American Assets Trust, Inc.
Form 10-Q
May 04, 2018
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2018
or
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to

AMERICAN ASSETS TRUST, INC.
(Exact Name of Registrant as Specified in its Charter)
Commission file number: 001-35030

AMERICAN ASSETS TRUST, L.P.
(Exact Name of Registrant as Specified in its Charter)
Commission file number: 333-202342-01

Maryland (American Assets Trust, Inc.) Maryland (American Assets Trust, L.P.) (State or other jurisdiction of incorporation or organization)	27-3338708 (American Assets Trust, Inc.) 27-3338894 (American Assets Trust, L.P.) (IRS Employer Identification No.)
11455 El Camino Real, Suite 200, San Diego, California (Address of Principal Executive Offices)	92130 (Zip Code)

(858) 350-2600
(Registrant’s Telephone Number, Including Area Code)

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

American Assets Trust, Inc. x Yes o No
American Assets Trust, L.P. x Yes o No
(American Assets Trust, L.P. became subject to filing requirements under Section 13 of the Securities Exchange Act of 1934, as amended, upon effectiveness of its Registration Statement on Form S-3 on February 6, 2015 and has filed all required reports subsequent to that date.)
Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during

the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files).

American Assets Trust, Inc. x Yes o No
American Assets Trust, L.P. x Yes o No

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

American Assets Trust, Inc.

Large Accelerated Filer	x	Accelerated Filer	o
Non-Accelerated Filer	o (Do not check if a smaller reporting company)	Smaller reporting company	o
Emerging growth company	o		

American Assets Trust, L.P.

Large Accelerated Filer	o	Accelerated Filer	o
Non-Accelerated Filer	x (Do not check if a smaller reporting company)	Smaller reporting company	o
Emerging growth company	o		

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

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

American Assets Trust, Inc. o Yes x No
American Assets Trust, L.P. o Yes x No

American Assets Trust, Inc. had 47,203,484 shares of common stock, par value $0.01 per share, outstanding as of May 4, 2018.

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EXPLANATORY NOTE

This report combines the quarterly reports on Form 10-Q for the quarter ended March 31, 2018 of American Assets Trust, Inc., a Maryland corporation, and American Assets Trust, L.P., a Maryland limited partnership, of which American Assets Trust, Inc. is the parent company and sole general partner. Unless otherwise indicated or unless the context requires otherwise, all references in this report to “we,” “us,” “our” or “the company” refer to American Assets Trust, Inc. together with its consolidated subsidiaries, including American Assets Trust, L.P. Unless otherwise indicated or unless the context requires otherwise, all references in this report to “our Operating Partnership” or “the Operating Partnership” refer to American Assets Trust, L.P. together with its consolidated subsidiaries.

American Assets Trust, Inc. operates as a real estate investment trust, or REIT, and is the sole general partner of the Operating Partnership. As of March 31, 2018, American Assets Trust, Inc. owned an approximate 73.2% partnership interest in the Operating Partnership. The remaining 26.8% partnership interests are owned by non-affiliated investors and certain of our directors and executive officers. As the sole general partner of the Operating Partnership, American Assets Trust, Inc. has full, exclusive and complete authority and control over the Operating Partnership’s day-to-day management and business, can cause it to enter into certain major transactions, including acquisitions, dispositions and refinancings, and can cause changes in its line of business, capital structure and distribution policies.

The company believes that combining the quarterly reports on Form 10-Q of American Assets Trust, Inc. and the Operating Partnership into a single report will result in the following benefits:

- better reflects how management and the analyst community view the business as a single operating unit;
- enhance investors' understanding of American Assets Trust, Inc. and the Operating Partnership by enabling them to view the business as a whole and in the same manner as management;
- greater efficiency for American Assets Trust, Inc. and the Operating Partnership and resulting savings in time, effort and expense; and
- greater efficiency for investors by reducing duplicative disclosure by providing a single document for their review.

Management operates American Assets Trust, Inc. and the Operating Partnership as one enterprise. The management of American Assets Trust, Inc. and the Operating Partnership are the same.

There are a few differences between American Assets Trust, Inc. and the Operating Partnership, which are reflected in the disclosures in this report. We believe it is important to understand the differences between American Assets Trust, Inc. and the Operating Partnership in the context of how American Assets Trust, Inc. and the Operating Partnership operate as an interrelated consolidated company. American Assets Trust, Inc. is a REIT, whose only material asset is its ownership of partnership interests of the Operating Partnership. As a result, American Assets Trust, Inc. does not conduct business itself, other than acting as the sole general partner of the Operating Partnership, issuing public equity from time to time and guaranteeing certain debt of the Operating Partnership. American Assets Trust, Inc. itself does not hold any indebtedness. The Operating Partnership holds substantially all the assets of the company, directly or indirectly holds the ownership interests in the company’s real estate ventures, conducts the operations of the business and is structured as a partnership with no publicly-traded equity. Except for net proceeds from public equity issuances by American Assets Trust, Inc., which are generally contributed to the Operating Partnership in exchange for partnership units, the Operating Partnership generates the capital required by the company’s business through the Operating Partnership’s operations, by the Operating Partnership’s direct or indirect incurrence of indebtedness or through the issuance of operating partnership units.

Noncontrolling interests and stockholders’ equity and partners’ capital are the main areas of difference between the consolidated financial statements of American Assets Trust, Inc. and those of American Assets Trust, L.P. The partnership interests in the Operating Partnership that are not owned by American Assets Trust, Inc. are accounted for as partners' capital in the Operating Partnership's financial statements and as noncontrolling interests in American Assets Trust, Inc.'s financial statements. To help investors understand the significant differences between the company and the Operating Partnership, this report presents the following separate sections for each of American Assets Trust, Inc. and the Operating Partnership:

- consolidated financial statements;
- the following notes to the consolidated financial statements:
  Debt;
  Equity/Partners' Capital; and
  Earnings Per Share/Unit; and
- Liquidity and Capital Resources in Management's Discussion and Analysis of Financial Condition and Results of Operations.

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This report also includes separate Item 4. Controls and Procedures sections and separate Exhibit 31 and 32 certifications for each of American Assets Trust, Inc. and the Operating Partnership in order to establish that the Chief Executive Officer and the Chief Financial Officer of American Assets Trust, Inc. have made the requisite certifications and American Assets Trust, Inc. and the Operating Partnership are compliant with Rule 13a-15 or Rule 15d-15 of the Securities Exchange Act of 1934 and 18 U.S.C. §1350.

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AMERICAN ASSETS TRUST, INC. AND AMERICAN ASSETS TRUST, L.P.
QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTER ENDED MARCH 31, 2018

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PART 1 - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

American Assets Trust, Inc.
Consolidated Balance Sheets
(In Thousands, Except Share Data)

	March 31, 2018 (unaudited)	December 31, 2017
ASSETS		
Real estate, at cost		
Operating real estate	$2,539,491	$2,536,474
Construction in progress	74,447	68,272
Held for development	9,392	9,392
	2,623,330	2,614,138
Accumulated depreciation	(568,348)	(537,431)
Net real estate	2,054,982	2,076,707
Cash and cash equivalents	55,336	82,610
Restricted cash	9,889	9,344
Accounts receivable, net	8,797	9,869
Deferred rent receivables, net	39,279	38,973
Other assets, net	45,283	42,361
TOTAL ASSETS	$2,213,566	$2,259,864
LIABILITIES AND EQUITY		
LIABILITIES:		
Secured notes payable, net	$205,486	$279,550
Unsecured notes payable, net	1,045,178	1,045,470
Unsecured line of credit, net	33,031	—
Accounts payable and accrued expenses	43,507	38,069
Security deposits payable	8,683	6,570
Other liabilities and deferred credits, net	48,348	46,061
Total liabilities	1,384,233	1,415,720
Commitments and contingencies (Note 11)		
EQUITY:		
American Assets Trust, Inc. stockholders' equity		
Common stock, $0.01 par value, 490,000,000 shares authorized, 47,203,484 and 47,204,588 shares issued and outstanding at March 31, 2018 and December 31, 2017, respectively	473	473
Additional paid-in capital	919,793	919,066
Accumulated dividends in excess of net loss/income	(110,550)	(97,280)
Accumulated other comprehensive income	13,324	11,451
Total American Assets Trust, Inc. stockholders' equity	823,040	833,710
Noncontrolling interests	6,293	10,434
Total equity	829,333	844,144
TOTAL LIABILITIES AND EQUITY	$2,213,566	$2,259,864

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

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American Assets Trust, Inc.
Consolidated Statements of Comprehensive (Loss) Income
(Unaudited)
(In Thousands, Except Shares and Per Share Data)

	Three Months Ended March 31,	
	2018	2017
REVENUE:		
Rental income	$ 76,201	$ 70,040
Other property income	4,531	3,752
Total revenue	80,732	73,792
EXPENSES:		
Rental expenses	20,420	19,859
Real estate taxes	8,546	7,536
General and administrative	5,567	5,082
Depreciation and amortization	33,279	17,986
Total operating expenses	67,812	50,463
OPERATING INCOME	12,920	23,329
Interest expense	(13,820)	(13,331)
Other income, net	209	310
NET (LOSS) INCOME	(691)	10,308
Net loss (income) attributable to restricted shares	72	(60)
Net loss (income) attributable to unitholders in the Operating Partnership	166	(2,861)
NET (LOSS) INCOME ATTRIBUTABLE TO AMERICAN ASSETS TRUST, INC. STOCKHOLDERS	$ (453)	$ 7,387
(LOSS) EARNINGS PER COMMON SHARE		
(Loss) earnings per common share, basic	$ (0.01)	$ 0.16
Weighted average shares of common stock outstanding - basic	46,935,820	46,173,788
(Loss) earnings per common share, diluted	$ (0.01)	$ 0.16
Weighted average shares of common stock outstanding - diluted	46,935,820	64,062,610
DIVIDENDS DECLARED PER COMMON SHARE	$ 0.27	$ 0.26
COMPREHENSIVE (LOSS) INCOME		
Net (loss) income	$ (691)	$ 10,308
Other comprehensive income (loss) - unrealized income (loss) on swap derivative during the period	2,861	(996)
Reclassification of amortization of forward-starting swap included in interest expense	(320)	(145)
Comprehensive income	1,850	9,167
Comprehensive income attributable to non-controlling interest	(502)	(2,484)
Comprehensive income attributable to American Assets Trust, Inc.	$ 1,348	$ 6,683

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

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American Assets Trust, Inc.
Consolidated Statement of Equity
(Unaudited)
(In Thousands, Except Share Data)

	American Assets Trust, Inc. Stockholders' Equity						
	Common Shares						
	Shares	Amount	Additional Paid-in Capital	Accumulated Dividends in Excess of Net Income	Accumulated Other Comprehensive Income (Loss)	Noncontrolling Interests - Unitholders in the Operating Partnership	Total
Balance at December 31, 2017	47,204,588	$ 473	$ 919,066	$ (97,280)	$ 11,451	$ 10,434	$ 844,144
Net loss	—	—	—	(525)	—	(166)	(691)
Forfeiture of restricted stock	(1,104)	—	—	—	—	—	—
Dividends declared and paid	—	—	—	(12,745)	—	(4,643)	(17,388)
Stock-based compensation	—	—	727	—	—	—	727
Other comprehensive income (loss) - change in value of interest rate swaps	—	—	—	—	2,107	754	2,861
Reclassification of amortization of forward-starting swap included in interest expense	—	—	—	—	(234)	(86)	(320)
Balance at March 31, 2018	47,203,484	$ 473	$ 919,793	$ (110,550)	$ 13,324	$ 6,293	$ 829,333

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

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American Assets Trust, Inc.
Consolidated Statements of Cash Flows
(Unaudited)
(In Thousands)

	Three Months Ended March 31,	
	2018	2017
OPERATING ACTIVITIES		
Net (loss) income	$(691)	$10,308
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Deferred rent revenue and amortization of lease intangibles	47	(1,007)
Depreciation and amortization	33,279	17,986
Amortization of debt issuance costs and debt fair value adjustments	446	1,716
Stock-based compensation expense	727	639
Settlement of derivative instruments	—	10,430
Other noncash interest expense	(320)	(145)
Other, net	2,031	796
Changes in operating assets and liabilities		
Change in accounts receivable	577	1,726
Change in other assets	(337)	(1,038)
Change in accounts payable and accrued expenses	5,434	5,834
Change in security deposits payable	2,113	81
Change in other liabilities and deferred credits	666	279
Net cash provided by operating activities	43,972	47,605
INVESTING ACTIVITIES		
Capital expenditures	(10,138)	(7,253)
Leasing commissions	(1,227)	(902)
Deposit on property acquisition	—	(5,000)
Net cash used in investing activities	(11,365)	(13,155)
FINANCING ACTIVITIES		
Repayment of secured notes payable	(74,116)	(130,795)
Proceeds from unsecured line of credit	35,000	—
Repayment of unsecured line of credit	—	(20,000)
Proceeds from unsecured notes payable	—	250,000
Debt issuance costs	(2,656)	(1,812)
Proceeds from issuance of common stock, net	(176)	30,075
Dividends paid to common stock and unitholders	(17,388)	(16,723)
Net cash provided by (used in) financing activities	(59,336)	110,745
Net increase in cash and cash equivalents	(26,729)	145,195
Cash, cash equivalents and restricted cash, beginning of period	91,954	54,751
Cash, cash equivalents and restricted cash, end of period	$65,225	$199,946

The following table provides a reconciliation of cash, cash equivalents and restricted cash reported within the consolidated balance sheets that sum to the total of the same amounts shown in the consolidated statement of cash flows:

	Three Months Ended March 31,	
	2018	2017
Cash and cash equivalents	$55,336	$190,110

Restricted cash	9,889	9,836
Total cash, cash equivalents and restricted cash shown in the consolidated statement of cash flows	$65,225	$199,946

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

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American Assets Trust, L.P.
Consolidated Balance Sheets
(In Thousands, Except Unit Data)

	March 31, 2018 (unaudited)	December 31, 2017
ASSETS		
Real estate, at cost		
Operating real estate	$2,539,491	$2,536,474
Construction in progress	74,447	68,272
Held for development	9,392	9,392
	2,623,330	2,614,138
Accumulated depreciation	(568,348)	(537,431)
Net real estate	2,054,982	2,076,707
Cash and cash equivalents	55,336	82,610
Restricted cash	9,889	9,344
Accounts receivable, net	8,797	9,869
Deferred rent receivables, net	39,279	38,973
Other assets, net	45,283	42,361
TOTAL ASSETS	$2,213,566	$2,259,864
LIABILITIES AND EQUITY		
LIABILITIES:		
Secured notes payable, net	$205,486	$279,550
Unsecured notes payable, net	1,045,178	1,045,470
Unsecured line of credit, net	33,031	—
Accounts payable and accrued expenses	43,507	38,069
Security deposits payable	8,683	6,570
Other liabilities and deferred credits	48,348	46,061
Total liabilities	1,384,233	1,415,720
Commitments and contingencies (Note 11)		
CAPITAL:		
Limited partners' capital, 17,194,980 and 17,194,980 units issued and outstanding as of March 31, 2018 and December 31, 2017, respectively	1,326	6,135
General partner's capital, 47,203,484 and 47,204,588 units issued and outstanding as of March 31, 2018 and December 31, 2017, respectively	809,716	822,259
Accumulated other comprehensive income	18,291	15,750
Total capital	829,333	844,144
TOTAL LIABILITIES AND CAPITAL	$2,213,566	$2,259,864

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

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American Assets Trust, L.P.
Consolidated Statements of Comprehensive (Loss) Income
(Unaudited)
(In Thousands, Except Shares and Per Unit Data)

	Three Months Ended March 31,	
	2018	2017
REVENUE:		
Rental income	$76,201	$ 70,040
Other property income	4,531	3,752
Total revenue	80,732	73,792
EXPENSES:		
Rental expenses	20,420	19,859
Real estate taxes	8,546	7,536
General and administrative	5,567	5,082
Depreciation and amortization	33,279	17,986
Total operating expenses	67,812	50,463
OPERATING INCOME	12,920	23,329
Interest expense	(13,820)	(13,331)
Other income, net	209	310
NET (LOSS) INCOME	(691)	10,308
Net loss (income) attributable to restricted shares	72	(60)
NET (LOSS) INCOME ATTRIBUTABLE TO AMERICAN ASSETS TRUST, L.P.	$(619)	$ 10,248
(LOSS) EARNINGS PER UNIT - BASIC		
(Loss) earnings per unit, basic	$(0.01)	$ 0.16
Weighted average units outstanding - basic	64,130,800	64,062,610
(LOSS) EARNINGS PER UNIT - DILUTED		
(Loss) earnings per unit, diluted	$(0.01)	$ 0.16
Weighted average units outstanding - diluted	64,130,800	64,062,610
DISTRIBUTIONS PER UNIT	$0.27	$ 0.26
COMPREHENSIVE (LOSS) INCOME		
Net (loss) income	$(691)	$ 10,308
Other comprehensive income (loss) - unrealized income (loss) on swap derivative during the period	2,861	(996)
Reclassification of amortization of forward-starting swap included in interest expense	(320)	(145)
Comprehensive income	1,850	9,167
Comprehensive income attributable to Limited Partners	(502)	(2,484)
Comprehensive income attributable to General Partner	$1,348	$ 6,683

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

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American Assets Trust, L.P.
Consolidated Statement of Partners' Capital
(Unaudited)
(In Thousands, Except Unit Data)

	Limited Partners' Capital [1]		General Partner's Capital [2]		Accumulated Other Comprehensive Income (Loss)	Total Capital
	Units	Amount	Units	Amount		
Balance at December 31, 2017	17,194,980	$6,135	47,204,588	$822,259	$ 15,750	$844,144
Net loss	—	(166)	—	(525)	—	(691)
Forfeiture of restricted units	—	—	(1,104)	—	—	—
Distributions	—	(4,643)	—	(12,745)	—	(17,388)
Stock-based compensation	—	—	—	727	—	727
Other comprehensive income (loss) - change in value of interest rate swap	—	—	—	—	2,861	2,861
Reclassification of amortization of forward-starting swap included in interest expense	—	—	—	—	(320)	(320)
Balance at March 31, 2018	17,194,980	$1,326	47,203,484	$809,716	$ 18,291	$829,333

(1) Consists of limited partnership interests held by third parties.
(2) Consists of general partnership interests held by American Assets Trust, Inc.
The accompanying notes are an integral part of these consolidated financial statements.

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American Assets Trust, L.P.
Consolidated Statements of Cash Flows
(Unaudited, In Thousands)

	Three Months Ended March 31,	
	2018	2017
OPERATING ACTIVITIES		
Net (loss) income	$(691)	$10,308
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Deferred rent revenue and amortization of lease intangibles	47	(1,007)
Depreciation and amortization	33,279	17,986
Amortization of debt issuance costs and debt fair value adjustments	446	1,716
Stock-based compensation expense	727	639
Settlement of derivative instruments	—	10,430
Other noncash interest expense	(320)	(145)
Other, net	2,031	796
Changes in operating assets and liabilities		
Change in accounts receivable	577	1,726
Change in other assets	(337)	(1,038)
Change in accounts payable and accrued expenses	5,434	5,834
Change in security deposits payable	2,113	81
Change in other liabilities and deferred credits	666	279
Net cash provided by operating activities	43,972	47,605
INVESTING ACTIVITIES		
Capital expenditures	(10,138)	(7,253)
Leasing commissions	(1,227)	(902)
Deposit on property acquisition	—	(5,000)
Net cash used in investing activities	(11,365)	(13,155)
FINANCING ACTIVITIES		
Repayment of secured notes payable	(74,116)	(130,795)
Proceeds from unsecured line of credit	35,000	—
Repayment of unsecured line of credit	—	(20,000)
Proceeds from unsecured notes payable	—	250,000
Debt issuance costs	(2,656)	(1,812)
Contributions from American Assets Trust, Inc.	(176)	30,075
Distributions	(17,388)	(16,723)
Net cash provided by (used in) financing activities	(59,336)	110,745
Net increase in cash and cash equivalents	(26,729)	145,195
Cash, cash equivalents and restricted cash, beginning of period	91,954	54,751
Cash, cash equivalents and restricted cash, end of period	$65,225	$199,946

The following table provides a reconciliation of cash, cash equivalents and restricted cash reported within the consolidated balance sheets that sum to the total of the same amounts shown in the consolidated statement of cash flows:

	Three Months Ended March 31,	
	2018	2017
Cash and cash equivalents	$55,336	$190,110
Restricted cash	9,889	9,836

Total cash, cash equivalents and restricted cash shown in the consolidated statement of cash flows	$65,225	$199,946

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

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American Assets Trust, Inc. and American Assets Trust, L.P.
Notes to Consolidated Financial Statements
March 31, 2018
(Unaudited)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Business and Organization

American Assets Trust, Inc. (which may be referred to in these financial statements as the “Company,” “we,” “us,” or “our”) is a Maryland corporation formed on July 16, 2010 that did not have any operating activity until the consummation of our initial public offering on January 19, 2011. The Company is the sole general partner of American Assets Trust, L.P., a Maryland limited partnership formed on July 16, 2010 (the “Operating Partnership”). The Company’s operations are carried on through our Operating Partnership and its subsidiaries, including our taxable real estate investment trust ("REIT") subsidiary ("TRS"). Since the formation of our Operating Partnership, the Company has controlled our Operating Partnership as its general partner and has consolidated its assets, liabilities and results of operations.

We are a full service vertically integrated and self-administered REIT with approximately 195 employees providing substantial in-house expertise in asset management, property management, property development, leasing, tenant improvement construction, acquisitions, repositioning, redevelopment and financing.

As of March 31, 2018, we owned or had a controlling interest in 26 office, retail, multifamily and mixed-use operating properties, the operations of which we consolidate. Additionally, as of March 31, 2018, we owned land at four of our properties that we classify as held for development and/or construction in progress. A summary of the properties owned by us is as follows:

Retail		
Carmel Country Plaza	Gateway Marketplace	Alamo Quarry Market
Carmel Mountain Plaza	Del Monte Center	Hassalo on Eighth - Retail
South Bay Marketplace	Geary Marketplace	
Lomas Santa Fe Plaza	The Shops at Kalakaua	
Solana Beach Towne Centre	Waikele Center	

Office	
Torrey Reserve Campus	Lloyd District Portfolio
Solana Beach Corporate Centre	City Center Bellevue
The Landmark at One Market	
One Beach Street	
First & Main	

Multifamily	
Loma Palisades	Hassalo on Eighth - Residential
Imperial Beach Gardens	
Mariner's Point	
Santa Fe Park RV Resort	
Pacific Ridge Apartments	

Mixed-Use
Waikiki Beach Walk Retail and Embassy Suites™ Hotel

Held for Development and/or Construction in Progress
Solana Beach Corporate Centre – Land
Solana Beach – Highway 101 – Land

Torrey Point – Construction in Progress
Lloyd District Portfolio – Construction in Progress

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Basis of Presentation

Our consolidated financial statements include the accounts of the Company, our Operating Partnership and our subsidiaries. The equity interests of other investors in our Operating Partnership are reflected as noncontrolling interests.

All significant intercompany transactions and balances are eliminated in consolidation.

The accompanying consolidated financial statements of the Company and the Operating Partnership have been prepared in accordance with the rules applicable to Form 10-Q and include all information and footnotes required for interim financial statement presentation, but do not include all disclosures required under accounting principles generally accepted in the United States ("GAAP") for annual financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments, except as otherwise noted) considered necessary for a fair presentation have been included. These financial statements should be read in conjunction with the audited consolidated financial statements and notes therein included in the Company's and Operating Partnership's annual report on Form 10-K for the year ended December 31, 2017.

The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that in certain circumstances affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities, and revenues and expenses. These estimates are prepared using our best judgment, after considering past, current and expected events and economic conditions. Actual results could differ from these estimates.

Any reference to the number of properties, number of units, square footage, employee numbers or percentages of beneficial ownership of our shares are unaudited and outside the scope of our independent registered public accounting firm's review of our financial statements in accordance with the standards of the United States Public Company Accounting Oversight Board.

Consolidated Statements of Cash Flows—Supplemental Disclosures

The following table provides supplemental disclosures related to the Consolidated Statements of Cash Flows (in thousands):

	Three Months Ended March 31,	
	2018	2017
Supplemental cash flow information		
Total interest costs incurred	$14,277	$13,702
Interest capitalized	$457	$371
Interest expense	$13,820	$13,331
Cash paid for interest, net of amounts capitalized	$14,059	$10,708
Cash paid for income taxes	$31	$46
Supplemental schedule of noncash investing and financing activities		
Accounts payable and accrued liabilities for construction in progress	$(706)	$577
Accrued leasing commissions	$710	$193
Reduction to capital for prepaid offering costs	$176	$—

Significant Accounting Policies

We describe our significant accounting policies in Note 1 to the consolidated financial statements in Item 8 of our Annual Report on Form 10-K for the year ended December 31, 2017. Except for the adoption of the accounting standards during the first quarter of 2018 as discussed below, there have been no changes to our significant accounting policies during the three months ended March 31, 2018.

Segment Information

Segment information is prepared on the same basis that our chief operating decision maker reviews information for operational decision-making purposes. We operate in four business segments: the acquisition, redevelopment, ownership and management of retail real estate, office real estate, multifamily real estate and mixed-use real estate. The products for our retail segment primarily include rental of retail space and other tenant services, including tenant reimbursements, parking and storage space rental. The products for our office segment primarily include rental of office space and other tenant services, including tenant reimbursements, parking and storage space rental. The products for our multifamily segment include rental of apartments and other tenant services. The products of our mixed-use segment include rental of retail space and other tenant services, including tenant reimbursements, parking and storage space rental and operation of a 369-room all-suite hotel.

Recent Accounting Pronouncements

In February 2016, the Financial Accounting Standards Board (the "FASB") issued Accounting Standards Update ("ASU") No. 2016-2, Leases. This pronouncement is expected to result in the recognition of a right-to-use asset and related liability to account for future obligations under ground lease agreements for which we are the lessee. In addition, this pronouncement will require that lessees and lessors capitalize, as initial direct costs, only those costs that are incurred due to the execution of a lease. As of March 31, 2018, the remaining contractual payments under lease agreements for which we are the lessee aggregated approximately $37.5 million.

As a lessor, under current accounting standards, we recognize rental revenue from our operating leases on a straight-line basis over the respective lease terms. We commence recognition of rental revenue at the date the property is ready for its intended use and the tenant takes possession of or controls the physical use of the property. Under current accounting standards, tenant recoveries related to payments of real estate taxes, insurance, utilities, repairs and maintenance, common area expenses, and other operating expenses are considered lease components. We recognize these tenant recoveries as revenue when services are rendered in an amount equal to the related operating expenses incurred that are recoverable under the terms of the applicable lease.

Under this pronouncement, each lease agreement will be evaluated to identify the lease components and nonlease components at lease inception. The total consideration in the lease agreement will be allocated to the lease and nonlease components based on their relative standalone selling prices. Lessors will continue to recognize the lease revenue component using an approach that is substantially equivalent to existing guidance for operating leases (straight-line basis). In March 2018, the FASB approved an amendment to the lease ASU that would allow lessors to elect, as a practical expedient, not to allocate the total consideration to lease and nonlease components based on their relative standalone selling prices. This practical expedient will allow lessors to elect a combined single lease component presentation if (i) the timing and pattern of the revenue recognition of the combined single lease component is the same, and (ii) the related lease component and, the combined single lease component would be classified as an operating lease.

The pronouncement is effective for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2018, with early adoption permitted. We plan to adopt the provisions of ASU No. 2016-2 effective January 1, 2019 using the modified retrospective approach. We continue to evaluate the impact this pronouncement will have on our consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers. The pronouncement was issued to clarify the principles for recognizing revenue and to develop a common revenue standard and disclosure requirements for U.S. GAAP and International Financial Reporting Standards. The pronouncement is effective for reporting periods beginning after December 15, 2017. We adopted the provisions of the ASU effective January 1, 2018 using the modified retrospective approach. As discussed above, leases are specifically excluded from this and will be governed by the applicable lease codification..

We evaluated the revenue recognition for all contracts within this scope under existing accounting standards and under the new revenue recognition ASU and confirmed that there were no differences in the amounts recognized or the pattern of recognition. This evaluation included revenues from the hotel portion of our mixed-use property, parking income and excise taxes charged to customers. Therefore, the adoption of this ASU did not result in an adjustment to our retained earnings on January 1, 2018.

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NOTE 2. ACQUIRED IN-PLACE LEASES AND ABOVE/BELOW MARKET LEASES
The following summarizes our acquired lease intangibles and leasing costs, which are included in other assets and other liabilities and deferred credits, as of March 31, 2018 and December 31, 2017 (in thousands):

	March 31, 2018	December 31, 2017
In-place leases	$48,442	$ 54,206
Accumulated amortization	(40,699)	(45,835)
Above market leases	21,262	21,262
Accumulated amortization	(20,306)	(20,084)
Acquired lease intangible assets, net	$8,699	$ 9,549
Below market leases	$67,348	$ 67,423
Accumulated accretion	(38,103)	(37,241)
Acquired lease intangible liabilities, net	$29,245	$ 30,182

NOTE 3. FAIR VALUE OF FINANCIAL INSTRUMENTS
A fair value measurement is based on the assumptions that market participants would use in pricing an asset or liability. The hierarchy for inputs used in measuring fair value is as follows:

1. Level 1 Inputs—quoted prices in active markets for identical assets or liabilities
2. Level 2 Inputs—observable inputs other than quoted prices in active markets for identical assets and liabilities
3. Level 3 Inputs—unobservable inputs

Except as disclosed below, the carrying amounts of our financial instruments approximate their fair value. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, for disclosure purposes, the level within which the fair value measurement is categorized is based on the lowest level input that is significant to the fair value measurement.
We measure the fair value of our deferred compensation liability, which is included in other liabilities and deferred credits on the consolidated balance sheet, on a recurring basis using Level 2 inputs. We measure the fair value of this liability based on prices provided by independent market participants that are based on observable inputs using market-based valuation techniques.

The fair value of the interest rate swap agreements are based on the estimated amounts we would receive or pay to terminate the contract at the reporting date and are determined using interest rate pricing models and interest rate related observable inputs. The effective portion of changes in the fair value of the derivatives that are designated as cash flow hedges are being recorded in accumulated other comprehensive (loss) income and will be subsequently reclassified into earnings during the period in which the hedged forecasted transaction affects earnings.

We incorporate credit valuation adjustments to appropriately reflect both our own non-performance risk and the respective counterparty's non-performance risk in the fair value measurements. In adjusting the fair value of our derivative contracts for the effect of non-performance risk, we considered the impact of netting and any applicable credit enhancements, such as collateral postings, thresholds, mutual puts, and guarantees.

Although we have determined that the majority of the inputs used to value our derivatives fall within Level 2 of the fair value hierarchy, the credit valuation adjustments associated with its derivatives utilize Level 3 inputs, such as estimates of current credit spreads to evaluate the likelihood of default by itself and its counterparties. However, as of March 31, 2018 we have assessed the significance of the impact of the credit valuation adjustments on the overall valuation of our derivative position and have determined that the credit valuation adjustments are not significant to the overall valuation of our derivative. As a result, we have determined that our derivative valuation in its entirety is classified in Level 2 of the fair value hierarchy.

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A summary of our financial liabilities that are measured at fair value on a recurring basis, by level within the fair value hierarchy is as follows (in thousands):

	March 31, 2018				December 31, 2017			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Deferred compensation liability	$—	$1,224	$—	$1,224	$—	$1,156	$—	$1,156
Interest rate swap asset	$—	$7,941	$—	$7,941	$—	$5,091	$—	$5,091
Interest rate swap liability	$—	$—	$—	$—	$—	$10	$—	$10

The fair value of our secured notes payable and unsecured senior guaranteed notes are sensitive to fluctuations in interest rates. Discounted cash flow analysis using observable market interest rates (Level 2) is generally used to estimate the fair value of our secured notes payable, using rates ranging from 3.8% to 4.9%.

Considerable judgment is necessary to estimate the fair value of financial instruments. The estimates of fair value presented herein are not necessarily indicative of the amounts that could be realized upon disposition of the financial instruments. The carrying values of our revolving line of credit and term loan set forth below are deemed to be at fair value since the outstanding debt is directly tied to monthly LIBOR contracts. A summary of the carrying amount and fair value of our secured financial instruments, all of which are based on Level 2 inputs, is as follows (in thousands):

	March 31, 2018		December 31, 2017	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Secured notes payable, net	$205,486	$210,402	$279,550	$286,156
Unsecured term loans, net	$248,430	$250,000	$248,839	$250,000
Unsecured senior guaranteed notes, net	$796,748	$786,549	$796,631	$802,699
Unsecured line of credit, net	$33,031	$35,000	$—	$—

NOTE 4. DERIVATIVE AND HEDGING ACTIVITIES

Our objectives in using interest rate derivatives are to add stability to interest expense and to manage our exposure to interest rate movements. To accomplish these objectives, we primarily use interest rate swaps as part of our interest rate risk management strategy. Interest rate swaps designated as cash flow hedges involve the receipt of variable-rate amounts from a counterparty in exchange for us making fixed-rate payments over the life of the agreements without exchange of the underlying notional amount.

The following is a summary of the terms of our outstanding interest rate swaps as of March 31, 2018 (dollars in thousands):

Swap Counterparty	Notional Amount	Effective Date	Maturity Date	Fair Value
Bank of America, N.A.	$100,000	1/9/2014	1/9/2019	$228
U.S. Bank N.A.	$100,000	3/1/2016	3/1/2023	$5,116
Wells Fargo Bank, N.A.	$50,000	5/2/2016	3/1/2023	$2,597

The effective portion of changes in the fair value of the derivatives that are designated as cash flow hedges are being recorded in accumulated other comprehensive income and will be subsequently reclassified into earnings during the period in which the hedged forecasted transaction affects earnings for as long as hedged cash flows remain probable. The valuation of these instruments is determined using widely accepted valuation techniques including discounted cash flow analysis on the expected cash flows of the derivative. This analysis reflects the contractual terms of the derivative, including the period to maturity, counter party credit risk and uses observable market-based inputs, including interest rate curves, and implied volatilities. The fair value of the interest rate swap is determined using the market standard methodology of netting the discounted future fixed cash receipts (or payments) and the discounted expected variable cash payments (or receipts). The variable cash payments (or receipts) are based on an expectation of future interest rates (forward curves) derived from observable market interest rate curves.

NOTE 5. OTHER ASSETS

Other assets consist of the following (in thousands):

	March 31, 2018	December 31, 2017
Leasing commissions, net of accumulated amortization of $29,689 and $28,318, respectively	$ 21,089	$ 20,633
Interest rate swap asset	7,941	5,091
Acquired above market leases, net	956	1,178
Acquired in-place leases, net	7,743	8,371
Lease incentives, net of accumulated amortization of $171 and $136, respectively	881	916
Other intangible assets, net of accumulated amortization of $1,112 and $1,115, respectively	214	227
Prepaid expenses and other	6,459	5,945
Total other assets	$ 45,283	$ 42,361

NOTE 6. OTHER LIABILITIES AND DEFERRED CREDITS

Other liabilities and deferred credits consist of the following (in thousands):

	March 31, 2018	December 31, 2017
Acquired below market leases, net	$ 29,245	$ 30,182
Prepaid rent and deferred revenue	10,253	8,429
Interest rate swap liability	—	10
Deferred rent expense and lease intangible	2,248	1,670
Deferred compensation	1,224	1,156
Deferred tax liability	123	123
Straight-line rent liability	5,188	4,428
Other liabilities	67	63
Total other liabilities and deferred credits, net	$ 48,348	$ 46,061

Straight-line rent liability relates to leases which have rental payments that decrease over time or one-time upfront payments for which the rental revenue is deferred and recognized on a straight-line basis.

NOTE 7. DEBT

Debt of American Assets Trust, Inc.

American Assets Trust, Inc. does not hold any indebtedness. All debt is held directly or indirectly by the Operating Partnership; however, American Assets Trust, Inc. has guaranteed the Operating Partnership's obligations under the (i) amended and restated credit facility, (ii) term loans and (iii) senior guaranteed notes. Additionally, American Assets Trust, Inc. has provided carve-out guarantees on certain property-level mortgage debt.

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Debt of American Assets Trust, L.P.

Secured notes payable

The following is a summary of our total secured notes payable outstanding as of March 31, 2018 and December 31, 2017 (in thousands):

Description of Debt	Principal Balance as of March 31, 2018	Principal Balance as of December 31, 2017	Stated Interest Rate as of March 31, 2018	Stated Maturity Date
Loma Palisades [1][2]	—	73,744	6.09 %	July 1, 2018
One Beach Street [1]	21,900	21,900	3.94 %	April 1, 2019
Torrey Reserve—North Court [3]	19,925	20,023	7.22 %	June 1, 2019
Torrey Reserve—VCI, VCII, VCIII [3]	6,731	6,764	6.36 %	June 1, 2020
Solana Beach Corporate Centre I-II [3]	10,665	10,721	5.91 %	June 1, 2020
Solana Beach Towne Centre [3]	35,552	35,737	5.91 %	June 1, 2020
City Center Bellevue [1]	111,000	111,000	3.98 %	November 1, 2022
	205,773	279,889		
Debt issuance costs, net of accumulated amortization of $798 and $1,191, respectively	(287)	(339)		
Total Secured Notes Payable Outstanding	$205,486	$ 279,550		

(1) Interest only.
(2) Loan repaid in full, without premium or penalty, on March 30, 2018.
(3) Principal payments based on a 30-year amortization schedule.

Certain loans require us to comply with various financial covenants. As of March 31, 2018, the Operating Partnership was in compliance with these financial covenants.

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Unsecured notes payable
The following is a summary of the Operating Partnership's total unsecured notes payable outstanding as of March 31, 2018 and December 31, 2017 (in thousands):

Description of Debt	Principal Balance as of March 31, 2018	Principal Balance as of December 31, 2017	Stated Interest Rate as of March 31, 2018		Stated Maturity Date
Term Loan A	$100,000	$100,000	Variable	(1)	January 9, 2019
Senior Guaranteed Notes, Series A	150,000	150,000	4.04	% (2)	October 31, 2021
Term Loan B	100,000	100,000	Variable	(3)	March 1, 2023
Term Loan C	50,000	50,000	Variable	(4)	March 1, 2023
Senior Guaranteed Notes, Series F	100,000	100,000	3.78	% (5)	July 19, 2024
Senior Guaranteed Notes, Series B	100,000	100,000	4.45	%	February 2, 2025
Senior Guaranteed Notes, Series C	100,000	100,000	4.50	%	April 1, 2025
Senior Guaranteed Notes, Series D	250,000	250,000	4.29	% (6)	March 1, 2027
Senior Guaranteed Notes, Series E	100,000	100,000	4.24	% (7)	May 23, 2029
	1,050,000	1,050,000			
Debt issuance costs, net of accumulated amortization of $6,159 and $5,866, respectively	(4,822)	(4,530)			
Total Unsecured Notes Payable	$1,045,178	$1,045,470			

(1) The Operating Partnership has entered into an interest rate swap agreement that is intended to fix the interest rate associated with Term Loan A at approximately 3.08% through its maturity date and extension options, subject to adjustments based on our consolidated leverage ratio.

(2) The Operating Partnership entered into a one-month forward-starting seven-year swap contract on August 19, 2014, which was settled on September 19, 2014 at a gain of approximately $1.6 million. The forward-starting seven-year swap contract was deemed to be a highly effective cash flow hedge, accordingly, the effective interest rate is approximately 3.88% per annum.

(3) The Operating Partnership has entered into an interest rate swap agreement that is intended to fix the interest rate associated with Term Loan B at approximately 3.15% through its maturity date, subject to adjustments based on our consolidated leverage ratio. Effective March 1, 2018, the effective interest rate associated with Term Loan B is approximately 2.75%, subject to adjustments based on our consolidated leverage ratio.

(4) The Operating Partnership has entered into an interest rate swap agreement that is intended to fix the interest rate associated with Term Loan C at approximately 3.14% through its maturity date, subject to adjustments based on our consolidated leverage ratio. Effective March 1, 2018, the effective interest rate associated with Term Loan C is approximately 2.74%, subject to adjustments based on our consolidated leverage ratio.

(5) The Operating Partnership entered into a treasury lock contract on May 31, 2017, which was settled on June 23, 2017 at a loss of approximately $0.5 million. The treasury lock contract was deemed to be a highly effective cash flow hedge, accordingly, the effective interest rate is approximately 3.85% per annum.

(6) The Operating Partnership entered into forward-starting interest rate swap contracts on March 29, 2016 and April 7, 2016, which were settled on January 18, 2017 at a gain of approximately $10.4 million. The forward-starting

interest swap rate contracts were deemed to be a highly effective cash flow hedge, accordingly, the effective interest rate is approximately 3.87% per annum.

(7) The Operating Partnership entered into a treasury lock contract on April 25, 2017, which was settled on May 11, 2017 at a gain of approximately $0.7 million. The treasury lock contract was deemed to be a highly effective cash flow hedge, accordingly, the effective interest rate is approximately 4.18% per annum.

Certain loans require us to comply with various financial covenants. As of March 31, 2018, the Operating Partnership was in compliance with these financial covenants.

On January 9, 2018, we entered into the Third Amendment to the Term Loan Agreement (as so amended, the "Term Loan Agreement"), which maintains the seven-year $150 million unsecured term loan (referred to herein as Term Loan B and Term Loan C) to the Operating Partnership that matures on March 1, 2023 (the “$150mm Term Loan”). Effective as of March 1, 2018, borrowings under the Term Loan Agreement with respect to the $150mm Term Loan bear interest at floating rates equal to, at the Operating Partnership’s option, either (1) LIBOR, plus a spread which ranges from 1.20% to 1.70% based on the Operating Partnership’s consolidated leverage ratio, or (2) a base rate equal to the highest of (a) 0%, (b) the prime rate, (c) the federal funds rate plus 50 bps or (d) the Eurodollar rate plus 100 bps, in each case plus a spread which ranges from 0.70% to 1.35% based on the Operating Partnership’s consolidated leverage ratio. Additionally, the Operating Partnership may elect for borrowings to bear interest based on a ratings-based pricing grid as per the Operating Partnership’s then-applicable investment grade debt ratings under the terms set forth in the Term Loan Agreement.

Second Amended and Restated Credit Facility

On January 9, 2018, we entered into a second amended and restated credit agreement (the "Second Amended and Restated Credit Facility"). The Second Amended and Restated Credit Facility provides for aggregate, unsecured borrowing of $450 million, consisting of a revolving line of credit of $350 million (the "Revolver Loan") and a term loan of $100 million (the "Term Loan A"). The Second Amended and Restated Credit Facility has an accordion feature that may allow us to increase the availability thereunder up to an additional $350 million, subject to meeting specified requirements and obtaining additional commitments from lenders. At March 31, 2018, there was $35 million outstanding under the Revolver Loan with approximately $2.0 million of debt issuance costs, net.

Borrowings under the Second Amended and Restated Credit Agreement initially bear interest at floating rates equal to, at our option, either (1) LIBOR, plus a spread which ranges from (a) 1.05% to 1.50% (with respect to the Revolver Loan) and (b) 1.30% to 1.90% (with respect to Term Loan A), in each case based on our consolidated leverage ratio, or (2) a base rate equal to the highest of (a) the prime rate, (b) the federal funds rate plus 50 bps or (c) LIBOR plus 100 bps, plus a spread which ranges from (i) 0.10% to 0.50% (with respect to the Revolver Loan) and (ii) 0.30% to 0.90% (with respect to Term Loan A), in each case based on our consolidated leverage ratio. For the three months ended March 31, 2018, the weighted average interest rate on the Revolver Loan was 3.40%.

The Revolver Loan initially matures on January 9, 2022, subject to our option to extend the Revolver Loan up to two times, with each such extension for a six-month period. The Term Loan A matures on January 9, 2019 with no further extension options. The foregoing extension options are exercisable by us subject to the satisfaction of certain conditions.

Additionally, the Second Amended and Restated Credit Facility includes a number of customary financial covenants, including:

- A maximum leverage ratio (defined as total indebtedness net of certain cash and cash equivalents to total asset value) of 60%,
- A maximum secured leverage ratio (defined as total secured debt to secured total asset value) of 40%,
- A minimum fixed charge coverage ratio (defined as consolidated earnings before interest, taxes, depreciation and amortization to consolidated fixed charges) of 1.50x,
- A minimum unsecured interest coverage ratio of 1.75x,
- A maximum unsecured leverage ratio of 60%, and
- Recourse indebtedness at any time cannot exceed 15% of total asset value.

The Second Amended and Restated Credit Facility provides that our annual distributions may not exceed the greater of (1) 95% of our funds from operation ("FFO") or (2) the amount required for us to (a) qualify and maintain our REIT status and (b) avoid the payment of federal or state income or excise tax. If certain events of default exist or would result from a distribution, we may be precluded from making distributions other than those necessary to qualify and maintain our status as a REIT.

As of March 31, 2018, the Operating Partnership was in compliance with the financial covenants in the Second Amended and Restated Credit Facility.

NOTE 8. PARTNERS' CAPITAL OF AMERICAN ASSETS TRUST, L.P.

Noncontrolling interests in our Operating Partnership are interests in the Operating Partnership that are not owned by us. Noncontrolling interests consisted of 17,194,980 common units (the “noncontrolling common units”), and represented approximately 26.8% of the ownership interests in our Operating Partnership at March 31, 2018. Common units and shares of our common stock have essentially the same economic characteristics in that common units and shares of our common stock share equally in the total net income or loss distributions of our Operating Partnership. Investors who own common units have the right to cause our Operating Partnership to redeem any or all of their common units for cash equal to the then-current market value of one share of our common stock, or, at our election,

shares of our common stock on a one-for-one basis.
During the three months ended March 31, 2018, no common units were converted into shares of our common stock.

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(Loss) Earnings Per Unit of the Operating Partnership

Basic (loss) earnings per unit (“EPU”) of the Operating Partnership is computed by dividing income applicable to unitholders by the weighted average Operating Partnership units outstanding, as adjusted for the effect of participating securities. Operating Partnership units granted in equity-based payment transactions that have non-forfeitable dividend equivalent rights are considered participating securities prior to vesting. The impact of unvested Operating Partnership unit awards on EPU has been calculated using the two-class method whereby earnings are allocated to the unvested Operating Partnership unit awards based on distributions and the unvested Operating Partnership units’ participation rights in undistributed earnings.

For the three months ended March 31, 2018, shares associated with convertible securities were not included because the inclusion would be anti-dilutive. The calculation of diluted EPU for the three month periods ended March 31, 2017 does not include the weighted average of 232,099 unvested Operating Partnership units, as these equity securities are either considered contingently issuable or the effect of including these equity securities was anti-dilutive to income from continuing operations and net income attributable to the unitholders.

NOTE 9. EQUITY OF AMERICAN ASSETS TRUST, INC.

Stockholders' Equity

On May 27, 2015, we entered into an at-the-market ("ATM") equity program with five sales agents in which we may, from time to time, offer and sell shares of our common stock having an aggregate offering price of up to $250.0 million. On March 2, 2018, we amended certain of these equity programs, terminated one such program and entered into a new equity program with one new sales agent. The sales of shares of our common stock made through the ATM equity program, as amended, are made in "at-the-market" offerings as defined in Rule 415 of the Securities Act of 1933, as amended. During the three months ended March 31, 2018, no shares of common stock were sold through the ATM equity program.

We intend to use the net proceeds from the ATM equity program to fund our development or redevelopment activities, repay amounts outstanding from time to time under our revolving line of credit or other debt financing obligations, fund potential acquisition opportunities and/or for general corporate purposes. As of March 31, 2018, we had the capacity to issue up to an additional $176.2 million in shares of our common stock under our ATM equity program. Actual future sales will depend on a variety of factors including, but not limited to, market conditions, the trading price of our common stock and our capital needs. We have no obligation to sell the remaining shares available for sale under the ATM equity program.

Dividends

The following table lists the dividends declared and paid on our shares of common stock and noncontrolling common units during the three months ended March 31, 2018:

Period	Amount per Share/Unit	Period Covered	Dividend Paid Date
First Quarter 2018	$ 0.27	January 1, 2018 to March 31, 2018	March 29, 2018

Taxability of Dividends

Earnings and profits, which determine the taxability of distributions to stockholders and holders of common units, may differ from income reported for financial reporting purposes due to the differences for federal income tax purposes in the treatment of revenue recognition and compensation expense and in the basis of depreciable assets and estimated useful lives used to compute depreciation.

Stock-Based Compensation

We follow the FASB guidance related to stock compensation which establishes financial accounting and reporting standards for stock-based employee compensation plans, including all arrangements by which employees receive shares of stock or other equity instruments of the employer. The guidance also defines a fair value-based method of accounting for an employee stock option or similar equity instrument.

The following table summarizes the activity of restricted stock awards during the three months ended March 31, 2018:

	Units	Weighted Average Grant Date Fair Value
Nonvested at January 1, 2018	268,768	$29.89
Granted	—	—
Vested	—	—
Forfeited	(1,104)	$29.71
Nonvested at March 31, 2018	267,664	$29.89

We recognize noncash compensation expense ratably over the vesting period, and accordingly, we recognized $0.7 million and $0.6 million in noncash compensation expense for the three month periods ended March 31, 2018 and 2017, respectively, which is included in general and administrative expense on the consolidated statements of comprehensive (loss) income. Unrecognized compensation expense was $3.3 million at March 31, 2018.

Earnings Per Share

We have calculated earnings per share ("EPS") under the two-class method. The two-class method is an earnings allocation methodology whereby EPS for each class of common stock and participating security is calculated according to dividends declared and participation rights in undistributed earnings. The weighted average unvested shares outstanding, which are considered participating securities, were 263,606 and 232,099 for the three months ended March 31, 2018 and 2017, respectively. Therefore, we have allocated our earnings for basic and diluted EPS between common shares and unvested shares as these unvested shares have nonforfeitable dividend equivalent rights. For the three months ended March 31, 2018, shares associated with convertible securities were not included because the inclusion would be anti-dilutive.

Diluted EPS is calculated by dividing the net income applicable to common stockholders for the period by the weighted average number of common and dilutive instruments outstanding during the period using the treasury stock method. For the three months ended March 31, 2018, shares associated with convertible securities were not included because the inclusion would be anti-dilutive. For the three months ended March 31, 2017, diluted shares exclude incentive restricted stock as these awards are considered contingently issuable. Additionally, the unvested restricted stock awards subject to time vesting are anti-dilutive for all periods presented, and accordingly, have been excluded from the weighted average common shares used to compute diluted EPS.

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The computation of basic and diluted EPS is presented below (dollars in thousands, except share and per share amounts):

	Three Months Ended March 31, 2018	Three Months Ended March 31, 2017
NUMERATOR		
Net (loss) income from operations	$(691)	$ 10,308
Less: Net loss (income) attributable to restricted shares	72	(60)
Less: Loss (income) from operations attributable to unitholders in the Operating Partnership	166	(2,861)
(Loss) income from continuing operations attributable to American Assets Trust, Inc. common stockholders—basic	(453)	7,387
Net (loss) income attributable to common stockholders—basic	$(453)	$ 7,387
(Loss) income from operations attributable to American Assets Trust, Inc. common stockholders—basic	$(453)	$ 7,387
Plus: Income from operations attributable to unitholders in the Operating Partnership	—	2,861
(Loss) income from continuing operations attributable to common stockholders—diluted	(453)	10,248
Net (loss) income attributable to common stockholders—diluted	$(453)	$ 10,248
DENOMINATOR		
Weighted average common shares outstanding—basic	46,935,820	46,173,788
Effect of dilutive securities—conversion of Operating Partnership units	—	17,888,822
Weighted average common shares outstanding—diluted	46,935,820	64,062,610
(Loss) earnings per common share, basic	$(0.01)	$ 0.16
(Loss) earnings per common share, diluted	$(0.01)	$ 0.16

NOTE 10. INCOME TAXES

We elected to be taxed as a REIT and operate in a manner that allows us to qualify as a REIT for federal income tax purposes commencing with our initial taxable year. As a REIT, we are generally not subject to corporate level income tax on the earnings distributed currently to our stockholders that we derive from our REIT qualifying activities. Taxable income from non-REIT activities managed through our TRS is subject to federal and state income taxes.

We lease our hotel property to a wholly owned TRS that is subject to federal and state income taxes. We account for income taxes using the asset and liability method, under which deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between GAAP carrying amounts and their respective tax bases. Additionally, we classify certain state taxes as income taxes for financial reporting purposes in accordance with ASC Topic 740, Income Taxes.

A deferred tax liability is included in our consolidated balance sheets of $0.1 million as of March 31, 2018 and December 31, 2017, respectively, in relation to real estate asset basis differences of property subject to state taxes based on income and certain prepaid expenses of our TRS.

Income tax benefit is recorded in other income, net on our consolidated statements of comprehensive (loss) income. For the three months ended March 31, 2018 and 2017, we recorded income tax benefit of $0.1 million and $0.2 million, respectively.

NOTE 11. COMMITMENTS AND CONTINGENCIES

Legal

We are sometimes involved in various disputes, lawsuits, warranty claims, environmental and other matters arising in the ordinary course of business. Management makes assumptions and estimates concerning the likelihood and amount of any potential loss relating to these matters.

We are currently a party to various legal proceedings. We accrue a liability for litigation if an unfavorable outcome is probable and the amount of loss can be reasonably estimated. If an unfavorable outcome is probable and a reasonable estimate of the loss is a range, we accrue the best estimate within the range; however, if no amount within the range is a better estimate than any other amount, the minimum within the range is accrued. Legal fees related to litigation are expensed as incurred. We do not believe that the ultimate outcome of these matters, either individually or in the aggregate, could have a material adverse effect on our financial position or overall trends in results of operations; however, litigation is subject to inherent uncertainties. Also, under our leases, tenants are typically obligated to indemnify us from and against all liabilities, costs and expenses imposed upon or asserted against us as owner of the properties due to certain matters relating to the operation of the properties by the tenant.

Commitments

At the Landmark at One Market, we lease (the "Annex Lease"), as lessee, a building adjacent to the Landmark at One Market under an operating lease effective through June 30, 2021, which we have the option to extend until 2031 by way of two five-year extension options.

At Waikiki Beach Walk, we sublease (the "FHB Sublease") a portion of the building of which Quiksilver is currently in possession, under an operating lease effective through December 31, 2021.

Current minimum annual payments under the leases are as follows, as of March 31, 2018 (in thousands):

Year Ending December 31,		
2018 (nine months ending December 31, 2018)	$2,464	
2019	3,347	
2020	3,422	
2021	3,460	(1)
2022	2,613	
Thereafter	22,210	
Total	$37,516	

(1) Lease payments on the Annex Lease will be equal to fair rental value from July 2021 through the end of the extended lease term. In the table above, we have shown the option lease payments for this period based on the stated rate for the month of June 2021 of $217,744.

We have management agreements with Outrigger Hotels & Resorts or an affiliate thereof (“Outrigger”) pursuant to which Outrigger manages each of the retail and hotel portions of the Waikiki Beach Walk property. Under the management agreement with Outrigger relating to the retail portion of Waikiki Beach Walk (the “retail management agreement”), we pay Outrigger a monthly management fee of 3.0% of net revenues from the retail portion of Waikiki Beach Walk. Pursuant to the terms of the retail management agreement, if the agreement is terminated in certain instances, including our election not to repair damage or destruction at the property, a condemnation or our failure to make required working capital infusions, we would be obligated to pay Outrigger a termination fee equal to the sum of the management fees paid for the two calendar months immediately preceding the termination date. The retail management agreement may not be terminated by us or by Outrigger without cause. Under our management agreement with Outrigger relating to the hotel portion of Waikiki Beach Walk (the “hotel management agreement”), we pay Outrigger a monthly management fee of 6.0% of the hotel's gross operating profit, as well as 3.0% of the hotel's gross revenues; provided that the aggregate management fee payable to Outrigger for any year shall not exceed 3.5% of the hotel's gross revenues for such fiscal year. Pursuant to the terms of the hotel management agreement, if the agreement is terminated in certain instances, including upon a transfer by us of the hotel or upon a default by us under the hotel management agreement, we would be required to pay a cancellation fee calculated by multiplying (1) the management fees for the previous 12 months by (2) (a) eight, if the agreement is terminated in the first 11 years of its term, or (b) four, three, two or one, if the agreement is terminated in the twelfth, thirteenth, fourteenth or fifteenth year, respectively, of its term. The hotel management agreement may not be terminated by us or by Outrigger without cause.

A wholly owned subsidiary of our Operating Partnership, WBW Hotel Lessee LLC, entered into a franchise license agreement with Embassy Suites Franchise LLC, the franchisor of the brand “Embassy Suites™,” to obtain the non-exclusive right to operate the hotel under the Embassy Suites™ brand for 20 years. The franchise license agreement provides that WBW Hotel Lessee LLC must comply with certain management, operational, record keeping, accounting, reporting and marketing standards and procedures. In connection with this agreement, we are also subject to the terms of a product improvement plan pursuant to which we expect to undertake certain actions to ensure that our hotel's infrastructure is maintained in compliance with the franchisor's brand standards. In addition, we must pay to Embassy Suites Franchise LLC a monthly franchise royalty fee equal to 4.0% of the hotel's gross room revenue through December 2021 and 5.0% of the hotel's gross room revenue thereafter, as well as a monthly program fee equal to 4.0% of the hotel's gross room revenue. If the franchise license is terminated due to our failure to make required improvements or to otherwise comply with its terms, we may be liable to the franchisor for a termination payment, which could be as high as $7.5 million based on operating performance through March 31, 2018.

Our Del Monte Center property has ongoing environmental remediation related to ground water contamination. The environmental issue existed at purchase and remains in remediation. The final stages of the remediation will include routine, long term ground monitoring by the appropriate regulatory agency over the next five to seven years. The work performed is financed through an escrow account funded by the seller upon purchase of the Del Monte Center. We believe the funds in the escrow account are sufficient for the remaining work to be performed. However, if further work is required costing more than the remaining escrow funds, we could be required to pay such overage, although we may have a contractual claim for such costs against the prior owner or our environmental remediation consultant.

Concentrations of Credit Risk

Our properties are located in Southern California, Northern California, Hawaii, Oregon, Texas, and Washington. The ability of the tenants to honor the terms of their respective leases is dependent upon the economic, regulatory and social factors affecting the markets in which the tenants operate. Thirteen of our consolidated properties are located in Southern California, which exposes us to greater economic risks than if we owned a more geographically diverse portfolio. Tenants in the retail industry accounted for 32.4% of total revenues for the three months ended March 31, 2018. This makes us susceptible to demand for retail rental space and subject to the risks associated with an investment in real estate with a concentration of tenants in the retail industry. Furthermore, tenants in the office industry accounted for 33.2% of total revenues for the three months ended March 31, 2018. This makes us susceptible to demand for office rental space and subject to the risks associated with an investment in real estate with a concentration of tenants in the office industry. For the three months ended March 31, 2018 and 2017, no tenant accounted for more than 10% of our total rental revenue.

NOTE 12. OPERATING LEASES

Our leases with office, retail, mixed-use and residential tenants are classified as operating leases. Leases at our office and retail properties and the retail portion of our mixed-use property generally range from three to ten years (certain leases with anchor tenants may be longer), and in addition to minimum rents, usually provide for cost recoveries for the tenant's share of certain operating costs and also may include percentage rents based on the tenant's level of sales achieved. Leases on apartments generally range from 7 to 15 months, with a majority having 12-month lease terms. Rooms at the hotel portion of our mixed-use property are rented on a nightly basis.

As of March 31, 2018, minimum future rentals from noncancelable operating leases, before any reserve for uncollectible amounts and assuming no early lease terminations, at our office and retail properties and the retail portion of our mixed-use property are as follows (in thousands):

Year Ending December 31,	
2018 (nine months ending December 31, 2018)	$130,747
2019	159,736
2020	139,343
2021	116,692
2022	97,455
Thereafter	241,894
Total	$885,867

The above future minimum rentals exclude residential leases, which typically have a term of 12 months or less, and exclude the hotel, as rooms are rented on a nightly basis.

NOTE 13. COMPONENTS OF RENTAL INCOME AND EXPENSE

The principal components of rental income are as follows (in thousands):

	Three Months Ended March 31,	
	2018	2017
Minimum rents		
Retail	$19,654	$18,534
Office	23,306	23,122
Multifamily	11,486	7,235
Mixed-use	2,825	2,561
Cost reimbursement	8,342	7,888
Percentage rent	436	455
Hotel revenue	9,783	9,865
Other	369	380
Total rental income	$76,201	$70,040

Minimum rents include $(0.8) million and $0.2 million for the three months ended March 31, 2018 and 2017, respectively, to recognize minimum rents on a straight-line basis. In addition, net amortization of above and below market leases included in minimum rents were $0.7 million and $0.9 million for the three months ended March 31, 2018 and 2017, respectively.

The principal components of rental expenses are as follows (in thousands):

	Three Months Ended March 31,	
	2018	2017
Rental operating	$8,660	$8,073
Hotel operating	6,032	6,551
Repairs and maintenance	3,001	2,531
Marketing	412	436
Rent	794	757
Hawaii excise tax	1,033	1,025
Management fees	488	486
Total rental expenses	$20,420	$19,859

NOTE 14. OTHER INCOME, NET

The principal components of other income, net, are as follows (in thousands):

	Three Months Ended March 31,	
	2018	2017
Interest and investment income	$140	$147
Income tax benefit	65	163
Other non-operating income	4	—
Total other income, net	$209	$310

NOTE 15. RELATED PARTY TRANSACTIONS

We maintain a workers' compensation insurance policy with Insurance Company of the West, a California corporation ("ICW"), which is an insurance company majority owned and controlled by Ernest Rady, our Chief Executive Officer, President and Chairman of the Board. The workers' compensation policy was renewed on July 1, 2016 and the premium was approximately $0.2 million for the period from July 1, 2016 through July 1, 2017. We renewed this policy with ICW during the second quarter of 2017 and the premium is approximately $0.2 million for the period from July 1, 2017 through July 1, 2018.

During the first quarter of 2018, we signed a lease agreement with EDisability, LLC, an entity majority owned and controlled by Mr. Rady, for office space at Torrey Reserve Campus. Rent commences on June 1, 2018 for an initial lease term of five years at an average annual rental rate of $0.2 million. Rental revenue recognized on the lease will be included in rental income on the statements of comprehensive (loss) income.

The Waikiki Beach Walk entities have a 47.7% investment in WBW CHP LLC, an entity that was formed to, among other things, construct a chilled water plant to provide air conditioning to the property and other adjacent facilities. The operating expenses of WBW CHP LLC are recovered through reimbursements from its members, and reimbursements to WBW CHP LLC of $0.3 million and $0.3 million for the three months ended March 31, 2018 and 2017, respectively, are included in rental expenses on the statements of comprehensive (loss) income.

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American Assets Trust, Inc. and American Assets Trust, L.P.
Notes to Consolidated Financial Statements—(Continued)
March 31, 2018
(Unaudited)

NOTE 16. SEGMENT REPORTING
Segment information is prepared on the same basis that our management reviews information for operational decision-making purposes. We operate in four business segments: the acquisition, redevelopment, ownership and management of retail real estate, office real estate, multifamily real estate and mixed-use real estate. The products for our retail segment primarily include rental of retail space and other tenant services, including tenant reimbursements, parking and storage space rental. The products for our office segment primarily include rental of office space and other tenant services, including tenant reimbursements, parking and storage space rental. The products for our multifamily segment include rental of apartments and other tenant services. The products of our mixed-use segment include rental of retail space and other tenant services, including tenant reimbursements, parking and storage space rental and operation of a 369-room all-suite hotel.
We evaluate the performance of our segments based on segment profit, which is defined as property revenue less property expenses. We do not use asset information as a measure to assess performance and make decisions to allocate resources. Therefore, depreciation and amortization expense is not allocated among segments. General and administrative expenses, interest expense, depreciation and amortization expense and other income and expense are not included in segment profit as our internal reporting addresses these items on a corporate level.
Segment profit is not a measure of operating income or cash flows from operating activities as measured by GAAP, and it is not indicative of cash available to fund cash needs and should not be considered an alternative to cash flows as a measure of liquidity. Not all companies calculate segment profit in the same manner. We consider segment profit to be an appropriate supplemental measure to net income because it assists both investors and management in understanding the core operations of our properties.

The following table represents operating activity within our reportable segments (in thousands):

	Three Months Ended March 31,	
	2018	2017
Total Retail		
Property revenue	$26,157	$24,791
Property expense	(6,811)	(6,691)
Segment profit	19,346	18,100
Total Office		
Property revenue	26,770	25,990
Property expense	(8,013)	(7,801)
Segment profit	18,757	18,189
Total Multifamily		
Property revenue	12,424	7,891
Property expense	(4,997)	(3,211)
Segment profit	7,427	4,680
Total Mixed-Use		
Property revenue	15,381	15,120
Property expense	(9,145)	(9,692)
Segment profit	6,236	5,428
Total segments' profit	$51,766	$46,397

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American Assets Trust, Inc. and American Assets Trust, L.P.
Notes to Consolidated Financial Statements—(Continued)
March 31, 2018
(Unaudited)

The following table is a reconciliation of segment profit to net (loss) income attributable to stockholders (in thousands):

	Three Months Ended March 31,	
	2018	2017
Total segments' profit	$51,766	$46,397
General and administrative	(5,567)	(5,082)
Depreciation and amortization	(33,279)	(17,986)
Interest expense	(13,820)	(13,331)
Other income, net	209	310
Net (loss) income	(691)	10,308
Net loss (income) attributable to restricted shares	72	(60)
Net loss (income) attributable to unitholders in the Operating Partnership	166	(2,861)
Net (loss) income attributable to American Assets Trust, Inc. stockholders	$(453)	$7,387

The following table shows net real estate and secured note payable balances for each of the segments (in thousands):

	March 31, 2018	December 31, 2017
Net Real Estate		
Retail	$644,573	$ 658,654
Office	809,621	813,121
Multifamily	421,101	424,044
Mixed-Use	179,687	180,888
	$2,054,982	$ 2,076,707
Secured Notes Payable [(1)]		
Retail	$35,552	$ 35,737
Office	170,221	170,408
Multifamily	—	73,744
Mixed-Use	—	—
	$205,773	$ 279,889

(1) Excludes debt issuance costs of $0.3 million for each of the periods ending March 31, 2018 and December 31, 2017, respectively.

Capital expenditures for each segment for the three months ended March 31, 2018 and 2017 were as follows (in thousands):

	Three Months Ended March 31,	
	2018	2017
Capital Expenditures [(1)]		
Retail	$2,229	$1,246
Office	7,373	6,360
Multifamily	1,609	459
Mixed-Use	154	90
	$11,365	$8,155

(1) Capital expenditures represent cash paid for capital expenditures during the period and include leasing commissions paid.

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ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements

The following discussion should be read in conjunction with the consolidated financial statements and notes thereto appearing elsewhere in this report. We make statements in this report that are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 (set forth in Section 27A of the Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act). 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, demographics and results of operations are forward-looking statements. You can identify forward-looking statements by the use of forward-looking terminology such as “believes,” “expects,” “may,” “will,” “should,” “seeks,” “approximately,” “intends,” “plans,” “pro forma,” “estimates” or “anticipates” or 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.

Forward-looking statements involve numerous risks and uncertainties and you should not rely on them as predictions of future events. Forward-looking statements depend on assumptions, data or methods which may be incorrect or imprecise and we may not be able to realize them. 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;
- our failure to generate sufficient cash flows to service our outstanding indebtedness;
- defaults on, early terminations of or non-renewal of leases by tenants, including significant tenants;
- difficulties in identifying properties to acquire and completing acquisitions;
- difficulties in completing dispositions;
- our failure to successfully operate acquired properties and operations;
- our inability to develop or redevelop our properties due to market conditions;
- fluctuations in interest rates and increased operating costs;
- risks related to joint venture arrangements;
- our failure to obtain necessary outside financing;
- on-going litigation;
- general economic conditions;
- financial market fluctuations;
- risks that affect the general retail, office, multifamily and mixed-use environment;
- the competitive environment in which we operate;
- decreased rental rates or increased vacancy rates;
- conflicts of interests with our officers or directors;
- lack or insufficient amounts of insurance;
- environmental uncertainties and risks related to adverse weather conditions and natural disasters;
- other factors affecting the real estate industry generally;
- limitations imposed on our business and our ability to satisfy complex rules in order for us to continue to qualify as a real estate investment trust, or REIT, for U.S. federal income tax purposes; and
- changes in governmental regulations or interpretations thereof, such as real estate and zoning laws and increases in real property tax rates and taxation of REITs.

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,

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new information, data or methods, future events or other changes. For a further discussion of these and other factors, see the section entitled “Item 1A. Risk Factors” contained herein and in our annual report on Form 10-K for the year ended December 31, 2017.

Overview

References to “we,” “our,” “us” and “our company” refer to American Assets Trust, Inc., a Maryland corporation, together with our consolidated subsidiaries, including American Assets Trust, L.P., a Maryland limited partnership, of which we are the sole general partner and which we refer to in this report as our Operating Partnership.

We are a full service, vertically integrated and self-administered REIT that owns, operates, acquires and develops high quality retail, office, multifamily and mixed-use properties in attractive, high-barrier-to-entry markets in Southern California, Northern California, Oregon, Washington, Texas and Hawaii. As of March 31, 2018, our portfolio was comprised of twelve retail shopping centers; seven office properties; a mixed-use property consisting of a 369-room all-suite hotel and a retail shopping center; and six multifamily properties. Additionally, as of March 31, 2018, we owned land at four of our properties that we classified as held for development and/or construction in progress. Our core markets include San Diego; the San Francisco Bay Area; Portland, Oregon; Bellevue, Washington; and Oahu, Hawaii. We are a Maryland corporation formed on July 16, 2010 to acquire the entities owning various controlling and noncontrolling interests in real estate assets owned and/or managed by Ernest S. Rady or his affiliates, including the Ernest Rady Trust U/D/T March 13, 1983, or the Rady Trust, and did not have any operating activity until the consummation of our initial public offering on January 19, 2011. Our Company, as the sole general partner of our Operating Partnership, has control of our Operating Partnership and owned 73.2% of our Operating Partnership as of March 31, 2018. Accordingly, we consolidate the assets, liabilities and results of operations of our Operating Partnership.

Critical Accounting Policies

We identified certain critical accounting policies that affect certain of our more significant estimates and assumptions used in preparing our consolidated financial statements in our annual report on Form 10-K for the year ended December 31, 2017. We have not made any material changes to these policies during the periods covered by this report, other than those described in Footnote 1.

Same-store

We have provided certain information on a total portfolio, same-store and redevelopment same-store basis. Information provided on a same-store basis includes the results of properties that we owned and operated for the entirety of both periods being compared except for properties for which significant redevelopment or expansion occurred during either of the periods being compared, properties under development, properties classified as held for development and properties classified as discontinued operations. Information provided on a redevelopment same-store basis includes the results of properties undergoing significant redevelopment for the entirety or portion of both periods being compared. Same-store and redevelopment same-store is considered by management to be important measures because they assist in eliminating disparities due to the development, acquisition or disposition of properties during the particular period presented, and thus provides a more consistent performance measure for the comparison of the Company's stabilized and redevelopment properties, as applicable. Additionally, redevelopment same-store is considered by management to be an important measure because it assists in evaluating the timing of the start and stabilization of our redevelopment opportunities and the impact that these redevelopments have in enhancing our operating performance.

While there is judgment surrounding changes in designations, we typically reclassify significant development, redevelopment or expansion properties into same-store properties once they are stabilized. Properties are deemed stabilized typically at the earlier of (i) reaching 90% occupancy or (ii) four quarters following a property's inclusion in operating real estate. We typically remove properties from same-store properties when the development, redevelopment or expansion has or is expected to have a significant impact on the property's annualized base rent, occupancy and operating income within the calendar year. Our evaluation of significant impact related to development, redevelopment or expansion activity is based on quantitative and qualitative measures including, but not limited to the following: the total budgeted cost of planned construction activity compared to the property’s annualized base rent, occupancy and property operating income within the calendar year; percentage of development, redevelopment or expansion square footage to total property square footage; and the ability to maintain historic occupancy and rental rates. In consideration of these measures, we generally remove properties from same-store properties when we see a decline in a property's annualized base rent, occupancy and operating income within the calendar year as a direct result of ongoing redevelopment, development or expansion activity. Acquired properties are classified

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into same-store properties once we have owned such properties for the entirety of comparable period(s) and the properties are not under significant development or expansion.

Below is a summary of our same-store composition for the three months ended March 31, 2018 and 2017. For the three months ended March 31, 2018, Waikele Center was transferred out of same-store properties due to significant redevelopment activity. For the three months ended March 31, 2018, Pacific Ridge Apartments and Gateway Marketplace were classified as non-same-store properties as they were acquired on April 28, 2017 and July 6, 2017, respectively, when compared to the designations for the three months ended March 31, 2017. Torrey Reserve Campus, Hassalo on Eighth - Retail and Hassalo on Eighth - Multifamily were reclassified to same-store properties when compared to the designations for the three months ended March 31, 2017 as the entities became stabilized after their construction periods.

In our determination of same-store and redevelopment same-store properties for the three months ended March 31, 2018, Waikele Center has been identified as a same-store redevelopment property due to significant construction activity. Retail same-store net operating income increased approximately 2.9% for the three months ended March 31, 2018 compared to the same period in 2017. Retail redevelopment same-store net operating income increased approximately 2.8% for the three months ended March 31, 2018 compared to the same period in 2017.

	Three Months Ended March 31,	
	2018	2017
Same-Store	23	21
Non-Same Store	3	3
Total Properties	26	24
Redevelopment Same-Store	24	22
Total Development Properties	4	4

Outlook

We seek growth in earnings, funds from operations and cash flows primarily through a combination of the following: growth in our same-store portfolio, growth in our portfolio from property development and redevelopments and expansion of our portfolio through property acquisitions. Our properties are located in some of the nation's most dynamic, high-barrier-to-entry markets primarily in Southern California, Northern California, Oregon, Washington and Hawaii, which allow us to take advantage of redevelopment opportunities that enhance our operating performance through renovation, expansion, reconfiguration and/or retenanting. We evaluate our properties on an ongoing basis to identify these types of opportunities.

We intend to opportunistically pursue the development of future phases of Lloyd District Portfolio based on, among other things, market conditions and our evaluation of whether such opportunities would generate appropriate risk-adjusted financial returns. Our redevelopment and development opportunities are subject to various factors, including market conditions and may not ultimately come to fruition.

We continue to review acquisition opportunities in our primary markets that would complement our portfolio and provide long-term growth opportunities. Some of our acquisitions do not initially contribute significantly to earnings growth; however, we believe they provide long-term re-leasing growth, redevelopment opportunities and other strategic opportunities. Any growth from acquisitions is contingent upon our ability to find properties that meet our qualitative standards at prices that meet our financial hurdles. Changes in interest rates may affect our success in achieving earnings growth through acquisitions by affecting both the price that must be paid to acquire a property, as well as our ability to economically finance a property acquisition. Generally, our acquisitions are initially financed by available cash, mortgage loans and/or borrowings under our revolving line of credit, which may be repaid later with funds raised through the issuance of new equity or new long-term debt.

Leasing

Our same-store growth is primarily driven by increases in rental rates on new leases and lease renewals and changes in portfolio occupancy. Over the long-term, we believe that the infill nature and strong demographics of our properties provide us with a strategic advantage, allowing us to maintain relatively high occupancy and increase rental rates. We have continued to see signs of improvement for many of our tenants, as well as increased interest from prospective tenants for our spaces. While

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there can be no assurance that these positive signs will continue, we remain cautiously optimistic regarding the improved trends we have seen over the past few years. We believe the locations of our properties and diverse tenant base mitigate the potentially negative impact of the current economic environment. However, any reduction in our tenants' abilities to pay base rent, percentage rent or other charges will adversely affect our financial condition and results of operations.

During the three months ended March 31, 2018, we signed 22 retail leases for a total of 47,468 square feet of retail space including 43,241 square feet of comparable space leases (leases for which there was a prior tenant), at an average rental rate decrease on a cash basis of 4.2% and an average rental rate increase on a GAAP basis of 7.7%. New retail leases for comparable spaces were signed for 8,077 square feet at an average rental rate decrease on a cash and GAAP basis of 21.8% and 14.8%, respectively. Renewals for comparable retail spaces were signed for 35,164 square feet at an average rental rate increase on a cash basis of 1.7% and an average rental rate increase on a GAAP basis of 15.5%. Tenant improvements and incentives were $46.68 per square foot of retail space for comparable new leases for the three months ended March 31, 2018, mainly attributed to tenants at Carmel Mountain Plaza.

During the three months ended March 31, 2018, we signed 23 office leases for a total of 245,081 square feet of office space including 207,056 square feet of comparable space leases, at an average rental rate increase on a cash and GAAP basis of 11.6% and 29.8%, respectively. New office leases for comparable spaces were signed for 120,813 square feet at an average rental rate increase on a cash and GAAP basis of 21.9% and 46.6%, respectively. Renewals for comparable office spaces were signed for 86,243 square feet at an average rental rate increase on a cash and GAAP basis of 3.0% and 16.1%, respectively. Tenant improvements and incentives were $78.76 per square foot of office space for comparable new leases for the three months ended March 31, 2018, mainly attributed to tenants at City Center Bellevue and the Landmark at One Market.

The rental increases associated with comparable spaces generally include all leases signed in arms-length transactions reflecting market leverage between landlords and tenants during the period. The comparison between average rent for expiring leases and new leases is determined by including minimum rent and percentage rent paid on the expiring lease and minimum rent and, in some instances, projections of first lease year percentage rent, to be paid on the new lease. In some instances, management exercises judgment as to how to most effectively reflect the comparability of spaces reported in this calculation. The change in rental income on comparable space leases is impacted by numerous factors including current market rates, location, individual tenant creditworthiness, use of space, market conditions when the expiring lease was signed, capital investment made in the space and the specific lease structure. Tenant improvements and incentives include the total dollars committed for the improvement of a space as it relates to a specific lease, but may also include base-building costs (i.e. expansion, escalators or new entrances) which are required to make the space leasable. Incentives include amounts paid to tenants as an inducement to sign a lease that do not represent building improvements.

The leases signed in 2018 generally become effective over the following year, though some may not become effective until 2019 and beyond. Further, there is risk that some new tenants will not ultimately take possession of their space and that tenants for both new and renewal leases may not pay all of their contractual rent due to operating, financing or other matters. However, we believe that these increases do provide information about the tenant/landlord relationship and the potential fluctuations we may achieve in rental income over time.

Through the remainder of 2018, we believe our leasing volume will be in-line with our historical averages and result in overall positive increases in rental income. However, changes in rental income associated with individual signed leases on comparable spaces may be positive or negative, and we can provide no assurance that the rents on new leases will continue to increase at the above disclosed levels, if at all.

Capitalized Costs

Certain external and internal costs directly related to the development and redevelopment of real estate, including pre-construction costs, real estate taxes, insurance, interest, construction costs and salaries and related costs of personnel directly involved, are capitalized. We capitalize costs under development until construction is substantially complete and the property is held available for occupancy. The determination of when a development project is substantially complete and when capitalization must cease involves a degree of judgment. We consider a construction project as substantially complete and held available for occupancy upon the completion of landlord-owned tenant improvements or when the lessee takes possession of the unimproved space for construction of its own improvements, but not later than one year from cessation of major construction activity. We cease capitalization on the portion substantially completed and occupied or held available for occupancy, and capitalize only those costs associated with any remaining portion under construction.

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We capitalized external and internal costs related to both development and redevelopment activities combined of $0.7 million and $2.5 million for the three months ended March 31, 2018 and 2017, respectively.

We capitalized external and internal costs related to other property improvements combined of $8.7 million and $5.3 million for the three months ended March 31, 2018 and 2017, respectively.

Interest costs on developments and major redevelopments are capitalized as part of developments and redevelopments not yet placed in service. Capitalization of interest commences when development activities and expenditures begin and end upon completion, which is when the asset is ready for its intended use as noted above. We make judgments as to the time period over which to capitalize such costs and these assumptions have a direct impact on net income because capitalized costs are not subtracted in calculating net income. If the time period for capitalizing interest is extended, however, more interest is capitalized, thereby decreasing interest expense and increasing net income during that period. We capitalized interest costs related to development activities of $0.5 million and $0.4 million for the three months ended March 31, 2018 and 2017, respectively.

Results of Operations

For our discussion of results of operations, we have provided information on a total portfolio and same-store basis.

Comparison of the three months ended March 31, 2018 to the three months ended March 31, 2017

The following summarizes our consolidated results of operations for the three months ended March 31, 2018 compared to our consolidated results of operations for the three months ended March 31, 2017. As of March 31, 2018, our operating portfolio was comprised of 26 retail, office, multifamily and mixed-use properties with an aggregate of approximately 5.9 million rentable square feet of retail and office space, including the retail portion of our mixed-use property, 2,112 residential units (including 122 RV spaces) and a 369-room hotel. Additionally, as of March 31, 2018, we owned land at four of our properties that we classified as held for development and/or construction in progress. As of March 31, 2017, our operating portfolio was comprised of 24 retail, office, multifamily and mixed-use properties with an aggregate of approximately 5.9 million rentable square feet of retail and office space, including the retail portion of our mixed-use property, 1,579 residential units (including 122 RV spaces) and a 369-room hotel. Additionally, as of March 31, 2017, we owned land at four of our properties that we classified as held for development and/or construction in progress.

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The following table sets forth selected data from our unaudited consolidated statements of comprehensive (loss) income for the three months ended March 31, 2018 and 2017 (dollars in thousands):

	Three Months Ended March 31,		Change	%
	2018	2017		
Revenues				
Rental income	$76,201	$70,040	$6,161	9 %
Other property income	4,531	3,752	779	21