

Piedmont Office Realty Trust, Inc.
Form 10-K
February 17, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(Mark One)

Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the fiscal year ended December 31, 2015

or
 Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from to to
Commission file number 001-34626

PIEDMONT OFFICE REALTY TRUST, INC.
(Exact name of registrant as specified in its charter)

Maryland 58-2328421
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification Number)

11695 Johns Creek Parkway Ste. 350, Johns Creek, Georgia 30097
(Address of principal executive offices) (Zip Code)
(770) 418-8800
Registrant's telephone number, including area code

Securities registered pursuant to Section 12 (b) of the Act:
Title of each class Name of exchange on which registered
COMMON STOCK NEW YORK STOCK EXCHANGE

Securities registered pursuant to Section 12 (g) of the Act:
None
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.
Yes No

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

Yes No

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

Yes No

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Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company (as defined in Rule 12b-2 of the Act).

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

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

Yes No

As of June 30, 2015, the aggregate market value of the common stock of Piedmont Office Realty Trust, Inc., held by non-affiliates was \$2,654,544,041 based on the closing price as reported on the New York Stock Exchange. As of February 16, 2016, 145,063,043 shares of common stock were outstanding.

Documents Incorporated by Reference:

Registrant incorporates by reference portions of the Piedmont Office Realty Trust, Inc. Definitive Proxy Statement for the 2016 Annual Meeting of Stockholders (Items 10, 11, 12, 13, and 14 of Part III) to be filed no later than April 30, 2016.

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Certain statements contained in this Form 10-K may constitute forward-looking statements within the meaning of the federal securities laws. In addition, Piedmont Office Realty Trust, Inc. ("Piedmont"), or its executive officers on Piedmont's behalf, may from time to time make forward-looking statements in reports and other documents Piedmont files with the Securities and Exchange Commission or in connection with other written or oral statements made to the press, potential investors, or others. Statements regarding future events and developments and Piedmont's future performance, as well as management's expectations, beliefs, plans, estimates, or projections relating to the future, are forward-looking statements within the meaning of these laws. Forward-looking statements include statements preceded by, followed by, or that include the words "may," "will," "expect," "intend," "anticipate," "estimate," "believe," "con" or other similar words. Examples of such statements in this report include descriptions of our real estate, financing, and operating objectives; discussions regarding future dividends and share repurchases; and discussions regarding the potential impact of economic conditions on our real estate and lease portfolio.

These statements are based on beliefs and assumptions of Piedmont's management, which in turn are based on information available at the time the statements are made. Important assumptions relating to the forward-looking statements include, among others, assumptions regarding the demand for office space in the markets in which Piedmont operates, competitive conditions, and general economic conditions. These assumptions could prove inaccurate. The forward-looking statements also involve risks and uncertainties, which could cause actual results to differ materially from those contained in any forward-looking statement. Many of these factors are beyond Piedmont's ability to control or predict. Such factors include, but are not limited to, the following:

- Economic, regulatory, and/or socio-economic changes (including accounting standards) that impact the real estate market generally, or that could affect patterns of use of commercial office space, may cause our operating results to suffer and decrease the value of our real estate properties;
- The impact of competition on our efforts to renew existing leases or re-let space on terms similar to existing leases;
- Changes in the economies and other conditions affecting the office sector in general and the specific markets in which we operate, particularly in Chicago, Washington, D.C., and the New York metropolitan area, where we have high concentrations of office properties;
- Lease terminations or lease defaults, particularly by one of our large lead tenants;
 - Adverse market and economic conditions may negatively affect us and could cause us to recognize impairment charges on both our long-lived assets or goodwill or otherwise impact our performance;
- The success of our real estate strategies and investment objectives, including our ability to identify and consummate suitable acquisitions and divestitures;
- The illiquidity of real estate investments could significantly impede our ability to respond to adverse changes in the performance of our properties;
- Acquisitions of properties may have unknown risks and other liabilities at the time of acquisition;
- Development and construction delays and resultant increased costs and risks may negatively impact our operating results;
- Our real estate development strategies may not be successful;
- Future terrorist attacks in the major metropolitan areas in which we own properties could significantly impact the demand for, and value of, our properties;
- Costs of complying with governmental laws and regulations;
- Additional risks and costs associated with directly managing properties occupied by government tenants;
- Future offerings of debt or equity securities may adversely affect the market price of our common stock;
- Changes in market interest rates may have an effect on the value of our common stock;
- Uncertainties associated with environmental and other regulatory matters;
- Potential changes in political environment and reduction in federal and/or state funding of our governmental tenants;
- We may be subject to litigation, which could have a material adverse effect on our financial condition;
-

Changes in tax laws impacting REITs and real estate in general, as well as Piedmont's ability to continue to qualify as a REIT under the Internal Revenue Code (the "Code"); and

Other factors, including the risk factors discussed under Item 1A. of this Annual Report on Form 10-K.

Management believes these forward-looking statements are reasonable; however, undue reliance should not be placed on any forward-looking statements, which are based on current expectations. Further, forward-looking statements speak only as of the date they are made, and management undertakes no obligation to update publicly any of them in light of new information or future events.

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PART I

ITEM 1. BUSINESS

General

Piedmont Office Realty Trust, Inc. ("Piedmont") (NYSE: PDM) is a Maryland corporation that operates in a manner so as to qualify as a real estate investment trust ("REIT") for federal income tax purposes and engages in the acquisition, development, management, and ownership of commercial real estate properties throughout the United States, including properties that are under construction, are newly constructed, or have operating histories. Piedmont was incorporated in 1997 and commenced operations in 1998. Piedmont conducts business primarily through Piedmont Operating Partnership, L.P. ("Piedmont OP"), a Delaware limited partnership, as well as performing the management of its buildings through two wholly-owned subsidiaries, Piedmont Government Services, LLC and Piedmont Office Management, LLC. Piedmont owns 99.9% of, and is the sole general partner of, Piedmont OP and as such, possesses full legal control and authority over the operations of Piedmont OP. The remaining 0.1% ownership interest of Piedmont OP is held indirectly by Piedmont through its wholly-owned subsidiary, Piedmont Office Holdings, Inc. ("POH"), the sole limited partner of Piedmont OP. Piedmont OP owns properties directly, through wholly-owned subsidiaries and through both consolidated and unconsolidated joint ventures. References to Piedmont herein shall include Piedmont and all of its subsidiaries, including Piedmont OP and its subsidiaries and joint ventures.

Operating Objectives and Strategy

Based on our December 31, 2015 equity market capitalization of \$2.7 billion, Piedmont is among the top ten largest office REITs in the United States based on comparison to the constituents of the Bloomberg U.S. Office REIT Index. As of December 31, 2015, we owned and operated 69 office properties, one redevelopment asset, two development assets and one office building through an unconsolidated joint venture. Slightly under 80% of our Annualized Lease Revenue (see definition below) is generated from select office sub-markets in the following cities: Atlanta, Boston, Chicago, Dallas, Minneapolis, New York, and Washington, D.C.

Our portfolio of primarily Class A commercial office buildings was 91.5% and 87.7% leased as of December 31, 2015 and 2014, respectively. As we typically lease to larger, credit-worthy corporate users, our average lease size is approximately 23,000 square feet and as of December 31, 2015, we had an average lease term remaining of slightly under seven years. Our tenant base is primarily comprised of investment grade or nationally recognized corporations or governmental agencies, with 70% of our Annualized Lease Revenue derived from such tenants. No tenant other than the U.S. government accounts for more than 5% of our Annualized Lease Revenue.

Headquartered in metropolitan Atlanta, Georgia, with regional and/or local management offices in each of our major markets, Piedmont values operational excellence and ranks first among REITs based on the number of buildings owned and managed with Building Owners and Managers Association ("BOMA") 360 designations. BOMA 360 is a program that evaluates six major areas of building operations and management and benchmarks a building's performance against industry standards. The achievement of such a designation recognizes excellence in building operations and management. We also have focused on environmental sustainability initiatives at our properties, and approximately 62% of our office portfolio (based on Annualized Lease Revenue) maintains Energy Star labels (recognizing the top 25% of commercial buildings in energy consumption efficiency) as of December 31, 2015. In addition to operational excellence, we focus on fostering long-term relationships with our high-credit quality, diverse tenant base as evidenced by our 74% tenant retention rate over the past ten years.

Our primary objectives are to maximize the risk-adjusted return to our stockholders by increasing cash flow from operations, achieving sustainable growth in Funds from Operations, growing net asset value, and realizing long-term

capital appreciation. We manage risk by owning almost exclusively Class A, geographically diverse office properties which are among the most desirable in their respective, select office submarkets. In addition to the creditworthiness of our tenants, we strive to ensure our tenants represent a broad spectrum of industry types with lease maturities that are laddered over many years. Operationally, we maintain a low leverage structure, utilizing primarily unsecured financing facilities, along with laddered maturities. We utilize a national buying platform of property management support services to ensure optimal pricing for landlord and tenant services, as well as for building best practices and sustainability standards. The strategies we intend to execute to achieve these objectives include:

Capitalizing on Acquisition/Investment Opportunities

Our overall acquisition/investment strategy focuses on properties in select submarkets within certain major U.S. office markets that are generally characterized by their diverse industry base, attractive supply and demand ratios, potential rent growth, and appeal to investors. We target the acquisition of high quality, Class A properties that are attractively priced below replacement

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value and that complement our existing portfolio from a risk management and diversification perspective with a concentration upon select submarkets where efficiencies can be gained and our market expertise can be maximized.

Proactive Asset Management, Leasing Capabilities and Property Management

Proactive asset and property management encompasses a number of operating initiatives designed to maximize occupancy and rental rates, including the following: devoting significant resources to building and cultivating our relationships with commercial real estate executives; maintaining local management offices in markets in which we have a significant presence; demonstrating our commitment to our tenants by maintaining the high quality of our properties; driving a significant volume of leasing transactions in a manner that provides optimal returns by using creative approaches, including early extension, lease wrap-arounds and restructurings. We manage portfolio risk by structuring lease expirations to avoid, among other things, having multiple leases expire in the same market in a relatively short period of time; applying our leasing and operational expertise in meeting the specialized requirements of federal, state and local government agencies to attract and retain these types of tenants; evaluating potential tenants based on third-party and internal assessments of creditworthiness; and using our purchasing power and market knowledge to reduce our operating costs and those of our tenants.

Recycling Capital Efficiently

We use our proven, disciplined capital recycling capabilities to maximize total return to our stockholders by selectively disposing of non-core assets and assets where returns appear to have been maximized, and redeploying the proceeds into new investment opportunities with higher overall return prospects.

Financing Strategy

We employ a conservative leverage strategy by maintaining a debt-to-gross assets ratio of between 30%-40%. To effectively manage our long-term leverage strategy, we continue to analyze various sources of debt capital to prudently ladder debt maturities and to determine which sources will be the most beneficial to our investment strategy at any particular point in time.

Use of Joint Ventures to Improve Returns and Mitigate Risk

We may enter into a few, select strategic joint ventures with third parties to acquire, develop, improve or dispose of properties, thereby reducing the amount of capital required by us to make investments, diversifying our sources of capital and allowing us to reduce the concentration of certain properties and/or markets without disrupting our operating performance or local operating capabilities.

Redevelopment and Repositioning of Properties

As circumstances warrant, we may redevelop or reposition properties within our portfolio including the creation of additional amenities for our tenants to increase both occupancy and rental rates and thereby improve returns on our invested capital.

Information Regarding Disclosures Presented

Annualized Lease Revenue ("ALR") is calculated by multiplying (i) rental payments (defined as base rent plus operating expense reimbursements, if payable by the tenant on a monthly basis under the terms of a lease that has been executed, but excluding (a) rental abatements and (b) rental payments related to executed but not commenced leases

for space that was covered by an existing lease), by (ii) 12. In instances in which contractual rents or operating expense reimbursements are collected on an annual, semi-annual, or quarterly basis, such amounts are multiplied by a factor of 1, 2, or 4, respectively, to calculate the annualized figure. For leases that have been executed but not commenced relating to un-leased space, ALR is calculated by multiplying (i) the monthly base rental payment (excluding abatements) plus any operating expense reimbursements for the initial month of the lease term, by (ii) 12. Unless stated otherwise, this measure excludes our one redevelopment asset, two development assets, and our one property held in an unconsolidated joint venture.

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Employees

As of December 31, 2015, we had 143 full-time employees, with 52 of our employees working in our corporate office located in metropolitan Atlanta, Georgia. Our remaining employees work in regional and/or local management offices located in Atlanta, Georgia; Boston, Massachusetts; Minneapolis, Minnesota; Washington, D.C.; Orlando, Florida; Dallas, Texas; Houston, Texas; Chicago, Illinois; Detroit, Michigan; metropolitan New York, New York and Los Angeles, California. These employees are involved in acquiring and developing properties, as well as performing asset and property management services for our real estate properties and tenants.

Competition

We compete for tenants for our high-quality assets in major U.S. markets by fostering strong tenant relationships and by providing quality customer service including; leasing, asset management, property management, and construction management services. As the competition for high-credit-quality tenants is intense, we may be required to provide rent abatements, incur charges for tenant improvements and other concessions, or we may not be able to lease vacant space timely, all of which may impact our results of operations. We compete with other buyers who are interested in properties we elect to acquire, which may affect the amount that we are required to pay for such properties or may ultimately result in our decision not to acquire such properties. We also compete with sellers of similar properties when we sell properties, which may determine the amount of proceeds we receive from the disposal, or which may result in our inability to dispose of such properties due to the lack of an acceptable return.

Financial Information About Industry Segments

Our current business consists primarily of owning, managing, operating, leasing, acquiring, developing, investing in, and disposing of office real estate assets. We internally evaluate all of our real estate assets as one operating segment, and, accordingly, we do not report segment information.

Concentration of Credit Risk

We are dependent upon the ability of our current tenants to pay their contractual rent amounts as the rents become due. The inability of a tenant to pay future rental amounts would have a negative impact on our results of operations. As of December 31, 2015, no individual tenant represents 10% or more of our future revenues under non-cancelable leases. Additionally, no individual tenant represented 10% or more of our revenues for the year ended December 31, 2015.

Other Matters

Piedmont has contracts with various governmental agencies, exclusively in the form of operating leases in buildings we own. See Item 1A. "Risk Factors" for further discussion of the risks associated with these contracts.

Additionally, as the owner of real estate assets, we are subject to environmental risks. See Item 1A. "Risk Factors" for further discussion of the risks associated with environmental concerns.

Web Site Address

Access to copies of each of our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statements, and other filings with the Securities and Exchange Commission (the "SEC"), including any amendments to such filings, may be obtained free of charge from the following Web site,

<http://www.piedmontreit.com>, or directly from the SEC's Web site at <http://www.sec.gov>. These filings are available promptly after we file them with, or furnish them to, the SEC.

ITEM 1A. RISK FACTORS

Risks Related to Our Business and Operations

Economic, regulatory, and/or socio-economic changes that impact the real estate market generally, or that could affect patterns of use of commercial office space, may cause our operating results to suffer and decrease the value of our real estate properties.

The investment returns available from equity investments in real estate depend on the amount of income earned and capital appreciation generated by the properties, as well as the expenses incurred in connection with the properties. If our properties do not generate income sufficient to meet operating expenses, including debt service and capital expenditures, then our ability to make distributions to our stockholders could be adversely affected. In addition, there are significant expenditures associated with an investment in real estate (such as mortgage payments, real estate taxes, and maintenance costs) that generally do not decline when circumstances reduce the income from the property. The following factors, among others, may adversely affect the operating performance and long- or short-term value of our properties:

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• changes in the national, regional, and local economic climate, particularly in markets in which we have a concentration of properties;

- local office market conditions such as employment rates and changes in the supply of, or demand for, space in properties similar to those that we own within a particular area;

• changes in the patterns of office use due to technological advances which may make telecommuting more prevalent;

• the attractiveness of our properties to potential tenants;

• changes in interest rates and availability of permanent mortgage funds that may render the sale of a property difficult or unattractive or otherwise reduce returns to stockholders;

• the financial stability of our tenants, including bankruptcies, financial difficulties, or lease defaults by our tenants;

• changes in operating costs and expenses, including costs for maintenance, insurance, and real estate taxes, and our ability to control rents in light of such changes;

• the need to periodically fund the costs to repair, renovate, and re-let space;

• earthquakes, tornadoes, hurricanes and other natural disasters, civil unrest, terrorist acts or acts of war, which may result in uninsured or under insured losses;

• changes in, or increased costs of compliance with, governmental regulations, including those governing usage, zoning, the environment, and taxes; and

• changes in accounting standards.

In addition, periods of economic slowdown or recession, rising interest rates, or declining demand for real estate could result in a general decrease in rents or an increased occurrence of defaults under existing leases, which would adversely affect our financial condition and results of operations. Any of the above factors may prevent us from generating sufficient cash flow or maintaining the value of our real estate properties.

We face considerable competition in the leasing market and may be unable to renew existing leases or re-let space on terms similar to the existing leases, or we may expend significant capital in our efforts to re-let space, which may adversely affect our operating results.

Every year, we compete with a number of other developers, owners, and operators of office and office-oriented, mixed-use properties to renew leases with our existing tenants and to attract new tenants. To the extent that we are able to renew leases that are scheduled to expire in the short-term or re-let such space to new tenants, heightened competition resulting from adverse market conditions may require us to utilize rent concessions and tenant improvements to a greater extent than we historically have. In addition, competition for credit worthy tenants is intense and we may have difficulty competing with competitors, especially those who have purchased properties at discounted prices allowing them to offer space at reduced rental rates.

If our competitors offer office accommodations at rental rates below current market rates or below the rental rates we currently charge our tenants, we may lose potential tenants, and we may be pressured to reduce our rental rates below those we currently charge in order to retain tenants upon expiration of their existing leases. Even if our tenants renew their leases or we are able to re-let the space, the terms and other costs of renewal or re-letting, including the cost of required renovations, increased tenant improvement allowances, leasing commissions, declining rental rates, and other potential concessions, may be less favorable than the terms of our current leases and could require significant capital expenditures. If we are unable to renew leases or re-let space in a reasonable time, or if rental rates decline or tenant improvement, leasing commissions, or other costs increase, our financial condition, cash flows, cash available for distribution, value of our common stock, and ability to satisfy our debt service obligations could be adversely affected.

Our rental revenues will be significantly influenced by the economies and other conditions of the office market in general and of the specific markets in which we operate, particularly in Washington, D.C., the New York metropolitan

area, and Chicago where we have high concentrations of office properties.

Because our portfolio consists of office properties, we are subject to risks inherent in investments in a single property type. This concentration exposes us to the risk of economic downturns in the office sector to a greater extent than if our portfolio also included other sectors of the real estate industry. Our properties located in Washington, D.C., New York and the Chicago metropolitan area account for approximately 19.7%, 12.1%, and 11.3% respectively, of our ALR. As a result, we are particularly susceptible to adverse market conditions in these particular areas, including the reduction in demand for office properties, industry slowdowns, governmental cut backs, relocation of businesses and changing demographics. Adverse economic or real estate developments in the markets in which we have a concentration of properties, or in any of the other markets in which we operate, or any decrease in demand for office space resulting from the local or national government and business climates, could adversely affect our rental revenues and operating results.

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We depend on tenants for our revenue, and accordingly, lease terminations and/or tenant defaults, particularly by one of our significant lead tenants, could adversely affect the income produced by our properties, which may harm our operating performance, thereby limiting our ability to make distributions to our stockholders.

The success of our investments materially depends on the financial stability of our tenants, any of whom may experience a change in their business at any time. As a result, our tenants may delay lease commencements, decline to extend or renew their leases upon expiration, fail to make rental payments when due, or declare bankruptcy. Any of these actions could result in the termination of the tenants' leases, or expiration of existing leases without renewal, and the loss of rental income attributable to the terminated or expired leases. In the event of a tenant default or bankruptcy, we may experience delays in enforcing our rights as a landlord and may incur substantial costs in protecting our investment and re-letting our property. If significant leases are terminated or defaulted upon, we may be unable to lease the property for the rent previously received or sell the property without incurring a loss. In addition, significant expenditures, related to mortgage payments, real estate taxes, insurance, and maintenance costs, are generally fixed and do not decrease when revenues at the related property decrease.

The occurrence of any of the situations described above, particularly if it involves one of our significant lead tenants, could seriously harm our operating performance. As of December 31, 2015, our most substantial non-U.S. governmental lead tenants, based on ALR, were State of New York (approximately 4.5%), US Bancorp (approximately 4.0%), Independence Blue Cross (approximately 3.3%) and GE (approximately 3.1%). The revenues generated by the properties lead tenants occupy are substantially dependent upon the financial condition of these tenants and, accordingly, any event of bankruptcy, insolvency, or a general downturn in the business of any of these tenants may result in the failure or delay of such tenant's rental payments, which may have a substantial adverse effect on our operating performance.

Some of our leases provide tenants with the right to terminate their leases early, which could have an adverse effect on our cash flow and results of operations.

Certain of our leases permit our tenants to terminate their leases of all or a portion of the leased premises prior to their stated lease expiration dates under certain circumstances, such as providing notice by a certain date and, in many cases, paying a termination fee. In certain cases, such early terminations can be effectuated by our tenants with little or no termination fee being paid to us. As of December 31, 2015, approximately 4.5% of our ALR was comprised of leases with tenant-controlled options to exercise early termination rights (including contractions and terminations of whole leases) that could be effected during the subsequent twelve month period. Leases comprising approximately