.1% lower than the annualized rent prior to their respective renewals. Customers that renew with adjustments to square feet are reflected in the net leasing activity discussed above. The rental churn rate for the three and nine months ended September 30, 2016 was 1.1% and 4.8%, respectively.

During the three and nine months ended September 30, 2016, we commenced customer leases representing approximately \$2.5 million and \$8.0 million of MRR (and representing approximately \$29.8 million and \$95.9 million of annualized rent) at \$746 and \$669 per square foot, respectively.

As of September 30, 2016, our booked-not-billed MRR balance (which represents customer leases that have been executed, but for which lease payments have not commenced as of September 30, 2016) was approximately \$4.2 million, or \$50.8 million of annualized rent. The booked-not-billed balance is expected to contribute an incremental \$2.5 million to revenue in 2016 (representing \$14.1 million in annualized revenues), an incremental \$12.1 million in 2017 (representing \$20.3 million in annualized revenues) and an incremental \$16.5 million in annualized revenues thereafter. Offsetting these amounts is expected annualized churn of approximately 5% to 8% of annualized MRR in 2017, inclusive of an expected tenant departure in a leased facility in Northern Virginia with annualized MRR of approximately \$9.4 million. This revenue loss is expected to occur early in the first quarter of 2017 upon maturity of the tenant's lease. We are actively looking to release the facility which will have approximately two years of lease term remaining following the customer departure, plus an option to extend the term beyond the base agreement. We will continue to evaluate all options with regard to this facility.

We estimate the remaining capital cost to provide the space, power, connectivity and other services to the customer contracts which had been booked but not billed as of September 30, 2016 to be approximately \$35 million. This estimate generally includes C1 customers with newly contracted space of more than 3,300 square feet. The space, power, connectivity and other services provided to customers that contract for smaller amounts of space is generally provided by existing space which was previously developed.

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Results of Operations

Three Months Ended September 30, 2016 Compared to Three Months Ended September 30, 2015

Changes in revenues and expenses for the three months ended September 30, 2016 compared to the three months ended September 30, 2015 are summarized below (unaudited and in thousands):

	Three Months Ended September 30,			
	2016	2015	\$ Change	% Change
Revenues:				
Rental	\$ 77,005	\$ 62,744	\$ 14,261	23%
Recoveries from customers	8,703	6,158	2,545	41%
Cloud and managed services	16,243	18,573	(2,330)	-13%
Other	1,514	1,415	99	7%
Total revenues	103,465	88,890	14,575	16%
Operating expenses:				
Property operating costs	36,288	30,925	5,363	17%
Real estate taxes and insurance	2,566	1,462	1,104	76%
Depreciation and amortization	32,699	24,486	8,213	34%
General and administrative	19,942	19,440	502	3%
Transaction and integration costs	3,465	1,482	1,983	134%
Total operating expenses	94,960	77,795	17,165	22%
Operating income	8,505	11,095	(2,590)	-23%
Other income and expense:				
Interest income	1	1	—	0%
Interest expense	(6,179)	(5,418)	761	14%
Other expense, net	1	—	1	*
Income before taxes	2,328	5,678	(3,350)	-59%
Tax benefit of taxable REIT subsidiaries	4,210	2,560	1,650	64%
Net income	\$ 6,538	\$ 8,238	\$ (1,700)	-21%

* not applicable for comparison

Revenues. Total revenues for the three months ended September 30, 2016 were \$103.5 million compared to \$88.9 million for the three months ended September 30, 2015. The increase of \$14.6 million, or 16%, was largely attributable to the acquisition of the Piscataway facility on June 6, 2016, which contributed \$5.3 million in incremental revenue for the three months ended September 30, 2016 as well as organic growth in our customer base and placing additional square footage into service in conjunction with the development and expansion of our Dallas-Fort Worth, Richmond and Atlanta-Metro data centers.

The increase of \$11.9 million, or 15%, in combined rental and cloud and managed services revenue was largely attributable to the acquisition of the Piscataway facility on June 6, 2016, which contributed \$3.0 million in incremental revenue as well as newly leased space from ongoing expansions in our Atlanta-Metro, Dallas-Fort Worth and Richmond data centers, and increases in rents from previously leased space, net of downgrades at renewal and rental churn.

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As of September 30, 2016, our data centers were approximately 89% occupied based on leasable raised floor of approximately 1,021,000 square feet, with approximately 905,000 square feet occupied, with an average annualized rent of \$397 per leased raised floor square foot including cloud and managed services revenue, or \$328 per leased raised floor square foot excluding cloud and managed services revenue. As of September 30, 2016, the average annualized rent for our C1 product, including managed services for our C1 product, was \$197 per leased raised floor square foot, and the average annualized rent for our C2 product, including Cloud and managed services combined was \$1,267 per leased raised floor square foot. As of September 30, 2015, our data centers were 87% occupied and billing based on leasable raised floor of approximately 844,000 square feet, with approximately 736,000 square feet occupied and paying rent, with an average annualized rent of \$427 per leased raised floor square foot including cloud and managed services revenue, or \$328 per leased raised floor square foot excluding cloud and managed services revenue. The increase in leasable raised floor between 2015 and 2016 is primarily related to the addition of raised floor square footage from our redevelopment activities primarily in the Dallas-Fort Worth, Atlanta-Metro, and Richmond facilities, as well as the acquisition of the Piscataway facility. The decrease in average annualized rent per leased raised floor square foot is primarily due to an increase in mix of C1 customers in our portfolio. As of September 30, 2016, a larger portion of our customers were C1 customers (40% of MRR) compared to September 30, 2015 (33% of MRR). This increase in the proportion of C1 customers has contributed to the reduction in average annualized rent per square foot due to the fact that C1 customers lease larger amounts of space and power for longer periods and lower rates due to economies of scale in addition to reimbursing us for utilities and various other operating expenses, and that reimbursement is excluded from the calculation of annualized rent per square foot.

Higher recoveries from customers for the three months ended September 30, 2016 compared to the three months ended September 30, 2015 were primarily due to reimbursements associated with the acquisition of the Piscataway facility which contributed \$2.2 million to the increase. The remaining \$0.3 million increase was attributable to various other facilities. The \$0.1 million increase in other revenue for the three months ended September 30, 2016 compared to the three months ended September 30, 2015 was primarily due to less customer discounts issued during the period as well as higher straight line rent, offset by a lower level of scrap metal sales.

Property Operating Costs. Property operating costs for the three months ended September 30, 2016 were \$36.3 million compared to property operating costs of \$30.9 million for the three months ended September 30, 2015, an increase of \$5.4 million, or 17%. The breakdown of our property operating costs is summarized in the table below (unaudited and in thousands):

	Three Months Ended		\$	% Change
	2016	2015		
Property operating costs:				
Direct payroll	\$ 5,395	\$ 4,689	\$ 706	15%
Rent	4,105	4,932	(827)	-17%
Repairs and maintenance	3,308	2,442	866	35%
Utilities	11,640	9,630	2,010	21%
Management fee allocation	5,215	4,866	349	7%

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Other	6,625	4,366	2,259	52%
Total property operating costs	\$ 36,288	\$ 30,925	\$ 5,363	17%

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The acquisition of Piscataway contributed \$2.6 million to the total increase in property operating costs for the three months ended September 30, 2016, of which \$0.2 million related to direct payroll, \$0.2 million related to repairs and maintenance, \$1.3 million related to utilities, \$0.2 million related to management fee allocation and \$0.7 million related to other property operating costs, which included \$0.6 million related to temporary and security personnel. The remaining \$2.8 million increase in total property operating costs was primarily attributable to the revenue growth and expansion of our existing facilities, which included increased direct payroll allocation of \$0.5 million (exclusive of the increase attributable to Piscataway as discussed above), increased repair and maintenance expense of \$0.6 million which tends to fluctuate from period to period and increase with the expansion and lease-up of our facilities, increased utilities expense of \$0.7 million, increased management fee of \$0.1 million and an increase in other expenses of \$1.6 million, offset by a \$0.8 million decrease in rent expense primarily related to the exit of portions of leased facilities as customers migrated to owned facilities. Management fee allocation for our leased facilities acquired in 2015 is based on 10% of cash rental revenues for each facility and reflects an allocation of internal charges to cover back-office and service-related costs associated with the day-to-day operations of our data center facilities, with a corresponding offset to general and administrative expenses. Management fee allocation for our other facilities is based on 4% of cash rental revenues for each facility. The \$1.6 million increase in other expenses was primarily attributable to an increase in connectivity expenses and higher software license costs.

Real Estate Taxes and Insurance. Real estate taxes and insurance for the three months ended September 30, 2016 were \$2.6 million compared to \$1.5 million for the three months ended September 30, 2015. The increase of \$1.1 million, or 76%, was primarily attributable to property taxes associated with our acquisition of the Piscataway facility as well as property taxes at our leased facilities acquired in June 2015.

Depreciation and Amortization. Depreciation and amortization for the three months ended September 30, 2016 was \$32.7 million compared to \$24.5 million for the three months ended September 30, 2015. The increase of \$8.2 million, or 34%, was primarily due to additional depreciation of \$5.8 million, which was primarily due to additional depreciation of the Dallas-Fort Worth, Richmond and Atlanta-Metro data centers and a higher level of software depreciation, as well as higher amortization expense of \$2.4 million primarily related to increased amortization expense of acquired intangible assets associated with the Piscataway acquisition.

General and Administrative Expenses. General and administrative expenses were \$19.9 million for the three months ended September 30, 2016 compared to general and administrative expenses of \$19.4 million for the three months ended September 30, 2015, an increase of \$0.5 million, or 3%. The increase in general and administrative expenses was primarily attributable to increased payroll expenses related to sales and marketing personnel of \$0.6 million, higher equity-based compensation expense of \$0.6 million, higher payroll costs, net of sales and marketing personnel, of \$3.9 million and higher software license costs of \$0.7 million. These increases were partially offset by increased direct payroll allocation of \$4.6 million, increased management fee allocation of \$0.3 million, decreased outside services expense of \$0.2 million primarily related to consulting fees and a reduction in other expenses of \$0.2 million.

Transaction and Integration Costs. For the three months ended September 30, 2016, we incurred \$3.5 million in transaction and integration costs compared to \$1.5 million for the three months ended September 30, 2015. In the current period, \$3.4 million in costs were attributable to integration expenses primarily related to systems integration

and duplicate personnel, with the remaining \$0.1 million related to transaction costs incurred in the acquisition of the Piscataway facility. In the prior period, \$0.1 million in costs were attributable to expenses related to the examination of actual and potential acquisitions, with the remaining \$1.4 million related to integration costs related to the Carpathia acquisition. Acquisition-related costs for acquisitions accounted for as a business combination in accordance with ASC 805, Business Combinations, are expensed in the periods in which the costs are incurred and the services are received.

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Interest Expense. Interest expense was \$6.2 million and \$5.4 million for the three months ended September 30, 2016 and 2015. The increase of \$0.8 million, or 14%, was due primarily to an increase in the average debt balance of \$63.3 million, primarily as a result of our ongoing developments, expansions and acquisitions, partially offset by issuance of additional common shares and a decrease in the weighted average interest rate on our borrowings. The average debt balance, exclusive of debt issuance costs, for the three months ended September 30, 2016 was \$869.0 million, with a weighted average interest rate, including the effect of amortization of deferred financing costs, of 3.98%. This compared to an average debt balance, exclusive of debt issuance costs, of \$805.7 million for the three months ended September 30, 2015, with a weighted average interest rate, including the effect of interest rate swaps and amortization of deferred financing costs, of 4.04%. Interest capitalized in connection with our redevelopment activities during the three months ended September 30, 2016 and 2015 was \$2.5 million and \$2.7 million, respectively.

Tax Benefit of Taxable REIT Subsidiaries. The tax benefit of taxable REIT subsidiaries for the three months ended September 30, 2016 was \$4.2 million compared to \$2.6 million for the three months ended September 30, 2015. The current period tax benefit primarily related to recorded operating losses resulting from both current losses and prior period tax provision adjustments as well as certain transaction and integration costs. The prior period tax benefit primarily related to recorded operating losses which included certain transaction and integration costs. To the extent that the Company's taxable REIT subsidiaries continue to generate operating losses, a tax benefit will generally continue to be recognized due to the existing net deferred tax liability.

Net Income. A summary of the components of the decrease in net income of \$1.7 million for the three months ended September 30, 2016 as compared to the three months ended September 30, 2015 is as follows (unaudited and in millions):

	\$ Change
Increase in revenues, net of property operating costs, real estate taxes and insurance	\$ 8.1
Increase in general and administrative expense	(0.5)
Increase in depreciation and amortization	(8.2)
Increase in transaction and integration costs	(2.0)
Increase in interest expense net of interest income	(0.8)
Increase in tax benefit	1.7
Decrease in net income	\$ (1.7)

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Nine Months Ended September 30, 2016 Compared to Nine Months Ended September 30, 2015

Changes in revenues and expenses for the nine months ended September 30, 2016 compared to the nine months ended September 30, 2015 are summarized below (unaudited and in thousands):

	Nine Months Ended September 30,		\$ Change	% Change
	2016	2015		
Revenues:				
Rental	\$ 217,101	\$ 164,270	\$ 52,831	32%
Recoveries from customers	20,306	17,404	2,902	17%
Cloud and managed services	52,148	32,588	19,560	60%
Other	7,365	4,131	3,234	78%
Total revenues	296,920	218,393	78,527	36%
Operating expenses:				
Property operating costs	100,715	72,292	28,423	39%
Real estate taxes and insurance	6,326	4,421	1,905	43%
Depreciation and amortization	91,693	58,791	32,902	56%
General and administrative	61,836	47,893	13,943	29%
Transaction and integration costs	9,385	6,256	3,129	50%
Total operating expenses	269,955	189,653	80,302	42%
Operating income	26,965	28,740	(1,775)	-6%
Other income and expense:				
Interest income	3	2	1	50%
Interest expense	(17,034)	(15,559)	1,475	9%
Other expense, net	1	(83)	84	*
Income before taxes	9,935	13,100	(3,165)	-24%
Tax benefit of taxable REIT subsidiaries	9,269	5,695	3,574	63%
Net income	\$ 19,204	\$ 18,795	\$ 409	2%

* not applicable for comparison

Revenues. Total revenues for the nine months ended September 30, 2016 were \$296.9 million compared to \$218.4 million for the nine months ended September 30, 2015. The increase of \$78.5 million, or 36%, was primarily due to the current period including a full nine months of Carpathia's results compared to just over one quarter of results in the prior period, which contributed \$36.5 million to the increase, as well as organic growth in our customer base and placing additional square footage into service in conjunction with the development and expansion of our Dallas-Fort Worth, Richmond and Atlanta-Metro data centers. In addition, the acquisition of the Piscataway facility contributed \$6.9 million in incremental revenue for the nine months ended September 30, 2016.

The increase of \$72.4 million, or 37%, in combined rental and cloud and managed services revenue was primarily due to the current period including a full nine months of Carpathia's results compared to just over one quarter of results in the prior period, which contributed \$36.0 million to the increase, as well as the acquisition of the Piscataway facility which contributed \$3.8 million in incremental revenue for the nine months ended September 30, 2016. Additional increases, aggregating \$32.6 million, are attributable to newly leased space primarily from ongoing expansions in our Atlanta-Metro, Dallas-Fort Worth and Richmond data centers and increases in rents from previously leased space, net of downgrades at renewal and rental churn.

Higher recoveries from customers for the nine months ended September 30, 2016 compared to the nine months ended September 30, 2015 were primarily due to reimbursements associated with the acquisition of the Piscataway facility which contributed \$2.9 million to the increase. The \$3.2 million increase in other revenue for the nine months ended September 30, 2016 compared to the nine months ended September 30, 2015 was primarily due to higher straight line rent resulting from leasing activity associated with the ongoing expansion of facilities discussed above.

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Property Operating Costs. Property operating costs for the nine months ended September 30, 2016 were \$100.7 million compared to property operating costs of \$72.3 million for the nine months ended September 30, 2015, an increase of \$28.4 million, or 39%. The breakdown of our property operating costs is summarized in the table below (unaudited and in thousands):

	Nine Months Ended		\$ Change	% Change
	2016	2015		
Property operating costs:				
Direct payroll	\$ 15,320	\$ 12,212	\$ 3,108	25%
Rent	13,681	7,983	5,698	71%
Repairs and maintenance	9,662	6,578	3,084	47%
Utilities	28,516	25,223	3,293	13%
Management fee allocation	15,331	9,973	5,358	54%
Other	18,204	10,323	7,881	76%
Total property operating costs	\$ 100,715	\$ 72,292	\$ 28,423	39%

The acquisition of Carpathia contributed \$18.7 million to the total increase in property operating costs for the nine months ended September 30, 2016, of which \$0.9 million related to direct payroll, \$5.6 million related to rent expense, \$2.2 million related to repairs and maintenance, \$1.5 million related to utilities, \$3.8 million related to management fee allocation and \$4.7 million related to other property operating costs, which included \$3.6 million related to communication services. Management fee allocation for our leased facilities acquired in 2015 is based on 10% of cash rental revenues for each facility and reflects an allocation of internal charges to cover back-office and service-related costs associated with the day-to-day operations of our data center facilities, with a corresponding offset to general and administrative expenses. The remaining \$9.7 million increase in total property operating costs was primarily attributable to the revenue growth and expansion of our existing facilities, which included increased direct payroll allocation of \$2.2 million, increased rent expense of \$0.1 million, increased repair and maintenance expense of \$0.9 million which tends to fluctuate from period to period and increase with the expansion and lease-up of our facilities, increased utility expense of \$1.9 million primarily related to the newly acquired Piscataway facility and an increase in other expenses of \$3.0 million. The \$3.0 million increase in other expenses was primarily attributable to an increase in temporary and security personnel, increased software license costs and increased connectivity expenses. In addition, management fee allocation increased \$1.6 million (exclusive of the increase attributable to our leased facilities acquired in 2015 as discussed above). Management fee allocation for our other facilities is based on 4% of cash rental revenues for each facility.

Real Estate Taxes and Insurance. Real estate taxes and insurance for the nine months ended September 30, 2016 were \$6.3 million compared to \$4.4 million for the nine months ended September 30, 2015. The increase of \$1.9 million, or 43%, was primarily attributable to the acquisition of the Piscataway facility which contributed \$0.9 million as well as \$0.6 million related to our leased facilities acquired in 2015. The remaining \$0.4 million increase was attributable to various other locations.

Depreciation and Amortization. Depreciation and amortization for the nine months ended September 30, 2016 was \$91.7 million compared to \$58.8 million for the nine months ended September 30, 2015. The increase of \$32.9 million, or 56%, was primarily due to depreciation expense of \$9.7 million and amortization expense of \$6.7 million associated with the Carpathia acquisition. The remaining increase of \$16.5 million was due to additional depreciation of \$12.6 million, primarily due to additional depreciation of the Dallas-Fort Worth data center, as well as expansion of the Richmond and Atlanta-Metro data centers, and higher amortization expense of \$3.9 million primarily related to a higher level of leasing commissions.

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General and Administrative Expenses. General and administrative expenses were \$61.8 million for the nine months ended September 30, 2016 compared to general and administrative expenses of \$47.9 million for the nine months ended September 30, 2015, an increase of \$13.9 million, or 29%. The increase in general and administrative expenses was primarily related to the Carpathia acquisition and, to a lesser extent, the ongoing growth of the Company. Inclusive of expenses associated with the acquisition of Carpathia, the increase in general and administrative expenses was primarily attributable to increased advertising and marketing expenses of \$0.2 million, increased payroll expenses related to sales and marketing personnel of \$1.5 million, higher equity-based compensation expense of \$2.7 million, higher payroll costs, net of sales and marketing personnel, of \$6.0 million, higher software license costs of \$1.4 million, higher temporary personnel and consulting fees of \$1.0 million, increased travel expenses of \$0.7 million and a \$1.3 million increase in other expenses, offset by receipt of litigation settlement proceeds of \$0.9 million. The \$1.3 million increase in other expenses was primarily related to increased rent expense, increased repairs and maintenance expense, increased telephone and internet expense and higher dues and subscriptions.

Transaction and Integration Costs. For the nine months ended September 30, 2016, we incurred \$9.4 million in transaction and integration costs compared to \$6.3 million for the nine months ended September 30, 2015. In the current period, \$8.4 million in costs were attributable to integration expenses primarily related to systems integration and duplicate personnel, with the remaining \$1.0 million primarily related to transaction costs incurred in the acquisition of the Piscataway facility. In the prior period, \$4.5 million of expenses were incurred primarily related to the examination and acquisition of Carpathia, with the remaining \$1.8 million related to integration costs related to the Carpathia acquisition. Acquisition-related costs for acquisitions accounted for as a business combination in accordance with ASC 805, Business Combinations, are expensed in the periods in which the costs are incurred and the services are received.

Interest Expense. Interest expense for the nine months ended September 30, 2016 was \$17.0 million compared to \$15.6 million for the nine months ended September 30, 2015. The increase of \$1.5 million, or 9%, was due primarily to an increase in the average debt balance of \$162.1 million, primarily as a result of our ongoing developments, expansions and acquisitions, partially offset by issuance of additional common shares, a decrease in the weighted average interest rate on our borrowings and higher capitalized interest during the current period due to the growth in construction projects. The average debt balance, exclusive of debt issuance costs, for the nine months ended September 30, 2016 was \$850.5 million, with a weighted average interest rate, including the effect of amortization of deferred financing costs, of 3.99%. This compared to an average debt balance of \$688.5 million for the nine months ended September 30, 2015, with a weighted average interest rate, including the effect of interest rate swaps and amortization of deferred financing costs, of 4.39%. Interest capitalized in connection with our redevelopment activities during the nine months ended September 30, 2016 and 2015 was \$8.4 million and \$7.1 million, respectively.

Tax Benefit of Taxable REIT Subsidiaries. Tax benefit of taxable REIT subsidiaries for the nine months ended September 30, 2016 was \$9.3 million compared to \$5.7 million for the nine months ended September 30, 2015. The current period tax benefit primarily related to recorded operating losses resulting from both current period operating losses and prior period tax provision adjustments. The prior period tax benefit primarily related to recorded operating losses, including transaction and integration costs, as well as the reversal of valuation allowances which were related to deferred tax assets. These deferred tax assets were generally created by net operating losses of the taxable REIT subsidiary, and previously had valuation allowances applied to them in their entirety as there were continuing losses for that entity. With the acquisition of Carpathia, deferred tax liabilities were created, which in turn caused the

Company to release the previously recorded valuation allowances during the second quarter of 2015. To the extent that the Company's taxable REIT subsidiaries continue to generate operating losses, a tax benefit will generally continue to be recognized due to the existing net deferred tax liability.

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Net Income. A summary of the components of the increase in net income of \$0.4 million for the nine months ended September 30, 2016 as compared to the nine months ended September 30, 2015 is as follows (unaudited and in millions):

	\$ Change
Increase in revenues, net of property operating costs, real estate taxes and insurance	\$ 48.2
Increase in general and administrative expense	(13.9)
Increase in depreciation and amortization	(32.9)
Increase in transaction and integration costs	(3.1)
Increase in interest expense net of interest income	(1.5)
Increase in tax benefit	3.6
Increase in net income	\$ 0.4

Non-GAAP Financial Measures

We consider the following non-GAAP financial measures to be useful to investors as key supplemental measures of our performance: (1) FFO; (2) Operating FFO; (3) Adjusted Operating FFO; (4) MRR; (5) NOI; (6) EBITDA; and (7) Adjusted EBITDA. These non-GAAP financial measures should be considered along with, but not as alternatives to, net income or loss and cash flows from operating activities as a measure of our operating performance. FFO, Operating FFO, Adjusted Operating FFO, MRR, NOI, EBITDA and Adjusted EBITDA, as calculated by us, may not be comparable to FFO, Operating FFO, Adjusted Operating FFO, MRR, NOI, EBITDA and Adjusted EBITDA as reported by other companies that do not use the same definition or implementation guidelines or interpret the standards differently from us.

FFO, Operating FFO and Adjusted Operating FFO

We consider funds from operations (“FFO”) to be a supplemental measure of our performance which should be considered along with, but not as an alternative to, net income (loss) and cash provided by operating activities as a measure of operating performance. We calculate FFO 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 GAAP), adjusted to exclude gains (or losses) from sales of property, real estate-related depreciation and amortization and similar adjustments for unconsolidated partnerships and joint ventures. Our management uses FFO as a supplemental performance measure because, in excluding real estate-related depreciation and amortization and gains and losses from property dispositions, it provides a performance measure that, when compared year over year, captures trends in occupancy rates, rental rates and operating costs.

Due to the volatility and nature of certain significant charges and gains recorded in our operating results that management believes are not reflective of our core operating performance, management computes an adjusted measure of FFO, which we refer to as Operating FFO. We generally calculate Operating FFO as FFO excluding certain non-routine charges and gains and losses that management believes are not indicative of the results of our operating real estate portfolio. We believe that Operating FFO provides investors with another financial measure that may facilitate comparisons of operating performance between periods and, to the extent they calculate Operating FFO on a comparable basis, between REITs.

Adjusted Operating Funds From Operations (“Adjusted Operating FFO”) is a non-GAAP measure that is used as a supplemental operating measure and to provide additional information to users of the financial statements. We calculate Adjusted Operating FFO by adding or subtracting from Operating FFO items such as: maintenance capital investment, paid leasing commissions, amortization of deferred financing costs and bond discount, non-real estate depreciation, straight line rent adjustments, taxes and non-cash compensation.

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We offer these measures because we recognize that FFO, Operating FFO and Adjusted Operating FFO will be used by investors as a basis to compare our operating performance with that of other REITs. However, because FFO, Operating FFO and Adjusted Operating FFO exclude real estate depreciation and amortization and capture neither the changes in the value of our properties that result from use or market conditions, nor the level of capital expenditures and capitalized leasing commissions necessary to maintain the operating performance of our properties, all of which have real economic effect and could materially impact our financial condition, cash flows and results of operations, the utility of FFO, Operating FFO and Adjusted Operating FFO as measures of our operating performance is limited. Our calculation of FFO may not be comparable to measures calculated by other companies who do not use the NAREIT definition of FFO or do not calculate FFO in accordance with NAREIT guidance. In addition, our calculations of FFO, Operating FFO and Adjusted Operating FFO are not necessarily comparable to FFO, Operating FFO and Adjusted Operating FFO as calculated by other REITs that do not use the same definition or implementation guidelines or interpret the standards differently from us. FFO, Operating FFO and Adjusted Operating FFO are non-GAAP measures and should not be considered a measure of our results of operations or liquidity or as a substitute for, or an alternative to, net income (loss), cash provided by operating activities or any other performance measure determined in accordance with GAAP, nor is it indicative of funds available to fund our cash needs, including our ability to make distributions to our stockholders.

A reconciliation of net income to FFO, Operating FFO and Adjusted Operating FFO is presented below:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
FFO				
Net income	\$ 6,538	\$ 8,238	\$ 19,204	\$ 18,795
Real estate depreciation and amortization	28,493	21,022	79,771	51,649
FFO	35,031	29,260	98,975	70,444
Operating FFO				
Write off of unamortized deferred finance costs	—	—	—	83
Integration costs	3,355	1,360	8,434	1,783
Transaction costs	110	122	951	4,473
Deferred tax benefit associated with transaction and integration costs	(1,136)	(1,206)	(3,067)	(1,206)
Non-cash reversal of deferred tax asset valuation allowance	—	—	—	(3,175)
Operating FFO	37,360	29,536	105,293	72,402
Maintenance Capex	(1,731)	(1,408)	(2,446)	(2,034)
Leasing commissions paid	(4,402)	(3,005)	(13,597)	(9,871)
Amortization of deferred financing costs and bond discount	879	849	2,633	2,552
Non real estate depreciation and amortization	4,207	3,463	11,923	7,086
Straight line rent revenue and expense and other	(957)	(479)	(5,810)	(2,004)
Deferred tax benefit from operating results	(3,075)	(1,354)	(6,203)	(1,354)
Equity-based compensation expense	2,637	2,068	7,887	5,206
Adjusted Operating FFO	\$ 34,918	\$ 29,670	\$ 99,680	\$ 71,983

Monthly Recurring Revenue (MRR) and Recognized MRR

We calculate MRR as monthly contractual revenue under signed leases as of a particular date, which includes revenue from our C1, C2 and C3 rental and cloud and managed services activities, but excludes customer recoveries, deferred set-up fees, variable related revenues, non-cash revenues and other one-time revenues. MRR does not include the impact from booked-not-billed leases as of a particular date, unless otherwise specifically noted.

Separately, we calculate recognized MRR as the recurring revenue recognized during a given period, which includes revenue from our C1, C2 and C3 rental and cloud and managed services activities, but excludes customer recoveries, deferred set-up fees, variable related revenues, non-cash revenues and other one-time revenues.

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Management uses MRR and recognized MRR as supplemental performance measures because they provide useful measures of increases in contractual revenue from our customer leases. MRR and recognized MRR should not be viewed by investors as alternatives to actual monthly revenue, as determined in accordance with GAAP. Other companies may not calculate MRR or recognized MRR in the same manner. Accordingly, our MRR and recognized MRR may not be comparable to other companies' MRR and recognized MRR. MRR and recognized MRR should be considered only as supplements to total revenues as a measure of our performance. MRR and recognized MRR should not be used as measures of our results of operations or liquidity, nor is it indicative of funds available to meet our cash needs, including our ability to make distributions to our stockholders.

A reconciliation of total revenues to recognized MRR in the period and MRR at period end is presented below:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Recognized MRR				
Total period revenues (GAAP basis)	\$ 103,465	\$ 88,890	\$ 296,920	\$ 218,393
Less: Total period recoveries	(8,703)	(6,158)	(20,306)	(17,404)
Total period deferred setup fees	(2,377)	(1,477)	(6,536)	(4,135)
Total period straight line rent and other	(3,697)	(2,959)	(13,722)	(8,221)
Recognized MRR (in the period)	\$ 88,688	\$ 78,296	\$ 256,356	\$ 188,633
MRR				
Total period revenues (GAAP basis)	\$ 103,465	\$ 88,890	\$ 296,920	\$ 218,393
Less: Total revenues excluding last month	(69,427)	(59,455)	(262,882)	(188,958)
Total revenues for last month of period	34,038	29,435	34,038	29,435
Less: Last month recoveries	(2,398)	(1,661)	(2,398)	(1,661)
Last month deferred setup fees	(828)	(269)	(828)	(269)
Last month straight line rent and other	(1,034)	(1,291)	(1,034)	(1,291)
MRR (at period end) *	\$ 29,778	\$ 26,214	\$ 29,778	\$ 26,214

*Does not include our booked-not-billed MRR balance, which was \$4.2 million and \$5.1 million as of September 30, 2016 and 2015, respectively.

Net Operating Income (NOI)

We calculate net operating income ("NOI"), as net income (loss), excluding: interest expense, interest income, tax expense (benefit) of taxable REIT subsidiaries, depreciation and amortization, write off of unamortized deferred financing costs, gain (loss) on extinguishment of debt, transaction and integration costs, gain (loss) on sale of real estate, restructuring costs and general and administrative expenses. We allocate a management fee charge of 4% of cash revenues for all facilities, with the exception of the leased facilities acquired in 2015 which are allocated a charge

of 10% of cash revenues, as a property operating cost and a corresponding reduction to general and administrative expense to cover the day-to-day administrative costs to operate our data centers. The management fee charge is reflected as a reduction to net operating income.

Management uses NOI as a supplemental performance measure because it provides a useful measure of the operating results from our customer leases. In addition, we believe it is useful to investors in evaluating and comparing the operating performance of our properties and to compute the fair value of our properties. Our NOI may not be comparable to other REITs' NOI as other REITs may not calculate NOI in the same manner. NOI should be considered only as a supplement to net income as a measure of our performance and should not be used as a measure of our results of operations or liquidity or as an indication of funds available to meet our cash needs, including our ability to make distributions to our stockholders. NOI is a measure of the operating performance of our properties and not of our performance as a whole. NOI is therefore not a substitute for net income as computed in accordance with GAAP.

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A reconciliation of net income to NOI is presented below:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2016	2015	2016	2015
Net Operating Income (NOI)				
Net income	\$ 6,538	\$ 8,238	\$ 19,204	\$ 18,795
Interest expense	6,179	5,418	17,034	15,559
Interest income	(1)	(1)	(3)	(2)
Depreciation and amortization	32,699	24,486	91,693	58,791
Write off of unamortized deferred finance costs	—	—	—	83
Tax benefit of taxable REIT subsidiaries	(4,210)	(2,560)	(9,269)	(5,695)
Integration costs	3,355	1,360	8,434	1,783
Transaction costs	110	122	951	4,473
General and administrative expenses	19,942	19,440	61,836	47,893
NOI (1)	\$ 64,612	\$ 56,503	\$ 189,880	\$ 141,680
Breakdown of NOI by facility:				
Atlanta-Metro data center	\$ 20,030	\$ 17,964	\$ 60,887	\$ 51,605
Atlanta-Suwanee data center	11,051	10,376	33,823	30,600
Santa Clara data center	2,961	3,615	10,378	10,566
Richmond data center	7,850	5,340	22,428	14,528
Sacramento data center	1,780	1,870	5,842	5,641
Princeton data center	2,468	2,331	7,180	6,990
Dallas-Fort Worth data center	5,118	1,532	11,656	3,743
Leased data centers acquired in 2015	10,487	12,460	31,937	14,710
Piscataway	2,086	—	2,756	—
Other data centers	781	1,015	2,993	3,297
NOI (1)	\$ 64,612	\$ 56,503	\$ 189,880	\$ 141,680

(1) Includes facility level general and administrative expense allocation charges of 4% of cash revenue for all facilities, with the exception of the leased facilities acquired in 2015, which include general and administrative expense allocation charges of 10% of cash revenue. These allocated charges aggregated to \$5.2 million and \$4.9 million for the three month periods ended September 30, 2016 and 2015, respectively, and \$15.3 million and \$10.0 million for the nine month periods ended September 30, 2016 and 2015, respectively.

Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA) and Adjusted EBITDA

We calculate EBITDA as net income (loss) adjusted to exclude interest expense and interest income, provision (benefit) for income taxes (including income taxes applicable to sale of assets) and depreciation and amortization. Management believes that EBITDA is useful to investors in evaluating and facilitating comparisons of our operating performance between periods and between REITs by removing the impact of our capital structure (primarily interest expense) and asset base charges (primarily depreciation and amortization) from our operating results.

In addition to EBITDA, we calculate an adjusted measure of EBITDA, which we refer to as Adjusted EBITDA, as EBITDA excluding write off of unamortized deferred financing costs, gains (losses) on extinguishment of debt, transaction and integration costs, equity-based compensation expense, restructuring costs and gain (loss) on sale of real estate. We believe that Adjusted EBITDA provides investors with another financial measure that can facilitate comparisons of operating performance between periods and between REITs.

Management uses EBITDA and Adjusted EBITDA as supplemental performance measures as they provide useful measures of assessing our operating results. Other companies may not calculate EBITDA or Adjusted EBITDA in the same manner. Accordingly, our EBITDA and Adjusted EBITDA may not be comparable to others. EBITDA and Adjusted EBITDA should be considered only as supplements to net income (loss) as measures of our performance and should not be used as substitutes for net income (loss), as measures of our results of operations or liquidity or as indications of funds available to meet our cash needs, including our ability to make distributions to our stockholders.

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A reconciliation of net income to EBITDA and Adjusted EBITDA is presented below:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
EBITDA and Adjusted EBITDA				
Net income	\$ 6,538	\$ 8,238	\$ 19,204	\$ 18,795
Interest expense	6,179	5,418	17,034	15,559
Interest income	(1)	(1)	(3)	(2)
Tax benefit of taxable REIT subsidiaries	(4,210)	(2,560)	(9,269)	(5,695)
Depreciation and amortization	32,699	24,486	91,693	58,791
EBITDA	41,205	35,581	118,659	87,448
Write off of unamortized deferred finance costs	—	—	—	83
Equity-based compensation expense	2,637	2,068	7,887	5,206
Integration costs	3,355	1,360	8,434	1,783
Transaction costs	110	122	951	4,473
Adjusted EBITDA	\$ 47,307	\$ 39,131	\$ 135,931	\$ 98,993

Liquidity and Capital Resources

Short-Term Liquidity

Our short-term liquidity needs include funding capital expenditures for the redevelopment of data center space (a significant portion of which is discretionary), meeting debt service and debt maturity obligations, including interest payments on our 5.875% Senior Notes due 2022 (“Senior Notes”), funding payments for capital lease and lease financing obligations, funding distributions to our stockholders and unit holders, utility costs, site maintenance costs, real estate and personal property taxes, insurance, rental expenses, general and administrative expenses and certain recurring and non-recurring capital expenditures.

In addition to the \$197.8 million of capital expenditures, excluding acquisitions, incurred in the nine months ended September 30, 2016, we expect that we will incur approximately \$85 million in additional capital expenditures through December 31, 2016 in connection with the redevelopment of our data center facilities. We expect to spend approximately \$75 million of capital expenditures with vendors on redevelopment, and the remainder on other capital expenditures and capitalized overhead costs (including capitalized interest, commissions, payroll and other similar costs), personal property and other less material capital projects. We expect to fund these costs using operating cash flows and draws on our credit facility. A significant portion of these expenditures are discretionary in nature and we may ultimately determine not to make these expenditures or the timing of such expenditures may vary.

We expect to meet our short-term liquidity needs through operating cash flow, cash and cash equivalents and borrowings under our credit facility.

Our cash paid for capital expenditures, excluding acquisitions, for the nine months ended September 30, 2016 and 2015 are summarized in the table below (in thousands):

	Nine Months Ended	
	September 30,	
	2016	2015
Redevelopment	\$ 140,517	\$ 213,248
Personal property	18,665	9,240
Maintenance capital expenditures	2,446	2,034
Capitalized interest, commissions and other overhead costs	36,123	27,634
Total capital expenditures	\$ 197,751	\$ 252,156

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Long-Term Liquidity

Our long-term liquidity needs primarily consist of funds for property acquisitions, scheduled debt maturities, payment of principal at maturity of our Senior Notes, funding payments for capital lease and lease financing obligations, and recurring and non-recurring capital expenditures. We may also pursue additional redevelopment of our Atlanta-Metro, Dallas-Fort Worth, Richmond, Piscataway and Chicago data centers and future redevelopment of other space in our portfolio. We may also pursue development on land which QTS currently owns that is adjacent to our data center properties in Atlanta-Metro, Suwanee, Richmond, Dallas, and Chicago. The development and/or redevelopment of this space, including timing, is at our discretion and will depend on a number of factors, including availability of capital and our estimate of the demand for data center space in the applicable market. We expect to meet our long-term liquidity needs with net cash provided by operations, incurrence of additional long-term indebtedness, borrowings under our credit facility and issuance of additional equity or debt securities, subject to prevailing market conditions, as discussed below.

In March 2016, QTS filed an automatic shelf registration statement on Form S-3 with the SEC. Effective upon filing, the shelf provides for the potential sale of an unspecified amount of our Class A common stock, preferred stock, depositary shares representing preferred stock, warrants and rights to purchase our common stock or any combination thereof, subject to the ability of QTS to effect offerings on satisfactory terms based on prevailing conditions. The shelf registration statement is intended to allow us to have the flexibility to raise such funds in one or more offerings should we perceive market conditions to be favorable. Pursuant to this shelf registration, on April 1, 2016, we issued 6,325,000 shares of QTS' Class A common stock at a price of \$45.50 per share in an underwritten public offering, including the exercise in full of the underwriter's option to purchase an additional 825,000 shares. We used substantially all of the net proceeds of approximately \$276 million to repay amounts outstanding under our unsecured revolving credit facility.

Cash

As of September 30, 2016, we had \$11.8 million of unrestricted cash and cash equivalents.

The following tables present quarterly cash dividends and distributions paid to QTS' common stockholders and the Operating Partnership's unit holders for the nine months ended September 30, 2016 and 2015:

Nine Months Ended September 30, 2016

Record Date	Payment Date	Per Common Share and Per Unit Rate	Aggregate Dividend/Distribution Amount (in millions)
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June 17, 2016	July 6, 2016	\$	0.36	\$	19.7
March 18, 2016	April 5, 2016		0.36		17.4
December 17, 2015	January 6, 2016		0.32		15.4
				\$	52.5

Nine Months Ended September 30, 2015

Record Date	Payment Date	Per Common Share and Per Unit Rate		Aggregate Dividend/Distribution Amount (in millions)
June 19, 2015	July 8, 2015	\$	0.32	\$ 15.3
March 20, 2015	April 7, 2015		0.32	13.4
December 19, 2014	January 7, 2015		0.29	10.7
				\$ 39.4

Additionally, on October 5, 2016 we paid our regular quarterly cash dividend of \$0.36 per common share and per unit in the Operating Partnership to stockholders and unit holders of record as of the close of business on September 20, 2016.

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Indebtedness

As of September 30, 2016, we had approximately \$873.8 million of indebtedness, including capital leases and lease financing obligations, and excluding discounts and debt issuance costs.

Unsecured Credit Facility. In October 2015, we amended and restated our unsecured credit facility, increasing the total capacity by \$250 million and extending the term. At the same time, we terminated our secured credit facility relating to the Richmond data center. The amended unsecured credit facility has a total capacity of \$900 million and includes a \$150 million term loan which matures on December 17, 2020, another \$150 million term loan which matures on April 27, 2021, and a \$600 million revolving credit facility which matures on December 17, 2019, with a one year extension option. Amounts outstanding under the amended unsecured credit facility bear interest at a variable rate equal to, at our election, LIBOR or a base rate, plus a spread that will vary depending upon our leverage ratio. For revolving credit loans, the spread ranges from 1.55% to 2.15% for LIBOR loans and 0.55% to 1.15% for base rate loans. For term loans, the spread ranges from 1.50% to 2.10% for LIBOR loans and 0.50% to 1.10% for base rate loans. The amended unsecured credit facility also includes a \$200 million accordion feature.

Under the amended unsecured credit facility, the capacity may be increased from the current capacity of \$900 million to \$1.1 billion subject to certain conditions set forth in the credit agreement, including the consent of the administrative agent and obtaining necessary commitments. As of September 30, 2016, the weighted average interest rate for amounts outstanding under our unsecured credit facility was 2.04%. We are also required to pay a commitment fee to the lenders assessed on the unused portion of the unsecured revolving credit facility. At our election, we can prepay amounts outstanding under the unsecured credit facility, in whole or in part, without penalty or premium.

Our ability to borrow under the amended unsecured credit facility is subject to ongoing compliance with a number of customary affirmative and negative covenants, including limitations on liens, mergers, consolidations, investments, distributions, asset sales and affiliate transactions, as well as the following financial covenants: (i) the outstanding principal balance of the loans and letter of credit liabilities cannot exceed the unencumbered asset pool availability (as defined in the third amended and restated credit agreement), (ii) a maximum leverage ratio of total indebtedness to gross asset value (as defined in the third amended and restated credit agreement) not in excess of 60%, (iii) a minimum fixed charge coverage ratio (defined as the ratio of consolidated EBITDA, subject to certain adjustments, to consolidated fixed charges) for the prior two most recently-ended calendar quarters of not less than 1.70 to 1.00, (iv) tangible net worth of at least \$958 million plus 80% of the sum of net equity offering proceeds and the value of interests in the Operating Partnership issued upon contribution of assets to the Operating Partnership or its subsidiaries, (v) unhedged variable rate debt not greater than 35% of gross asset value and (vi) a maximum distribution payout ratio of the greater of (a) 95% of our “funds from operations” (as defined in the agreement) and (b) the amount required for QTS to qualify as a REIT under the Code. The interest rate applied to the outstanding balance of the unsecured credit facility decreases incrementally for every 5% below the maximum leverage ratio.

The availability under the amended unsecured revolving credit facility is the lesser of (i) \$600 million, (ii) 60% of unencumbered asset pool capitalized value, or (iii) the amount resulting in an unencumbered asset pool debt yield of 14%. In the case of clauses (ii), (iii) and (iv) of the preceding sentence, the amount available under the unsecured revolving credit facility is adjusted to take into account any other unsecured debt and certain capitalized leases. The availability of funds under our unsecured credit facility depends on compliance with our covenants. As of September 30, 2016, we had outstanding \$532.0 million of indebtedness under the amended unsecured credit facility, consisting of \$232.0 million of outstanding borrowings under our unsecured revolving credit facility and \$300.0 million outstanding under the term loans, exclusive of net debt issuance costs of \$2.6 million. In connection with the unsecured credit facility, as of September 30, 2016, we had an additional \$2.0 million letter of credit outstanding. In addition, we entered into two additional letters of credit in June 2016 related to our Chicago facility and newly acquired Piscataway facility in the amounts of \$0.5 million and \$0.1 million, respectively.

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5.875% Senior Notes due 2022. On July 23, 2014, the Operating Partnership and QTS Finance Corporation, a subsidiary of the operating partnership formed solely for the purpose of facilitating the offering of the Senior Notes described below (collectively, the “Issuers”), issued \$300 million aggregate principal amount of 5.875% Senior Notes due 2022. The Senior Notes have an interest rate of 5.875% per annum and were issued at a price equal to 99.211% of their face value. The proceeds from the offering were used to repay amounts outstanding under the unsecured credit facility, including \$75 million outstanding under the term loan. As of September 30, 2016, the discount recorded on the Senior Notes was \$1.8 million and the outstanding net debt issuance costs associated with the Senior Notes were \$6.3 million.

The Senior Notes are unconditionally guaranteed, jointly and severally, on a senior unsecured basis by all of the Operating Partnership’s existing subsidiaries (other than foreign subsidiaries, receivables entities and 2470 Satellite Boulevard, LLC, which is a Delaware limited liability company formed in December 2015 that acquired an office building in Duluth, Georgia and has de minimis operations) and future subsidiaries that guarantee any indebtedness of QTS, the Issuers or any other subsidiary guarantor. QTS Realty Trust, Inc. does not guarantee the Senior Notes and will not be required to guarantee the Senior Notes except under certain circumstances. The offering was conducted pursuant to Rule 144A of the Securities Act of 1933, as amended, and the Senior Notes were issued pursuant to an indenture, dated as of July 23, 2014, among QTS, the Operating Partnership, QTS Finance Corporation, the guarantors named therein, and Deutsche Bank Trust Company Americas, as trustee (the “Indenture”).

On March 23, 2015, the SEC declared effective the Operating Partnership and QTS Finance Corporation’s registration statement on Form S-4 pursuant to which the Issuers exchanged the originally issued Senior Notes for \$300 million of 5.875% Senior Notes due 2022 (the “Exchange Notes”) that are registered under the Securities Act of 1933, as amended. The exchange offer was completed on April 23, 2015, and all outstanding originally issued Senior Notes were tendered. The Exchange Notes did not provide the Company with any additional proceeds and satisfied its obligations under a registration rights agreement entered into in connection with the issuance of the Senior Notes.

The Indenture contains affirmative and negative covenants that, among other things, limit or restrict the Operating Partnership’s ability and the ability of certain of its subsidiaries (“Restricted Subsidiaries”) to: incur additional indebtedness; pay dividends; make certain investments or other restricted payments; enter into transactions with affiliates; enter into agreements limiting the ability of the operating partnership’s restricted subsidiaries to pay dividends; engage in sales of assets; and engage in mergers, consolidations or sales of substantially all of their assets. However, certain of these covenants will be suspended if and for so long as the Senior Notes are rated investment grade by specified debt rating services and there is no default under the Indenture. The Operating Partnership and its Restricted Subsidiaries also are required to maintain total unencumbered assets (as defined in the Indenture) of at least 150% of their unsecured debt on a consolidated basis.

The Senior Notes may be redeemed by the Issuers, in whole or in part, at any time prior to August 1, 2017 at a redemption price equal to (i) 100% of principal amount, plus (ii) accrued and unpaid interest to the redemption date, and (iii) a make-whole premium. Thereafter, the Issuers may redeem the Senior Notes prior to maturity at 104.406% of the principal amount at August 1, 2017 and declining ratably to par at August 1, 2020 and thereafter, in each case plus accrued and unpaid interest to the redemption date. At any time prior to August 1, 2017, the Issuers may, subject

to certain conditions, redeem up to 35% of the aggregate principal amount of the Senior Notes at 105.875% of the principal amount thereof, plus accrued and unpaid interest to the redemption date, with the net cash proceeds of certain equity offerings consummated by us or the Operating Partnership. Also, upon the occurrence of a change of control of us or the Operating Partnership, holders of the Senior Notes may require the Issuers to repurchase all or a portion of the Senior Notes at a price equal to 101% of the principal amount of the Senior Notes to be repurchased plus accrued and unpaid interest to the repurchase date.

Contingencies

We are subject to various routine legal proceedings and other matters in the ordinary course of business. While resolution of these matters cannot be predicted with certainty, management believes, based upon information currently available, that the final outcome of these proceedings will not have a material adverse effect on our financial condition, liquidity or results of operations.

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Contractual Obligations

The following table summarizes our contractual obligations as of September 30, 2016, including the future non-cancellable minimum rental payments required under operating leases and the maturities and scheduled principal repayments of indebtedness and other agreements (in thousands):

Obligations	2016	2017	2018	2019	2020	Thereafter	Total
Operating Leases	\$ 8,626	\$ 14,268	\$ 11,681	\$ 9,894	\$ 9,633	\$ 82,175	\$ 136,277
Capital Leases and Lease Financing Obligations	3,117	12,944	9,370	2,844	2,190	11,360	41,825
Future Principal Payments of Indebtedness (1)	—	—	—	232,000	150,000	450,000	832,000
Total (2)	\$ 11,743	\$ 27,212	\$ 21,051	\$ 244,738	\$ 161,823	\$ 543,535	\$ 1,010,102

(1) Does not include the related debt issuance costs and discount on Senior Notes nor the related debt issuance costs on the term loans reflected at September 30, 2016. Also does not include letters of credit of \$2.0 million, \$0.5 million and \$0.1 million outstanding as of September 30, 2016 under our unsecured credit facility.

(2) Total obligations does not include contractual interest that we are required to pay on our long-term debt obligations. Contractual interest payments on our credit facility, Senior Notes, capital leases, lease financing obligations and other financing arrangements through the scheduled maturity date, assuming no prepayment of debt, are shown below. Interest payments were estimated based on the principal amount of debt outstanding and the applicable interest rate as of September 30, 2016 (in thousands):

2016	2017	2018	2019	2020	Thereafter	Total
\$ 7,712	\$ 30,627	\$ 30,332	\$ 29,809	\$ 21,800	\$ 29,780	\$ 150,060

Cash Flows

(in thousands)	Nine Months Ended September 30,	
	2016	2015
Cash flow provided by (used for):		
Operating activities	\$ 103,495	\$ 72,319
Investing activities	(320,732)	(541,021)
Financing activities	220,202	468,644

Nine Months Ended September 30, 2016 Compared to Nine Months Ended September 30, 2015

Cash flow provided by operating activities was \$103.5 million for the nine months ended September 30, 2016 compared to \$72.3 million for the nine months ended September 30, 2015. There was an increase in cash operating income of \$31.8 million from the prior period related to our expansion, leasing activity, acquisitions, and equity issuances as discussed below, as well as an increase in cash flow associated with net changes in working capital of \$0.6 million primarily related to changes in accounts payable, accrued expenses and rents and other receivables.

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Cash flow used for investing activities decreased by \$220.3 million to \$320.7 million for the nine months ended September 30, 2016, compared to \$541.0 million for the nine months ended September 30, 2015. The decrease was due primarily to a decrease in cash paid for acquisitions of \$165.9 million. The cash paid for the acquisition of Carpathia in the prior period was \$288.9 million compared to the acquisition of the Piscataway facility in the current period of \$123.0 million. In addition, there was a decrease in cash paid for capital expenditures of \$54.4 million, primarily related to redevelopment of our Dallas-Fort Worth, Atlanta-Metro, Chicago and Richmond data centers. These expenditures include capitalized soft costs such as interest, payroll and other costs to redevelop properties, which were, in the aggregate, \$17.6 million and \$15.7 million for the nine months ended September 30, 2016 and 2015 respectively.

Cash flow provided by financing activities was \$220.2 million for the nine months ended September 30, 2016, compared to \$468.6 million for the nine months ended September 30, 2015. The decrease was primarily due to lower proceeds of \$153.2 million under our unsecured credit facility due to less proceeds being needed for capital expenditures, higher payments of cash dividends to common stockholders of \$12.6 million which was due to the increase in shares outstanding primarily related to the March 2015, June 2015 and April 2016 equity issuances, and a decrease in net equity proceeds of \$93.8 million. Partially offsetting these decreases in cash provided by financing activities was a decrease in mortgage principal debt repayments of \$16.6 million due to the repayment of our Atlanta-Metro equipment loan in June 2015.

Critical Accounting Policies

The Company applies those accounting policies that management believes best reflect the underlying business and economic events, consistent with accounting principles generally accepted in the United States. Inherent in such policies are certain key assumptions and estimates made by management. Management periodically updates its estimates used in the preparation of the consolidated financial statements based on its latest assessment of the current and projected business and general economic environment. Information regarding the Company's Critical Accounting Policies and Estimates is included in Item 7 of the Company's Annual Report on Form 10-K for the year ended December 31, 2015.

Inflation

Substantially all of our long-term leases—leases with a term greater than three years—contain rent increases and reimbursement for certain operating costs. As a result, we believe that we are largely insulated from the effects of inflation over periods greater than three years. Leases with terms of three years or less will be replaced or renegotiated within three years and should adjust to reflect changed conditions, also mitigating the effects of inflation. Moreover, to the extent that there are material increases in utility costs, we generally reserve the right to renegotiate the rental rate to incorporate significant utility rate increases. However, any increases in the costs of redevelopment of our properties will generally result in a higher cost of the property, which will result in increased cash requirements to redevelop our properties and increased depreciation and amortization expense in future periods, and, in some

circumstances, we may not be able to directly pass along the increase in these redevelopment costs to our customers in the form of higher rental rates.

Distribution Policy

To satisfy the requirements to qualify as a REIT, and to avoid paying tax on our income, QTS intends to continue to make regular quarterly distributions of all, or substantially all, of its REIT taxable income (excluding net capital gains) to its stockholders.

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All distributions will be made at the discretion of our board of directors and will depend on our historical and projected results of operations, liquidity and financial condition, QTS' REIT qualification, our debt service requirements, operating expenses and capital expenditures, prohibitions and other restrictions under financing arrangements and applicable law and other factors as our board of directors may deem relevant from time to time. We anticipate that our estimated cash available for distribution will exceed the annual distribution requirements applicable to REITs and the amount necessary to avoid the payment of tax on undistributed income. However, under some circumstances, we may be required to make distributions in excess of cash available for distribution in order to meet these distribution requirements and we may need to borrow funds to make certain distributions. If we borrow to fund distributions, our future interest costs would increase, thereby reducing our earnings and cash available for distribution from what they otherwise would have been.

The Operating Partnership also includes certain partners that are subject to a taxable income allocation, however, not entitled to receive recurring distributions. The partnership agreement does stipulate however, to the extent that taxable income is allocated to these partners that the partnership will make a distribution to these partners equal to the lesser of the actual per unit distributions made to Class A partners or an estimated amount to cover federal, state and local taxes on the allocated taxable income. No distributions related to allocated taxable income were made to these partners for the nine months ended September 30, 2016 and 2015.

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

Our future income, cash flows and fair values relevant to financial instruments are dependent upon prevailing market interest rates. Market risk refers to the risk of loss from adverse changes in market prices and interest rates. The primary market risk to which we believe we are exposed is interest rate risk. Many factors, including governmental monetary and tax policies, domestic and international economic and political considerations and other factors that are beyond our control, contribute to interest rate risk.

As of September 30, 2016, we had outstanding \$532.0 million of consolidated indebtedness that bore interest at variable rates.

We monitor our market risk exposures using a sensitivity analysis. Our sensitivity analysis estimates the exposure to market risk sensitive instruments assuming a hypothetical 1% change in year-end interest rates. A 1% increase in interest rates would increase the interest expense on the \$532 million of variable indebtedness outstanding as of September 30, 2016 by approximately \$5.3 million annually. Conversely, a decrease in the LIBOR rate to 0% would decrease the interest expense on this \$532.0 million of variable indebtedness outstanding by approximately \$2.8 million annually based on the one month LIBOR rate of approximately 0.5% as of September 30, 2016.

The above analyses do not consider the effect of any change in overall economic activity that could impact interest rates or expected changes associated with future indebtedness. 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, these analyses assume no changes in our financial structure.

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ITEM 4. Controls and Procedures

QTS Realty Trust, Inc.

Disclosure Controls and Procedures

Based on an evaluation of disclosure controls and procedures for the period ended September 30, 2016, conducted by the Company's management, with the participation of the Chief Executive Officer and Chief Financial Officer, the Chief Executive Officer and Chief Financial Officer concluded that QTS' disclosure controls and procedures are effective to ensure that information required to be disclosed by QTS in reports that it files or submits under the Securities Exchange Act of 1934 is accumulated and communicated to the Company's management (including the Chief Executive Officer and Chief Financial Officer) to allow timely decisions regarding required disclosure, and is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms.

Changes in Internal Control over Financial Reporting

There were no changes in QTS' internal control over financial reporting during the period ended September 30, 2016, that have materially affected, or are reasonably likely to materially affect, QTS' internal control over financial reporting.

QualityTech LP

Disclosure Controls and Procedures

Based on an evaluation of disclosure controls and procedures for the period ended September 30, 2016, conducted by the Company's management, with the participation of the Chief Executive Officer and Chief Financial Officer, the Chief Executive Officer and Chief Financial Officer concluded that the Operating Partnership's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Operating Partnership in reports that it files or submits under the Securities Exchange Act of 1934 is accumulated and communicated to the Company's management (including the Chief Executive Officer and Chief Financial Officer) to allow timely decisions regarding required disclosure, and is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms.

Changes in Internal Control over Financial Reporting

There were no changes in the Operating Partnership's internal control over financial reporting during the period ended September 30, 2016, that have materially affected, or are reasonably likely to materially affect, the Operating Partnership's internal control over financial reporting.

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PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

In the ordinary course of our business, we are subject to claims and administrative proceedings, none of which we believe are material or would be expected to have, individually or in the aggregate, a material adverse effect on us.

ITEM 1A. Risk Factors

There have been no material changes to the risk factors disclosed in our Form 10-K for the year ended December 31, 2015, filed with the Securities and Exchange Commission (“SEC”) on February 29, 2016, which are accessible on the SEC’s website at www.sec.gov.

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

Unregistered Sales of Equity Securities

QTS did not sell any securities during the nine months ended September 30, 2016 that were not registered under the Securities Act of 1933, as amended (the “Securities Act”).

QTS from time to time issues shares of Class A common stock pursuant to the QTS Realty Trust, Inc. 2013 Equity Incentive Plan (the “2013 Equity Incentive Plan”) upon exercise of stock options issued under the 2013 Equity Incentive Plan, and upon redemption of Class A units of limited partnership of the Operating Partnership (either through Class A units previously held or those received from conversion of Class O units or Class RS LTIP units from the QualityTech, LP 2010 Equity Incentive Plan). Pursuant to the partnership agreement of the Operating Partnership, each time QTS issues shares of common stock, the Operating Partnership issues to QTS, its general partner, an equal number of Class A units. The units issued to QTS are not registered under the Securities Act in reliance on Section 4(a)(2) of the Securities Act due to the fact that Class A units were issued only to QTS and therefore, did not involve a public offering. During the nine months ended September 30, 2016, the Operating Partnership issued

approximately 131,000 Class A units to QTS in connection with Class A unit redemptions and stock option exercises and issuances pursuant to the 2013 Equity Incentive Plan, with a value of approximately \$6.9 million based on the respective dates of the redemptions and option exercises, as applicable. In addition, during the nine months ended September 30, 2016, the Operating Partnership issued approximately 6.3 million Class A units to QTS in connection with the underwritten public offering in April 2016 with a value of approximately \$287.8 million.

Repurchases of Equity Securities

During the three months ended September 30, 2016, certain of our employees surrendered Class A common stock owned by them to satisfy their statutory minimum federal and state tax obligations in connection with the vesting of restricted common stock under the 2013 Equity Incentive Plan.

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The following table summarizes all of these repurchases during the three months ended September 30, 2016:

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 of shares that may yet be purchased under the plans or programs
July 1, 2016 through July 31, 2016	—	N/A	N/A	N/A
August 1, 2016 through August 31, 2016	1,198	(1) \$ 40.19	N/A	N/A
September 1, 2016 through September 30, 2016	7,571	(1) \$ 29.25	N/A	N/A
Total	8,769	(1) \$ 30.74		

(1) The number of shares purchased represents shares of Class A common stock surrendered by certain of our employees to satisfy their statutory minimum federal and state tax obligations associated with the vesting of restricted common stock. With respect to these shares, the price paid per share is based on the closing price of our Class A common stock as of the date of the determination of the statutory minimum federal income tax.

ITEM 3. Defaults Upon Senior Securities

None.

ITEM 4. Mine Safety Disclosures

Not applicable.

ITEM 5. Other Information

None.

ITEM 6. Exhibits

Exhibit Number	Exhibit Description
2.1	Stock Purchase Agreement, dated May 6, 2015, by and among Quality Technology Services Holding, LLC, Carpathia Holdings, LLC and Carpathia Acquisition, Inc. (Filed as Exhibit 2.1 to the Current Report on Form 8-K filed with the SEC on May 12, 2015)
2.2	First Amendment to Stock Purchase Agreement, effective as of June 12, 2015, by and among Quality Technology Services Holding, LLC, Carpathia Holdings, LLC and Carpathia Acquisition, Inc. (Filed as Exhibit 2.1 to the Current Report on Form 8-K filed with the SEC on June 19, 2015)
3.1	Articles of Amendment and Restatement of QTS Realty Trust, Inc. (Filed as Exhibit 3.1 to the Current Report on Form 8-K filed with the SEC on October 17, 2013)
3.2	Amended and Restated Bylaws of QTS Realty Trust, Inc. (Filed as Exhibit 3.2 to the Registration Statement on Form S-11/A filed with the SEC on September 26, 2013)
4.1	Form of Specimen Class A Common Stock Certificate (Filed as Exhibit 4.1 to the Registration Statement on Form S-11/A filed with the SEC on September 26, 2013)
4.2	Indenture, dated July 23, 2014, by and among QualityTech, LP, QTS Finance Corporation, QTS Realty Trust, Inc., certain subsidiaries of QualityTech, LP and Deutsche Bank Trust Company Americas (Filed as Exhibit 4.1 to the Current Report on Form 8-K filed with the SEC on July 25, 2014)

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- 4.3 Supplemental Indenture, dated as of December 22, 2014, by and among QualityTech, LP, QTS Finance Corporation, QTS Realty Trust, Inc., the entities identified therein as Guaranteeing Subsidiaries, the entities identified therein as Subsidiary Guarantors, and Deutsche Bank Trust Company Americas, to the Indenture dated, as of July 23, 2014, by and among QualityTech, LP, and QTS Finance Corporation, as issuers, QTS Realty Trust, Inc., each of the subsidiary guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee (Filed as Exhibit 4.3 to the Company's Annual Report on Form 10-K for the year ended December 31, 2014 filed with the SEC on February 23, 2015)
- 4.4 Supplemental Indenture, dated as of September 28, 2015, by and among QualityTech, LP, QTS Finance Corporation, QTS Realty Trust, Inc., the entities identified therein as Guaranteeing Subsidiaries, the entities identified therein as Subsidiary Guarantors, and Deutsche Bank Trust Company Americas, to the Indenture dated, as of July 23, 2014, by and among QualityTech, LP, and QTS Finance Corporation, as issuers, QTS Realty Trust, Inc., each of the subsidiary guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee (Filed as Exhibit 4.4 to the Company's Quarterly Report on Form 10-Q for the period ended September 30, 2015 filed with the SEC on November 6, 2015)
- 4.5 Supplemental Indenture, dated as of June 23, 2016, by and among QualityTech, LP, QTS Finance Corporation, QTS Realty Trust, Inc., the entities identified therein as Guaranteeing Subsidiaries, the entities identified therein as Subsidiary Guarantors, and Deutsche Bank Trust Company Americas, to the Indenture dated, as of July 23, 2014, by and among QualityTech, LP, and QTS Finance Corporation, as issuers, QTS Realty Trust, Inc., each of the subsidiary guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee (Filed as Exhibit 4.5 to the Company's Quarterly Report on Form 10-Q for the period ended June 30, 2016 filed with the SEC on August 5, 2016)
- 4.6 Form of 5.875% Senior Notes due 2022 (included in Exhibit 4.2 hereto)
- 10.1 Employment Agreement dated as of May 6, 2015 by and among QTS Realty Trust, Inc., QualityTech, LP, Quality Technology Services Holding, LLC, Quality Technology Services, LLC, and Jon Greaves
- 10.2 Amendment No. 1 to Employment Agreement dated as of March 21, 2016 by and among QTS Realty Trust, Inc., QualityTech, LP, Quality Technology Services Holding, LLC, Quality Technology Services, LLC, and Jon Greaves
- 10.3 Employment Agreement dated as of August 31, 2016 by and among QTS Realty Trust, Inc., QualityTech, LP, Quality Technology Services, LLC, and Steven Bloom
- 31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (QTS Realty Trust, Inc.)
- 31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (QTS Realty Trust, Inc.)
- 31.3 Certification of Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (QualityTech, LP)
- 31.4

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Certification of Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (QualityTech, LP)

- 32.1 Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (QTS Realty Trust, Inc.)
- 32.2 Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (QualityTech, LP)

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- 101 The following materials from QTS Realty Trust, Inc.'s and QualityTech, LP's Quarterly Report on Form 10-Q for the period ended September 30, 2016, formatted in XBRL (eXtensible Business Reporting Language):
- (i) condensed consolidated balance sheets, (ii) condensed consolidated statements of operations and comprehensive income (loss), (iii) condensed consolidated statements of equity and partners' capital, (iv) condensed consolidated statements of cash flow, and (v) the notes to the condensed consolidated financial statements

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SIGNATURES

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

QTS Realty Trust, Inc.

DATE: November 8, 2016 /s/ Chad L. Williams
Chad L. Williams
Chairman and Chief Executive Officer

DATE: November 8, 2016 /s/ William H. Schafer
William H. Schafer
Chief Financial Officer
(Principal Financial Officer and Principal Accounting Officer)

QualityTech, LP

By: QTS Realty Trust, Inc.,
its general partner

DATE: November 8, 2016 /s/ Chad L. Williams
Chad L. Williams
Chairman and Chief Executive Officer

DATE: November 8, 2016 /s/ William H. Schafer
William H. Schafer
Chief Financial Officer
(Principal Financial Officer and Principal Accounting Officer)