

Edgar Filing: Equity Commonwealth - Form 10-K

Equity Commonwealth  
Form 10-K  
February 16, 2017

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM 10-K

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

For the fiscal year ended December 31, 2016  
OR

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

Commission File Number 1-9317

EQUITY COMMONWEALTH

(Exact Name of Registrant as Specified in Its Charter)

Maryland

04-6558834

(State or Other Jurisdiction of Incorporation or Organization) (IRS Employer Identification No.)

Two North Riverside Plaza, Suite 2100, Chicago, IL 60606

(Address of Principal Executive Offices) (Zip Code)

(312) 646-2800

(Registrant's Telephone Number, Including Area Code)

Securities registered pursuant to Section 12(b) of the Act:

Title Of Each Class

Name of Each Exchange On Which Registered

Common Shares of Beneficial Interest

New York Stock Exchange

6 1/2% Series D Cumulative Convertible Preferred Shares of Beneficial Interest

New York Stock Exchange

5.75% Senior Notes due 2042

New York Stock Exchange

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

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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting

Edgar Filing: Equity Commonwealth - Form 10-K

company” in Rule 12b-2 of the Exchange Act. (Check One):

Large accelerated filer  x

Accelerated filer  o

Non-accelerated filer  o

Smaller reporting company  o

(Do not check if a 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  o No  y

The aggregate market value of the voting common shares of beneficial ownership, \$0.01 par value, or common shares, of the registrant held by non-affiliates was \$3.6 billion based on the \$29.13 closing price per common share on the New York Stock Exchange on June 30, 2016.

Number of registrant’s common shares of beneficial interest, \$0.01 par value per share, outstanding as of February 13, 2017: 124,064,195.

**DOCUMENTS INCORPORATED BY REFERENCE**

Certain Information required by Items 10, 11, 12, 13 and 14 of Part III of this Annual Report on Form 10-K is incorporated herein by reference to the definitive Proxy Statement for the 2017 Annual Meeting of Shareholders, which Equity Commonwealth intends to file no later than 120 days after the end of its fiscal year ended December 31, 2016, or our definitive Proxy Statement.

---

#### FORWARD LOOKING STATEMENTS

Some of the statements contained in this Annual Report on Form 10-K constitute forward-looking statements within the meaning of the federal securities laws. Any forward-looking statements contained in this Annual Report on Form 10-K are intended to be made pursuant to the safe harbor provisions of 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. Forward-looking statements relate to expectations, beliefs, projections, future plans and strategies, anticipated events or trends and similar expressions concerning matters that are not historical facts. In particular, statements pertaining to our capital resources, portfolio performance and results of operations contain forward-looking statements. Likewise, all of our statements regarding anticipated growth in our funds from operations and anticipated market conditions are forward-looking statements. In some cases, you can identify forward-looking statements by the use of forward-looking terminology such as “may,” “will,” “should,” “expects,” “intends,” “plans,” “anticipates,” “believes,” “predicts,” or “potential” or the negative of these words and phrases or similar words or phrases which are predictions of or indicate future events or trends and which do not relate solely to historical matters. You can also identify forward-looking statements by discussions of strategy, plans or intentions.

The forward-looking statements contained in this Annual Report on Form 10-K reflect our current views about future events and are subject to numerous known and unknown risks, uncertainties, assumptions and changes in circumstances that may cause our actual results to differ significantly from those expressed in any forward-looking statement. We do not guarantee that the transactions and events described will happen as described (or that they will happen at all). We disclaim any obligation to publicly update or revise any forward-looking statement to reflect changes in underlying assumptions or factors, of new information, data or methods, future events or other changes. For a further discussion of these and other factors that could cause our future results to differ materially from any forward-looking statements, see the section entitled “Risk Factors” in this Annual Report on Form 10-K.

---

EQUITY COMMONWEALTH  
2016 FORM 10-K ANNUAL REPORT

Table of Contents

Part I

<u>Item 1. Business</u>	<u>1</u>
<u>Item 1A. Risk Factors</u>	<u>4</u>
<u>Item 1B. Unresolved Staff Comments</u>	<u>20</u>
<u>Item 2. Properties</u>	<u>21</u>
<u>Item 3. Legal Proceedings</u>	<u>22</u>
<u>Item 4. Mine Safety Disclosures</u>	<u>22</u>

Part II

<u>Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	<u>23</u>
<u>Item 6. Selected Financial Data</u>	<u>26</u>
<u>Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>28</u>
<u>Item 7A. Quantitative and Qualitative Disclosures About Market Risk</u>	<u>47</u>
<u>Item 8. Financial Statements and Supplementary Data</u>	<u>49</u>
<u>Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	<u>49</u>
<u>Item 9A. Controls and Procedures</u>	<u>49</u>
<u>Item 9B. Other Information</u>	<u>50</u>

Part III

<u>Item 10. Directors, Executive Officers and Corporate Governance</u>	<u>51</u>
<u>Item 11. Executive Compensation</u>	<u>51</u>
<u>Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	<u>51</u>
<u>Item 13. Certain Relationships and Related Transactions, and Director Independence</u>	<u>51</u>
<u>Item 14. Principal Accountant Fees and Services</u>	<u>51</u>

Part IV

<u>Item 15. Exhibits and Financial Statement Schedules</u>	<u>52</u>
<u>Signatures</u>	

## EXPLANATORY NOTE

References in this Annual Report on Form 10-K to the Company, EQC, we, us or our, refer to Equity Commonwealth and its consolidated subsidiaries as of December 31, 2016, unless the context indicates otherwise.

### PART I

#### Item 1. Business.

**The Company.** We are an internally managed and self-advised real estate investment trust, or REIT, engaged in the ownership and operation primarily of office buildings throughout the United States. We were formed in 1986 under Maryland law and we have elected to be taxed as a REIT under the Internal Revenue Code of 1986, as amended (the Code).

On November 10, 2016, we converted to what is commonly referred to as an umbrella partnership real estate investment trust, or UPREIT, structure. In connection with this conversion, the Company contributed substantially all of its assets to EQC Operating Trust, a Maryland real estate investment trust through which the Company conducts its business (the Operating Trust), and the Operating Trust assumed substantially all of the Company's liabilities pursuant to a contribution and assignment agreement between the Company and the Operating Trust.

The Company now conducts and intends to continue to conduct substantially all of its activities through the Operating Trust. The Company beneficially owned, directly and indirectly, 100.0% of the outstanding shares of beneficial interest, designated as units, in the Operating Trust (OP Units) as of December 31, 2016 and the Company is the sole trustee of the Operating Trust. As the sole trustee, the Company generally has the exclusive power under the declaration of trust of the Operating Trust to manage and conduct the business of the Operating Trust, subject to certain limited approval and voting rights of other holders of OP Units that may be admitted in the future.

At December 31, 2016, our portfolio included 33 properties, one land parcel and one property taken out of a service which is now classified as a land parcel, with a combined 16.1 million square feet for a total investment of \$2.9 billion at cost and a depreciated book value of \$2.1 billion. After our new Board of Trustees was elected in 2014, we brought on new executive officers and employees while transitioning from external management to internal management, after which we undertook a comprehensive review of our portfolio and our operations and developed a strategy that focused on disposing of a significant portion of our assets to reshape our portfolio to higher quality properties in better, long-term markets. In 2014, we sold 14 properties with a combined 2.8 million square feet for an aggregate gross sales price of \$215.9 million, excluding closing costs and mortgage debt repayments, and our entire stake of common shares of Select Income REIT and its consolidated subsidiaries (SIR) for \$704.8 million. Since that time, we have disposed of 121 properties and one land parcel through December 31, 2016, with a combined 26.9 million square feet for an aggregate gross sales price of \$3.3 billion, excluding closing costs. As a result of these dispositions, we have concentrated our portfolio, exiting 90 cities, 17 states and Australia.

We remain focused on creating value through proactive asset management and improving operating results, while evaluating opportunities to invest capital in high-quality assets in favorable markets that offer a compelling risk-reward profile. We have generated significant proceeds from dispositions and have a cash balance of \$2.1 billion as of December 31, 2016. The set of opportunities that we pursue in the future may include office as well as other property types in order to create a foundation for long-term growth.

As of December 31, 2016, we had 58 full-time employees. Our principal executive offices are located at Two North Riverside Plaza, Suite 2100, Chicago, Illinois 60606, and our telephone number is (312) 646-2800.

#### Policies with Respect to Certain Activities

The discussion below sets forth certain additional information regarding our investment, repositioning, disposition and financing policies. These policies are established by our Board of Trustees and may be changed by our Board of Trustees at any time without shareholder approval.

Investment Policies. In evaluating potential investments and asset sales, we consider various factors, including but not limited to the following:

the historical and projected rents received and likely to be received from the property;

1

---

the historical and expected operating expenses, including real estate taxes, incurred and expected to be incurred at the property;

the growth, tax and regulatory environments of the market in which the property is located;

the quality, experience and credit worthiness of the property's tenants;

occupancy and demand for similar properties in the same or nearby markets;

the construction quality, physical condition and design of the property, and expected capital expenditures that may be needed to be made to the property;

the location and type of property; and

the pricing of comparable properties as evidenced by recent market sales.

We have no policies which specifically limit the percentage of our assets which may be invested in any individual property, in any one type of property, in properties in one geographic area, in properties leased to any one tenant, in properties leased to an affiliated group of tenants, in real estate joint ventures, or in participating, or convertible or other types of mortgages. Further, we have in the past provided seller financing for properties we have sold and may do so again in the future.

In the past, we have considered the possibility of entering into mergers or strategic combinations with other companies. We may undertake such considerations in the future.

**Office Repositioning Strategy.** In December of 2016, our Board of Trustees adopted an office repositioning strategy to own and acquire, at a discount to replacement cost, high-quality multi-tenant assets in markets and sub-markets with favorable long-term supply and demand fundamentals. Our efforts in the office sector will primarily be focused on larger buildings in central business districts and major urban areas that offer an attractive quality of life, including opportunities for tenants to live and play in close proximity to where they work, with a preference for markets that have above average limitations on new supply.

**Disposition Strategy.** Prior to the adoption of the office repositioning strategy in December of 2016, we pursued and successfully implemented a disposition strategy adopted by our Board of Trustees. This plan resulted from a comprehensive review of our portfolio and operations after our transition from external management to internal management in 2014. To reshape our portfolio to higher quality assets, we sought to dispose of properties that had one or more of the following attributes:

assets that did not offer an opportunity to create a competitive advantage;

assets that were less than 150,000 square feet;

assets that were not office buildings;

assets that were not located in the U.S.; or

assets that produced a low cash yield or required significant capital expenditures.

Disposition decisions were made based on a number of factors including those set forth above and the following:

the proposed sale price; and

the existence of alternative sources, uses or needs for capital.

**Financing Policies.** Our credit agreement and our debt indenture and its supplements contain financial covenants that, among other things, restrict our ability to incur indebtedness and require us to maintain certain financial ratios and a minimum net worth. Our Board of Trustees may determine to seek additional capital through equity offerings, debt financings, retention of cash flows in excess of distributions to shareholders or a combination of these methods. Some of our properties are encumbered by mortgages. To the extent that our Board of Trustees decides to obtain additional debt financing, we may do so on an unsecured basis or a secured basis, subject to limitations in existing financing or other contractual arrangements; we may seek to obtain other lines of credit or to issue securities senior to our common and/or preferred shares, including preferred shares or debt securities which may be convertible into common shares or be accompanied by warrants to purchase common shares; or we may engage in transactions which involve a sale or other conveyance of properties to affiliated or unaffiliated entities. We may finance acquisitions by an exchange of properties, by borrowing under our credit facility, by assuming outstanding mortgage debt on the acquired properties, by the issuance of additional equity or debt securities or by using retained cash flow from operations which may exceed our earnings. The proceeds from any of our financings may be used to pay distributions,

to provide working capital, to refinance existing indebtedness or to finance acquisitions and expansions of existing or new properties. We may from time to time re-evaluate and modify our financing policies in light of then current

2

---



market conditions, relative availability and costs of debt and equity capital, the changing values of properties, growth and acquisition opportunities and other factors, and we may increase or decrease our ratio of debt to total capitalization.

**Competition.** Investing in and operating real estate is a highly competitive business. We compete against other REITs, numerous financial institutions, individuals and public and private companies who are actively engaged in this business. Also, we compete for tenants and investments based on a number of factors including pricing, underwriting criteria and reputation. Our ability to successfully compete is also impacted by economic and population trends, availability of acceptable investment opportunities, our ability to negotiate beneficial leasing and investment terms, availability and cost of capital and new and existing laws and regulations. Some of our competitors are dominant in selected geographic markets, including in markets in which we operate. Many of our competitors have greater financial and other resources than we have.

For additional information on competition and the risks associated with our business, please see "Risk Factors" in Part I, Item 1A of this Annual Report on Form 10-K.

**Environmental and Climate Change Matters.** Under various federal, state and local laws related to environmental, health and safety matters, owners and operators, including tenants of real estate may be subject to liabilities resulting from the presence of hazardous substances, waste or petroleum products at, on, under, or emanating from such property, including costs for investigating and remediating or removing hazardous substances present at or migrating from such properties, liabilities for property damage or personal injuries, natural resource damages, and costs and losses arising from property use restrictions or diminution in value. We, or our tenants, also may incur liability for failing to comply with environmental, health and safety laws. We do not believe that there are environmental conditions or issues at any of our properties that have had or will have a material adverse effect on us. However, no assurances can be given that conditions or issues are not present at our properties or that costs we may be required to incur in the future to remediate contamination or comply with environmental, health and safety laws will not have a material adverse effect on our business or financial condition.

We estimate the cost to remove hazardous substances or address environmental issues at some of our properties based in part on environmental surveys conducted on our properties.

Some of our properties have been or may be impacted by releases of hazardous substances or petroleum products. Such contamination may arise from a variety of sources, including historic uses of our properties for commercial or industrial purposes, spills of such materials at adjacent properties, or releases from tanks used on our properties to store petroleum or hazardous substances. In addition, certain of our properties are on sites upon which or are adjacent to or near other properties upon which others, including former owners or tenants, have engaged, or may in the future engage, in activities that may release petroleum products or other hazardous or toxic substances. Though we have reviewed these and our other properties for potential environmental liabilities, we cannot assure that we have identified all potential environmental liabilities.

Certain of our buildings contain asbestos. We believe any asbestos in our buildings is contained in accordance with current regulations. If we remove the asbestos or renovate or demolish these properties, certain environmental regulations govern the manner in which the asbestos must be handled and removed, which could result in increased costs.

For more information regarding environmental matters and their possible adverse impact on us, see "Risk Factors—Risks Related to Our Business—We could incur significant costs and liabilities with respect to environmental matters" in Part I, Item 1A of this Annual Report on Form 10-K.

The current political debate about climate change has resulted in various treaties, laws and regulations which are intended to limit carbon emissions. We believe these laws being enacted or proposed may cause energy costs at our properties to increase, but we do not expect the direct impact of these increases to be material to our results of operations because the increased costs either would be the responsibility of our tenants directly or in large part may be passed through by us to our tenants as additional lease payments. Although we do not believe it is likely in the foreseeable future, laws enacted to mitigate climate change may make some of our buildings obsolete or cause us to make material investments in our properties which could materially and adversely affect our financial condition. We

## Edgar Filing: Equity Commonwealth - Form 10-K

continuously study ways to improve the energy efficiency at all of our properties. For more information regarding climate change matters and their possible adverse impact on us, see "Risk Factors—Risks Related to Our Business—We may be adversely affected by laws, regulations or other issues related to climate change" in Part I, Item 1A of this Annual Report on Form 10-K.

3

---

### Information About Industry Segments

Our primary business is the ownership and operation of office properties, and we account for the operations of all our properties in one reporting segment, as further described in Note 17 of the Notes to Consolidated Financial Statements included in Part IV, Item 15 of this Annual Report on Form 10-K.

### Information About Geographic Areas

As of December 31, 2016 and 2015, all of our assets were located in the United States. We owned assets in Australia prior to the sale of these assets in June 2015. As of December 31, 2014, we had assets in Australia of \$252.0 million. For the years ended December 31, 2015 and 2014, we recognized revenues in Australia of \$12.7 million and \$30.1 million, respectively.

### Internet Website

Our internet website address is [www.eqcre.com](http://www.eqcre.com). Copies of our Corporate Governance Guidelines, Code of Business Conduct and Ethics and the charters of our Audit, Compensation and Nominating and Corporate Governance committees are posted on our website and may be obtained free of charge by writing to our Secretary, Equity Commonwealth, Two North Riverside Plaza, Suite 2100, Chicago, Illinois 60606. We make available, free of charge, on our website, our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to these reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, or the Exchange Act, as soon as reasonably practicable after these forms are filed with, or furnished to, the SEC. Any shareholder or other interested party who desires to communicate with our Board of Trustees, or our non-management Trustees, individually or as a group, may do so by contacting our investor relations department through our website. Our website address is included several times in this Annual Report on Form 10-K as a textual reference only and the information on the website is not incorporated by reference into this Annual Report on Form 10-K.

### RISK FACTORS

#### Item 1A. Risk Factors.

Our business faces many risks. The risks described below may not be the only risks we face but are the risks we know of that we believe may be material at this time. Additional risks that we do not yet know of, or that we currently think are immaterial, may also impair our business operations or financial results. If any of the events or circumstances described in the following risks occurs, our business, financial condition or results of operations could suffer and the trading price of our securities could decline. Investors and prospective investors should consider the following risks and the information contained under the heading "Forward Looking Statements" before deciding whether to invest in our securities.

#### Risks Related to Our Business

We may not be successful in repositioning our portfolio, which may reduce the size of our business and negatively affect our financial condition or results of operations.

We are focused on increasing the Company's exposure to high-quality, multi-tenant assets in markets with favorable long-term supply and demand fundamentals. Although we are seeking to reinvest the capital we have received from dispositions in a manner consistent with our office repositioning strategy, we cannot provide any assurances that we will be successful. During the time that we are looking for reinvestment opportunities, our financial condition and results of operations may be materially and adversely affected. While we are looking for reinvestment opportunities, our operating income is likely to be reduced, which may adversely affect our results of operations or decrease amounts available to be distributed to shareholders. Prior to any investment of proceeds from our completed dispositions, the market price of our common shares may fluctuate or decrease as a result of investors' perceptions of our ability to successfully capitalize on strategic opportunities in order to reposition our portfolio.

The ability of our management team to implement this repositioning strategy depends substantially on identifying and completing dispositions and acquisitions that meet our criteria. Specifically, our management team must successfully

identify and underwrite acquisitions that strengthen and augment (or establish) the Company's presence in markets that meet our criteria and acquire applicable properties at favorable prices in order to successfully deploy the capital received from the dispositions that have occurred in recent years and from any future dispositions. We are seeking to reinvest capital received from dispositions we complete but cannot provide any assurances that we will be successful. In addition, even if we are ultimately successful, it may take a long period of time before we are able to effectively implement our repositioning strategy.

Our office repositioning strategy may require dispositions on unfavorable terms or that result in expenses or reputational harm.

Our current business plan focuses on owning larger office buildings in central business districts and major urban areas in markets and sub-markets with favorable long-term supply and demand fundamentals. In order to execute this strategy, we will need to selectively dispose of certain assets, hold other assets and acquire new assets. We cannot be assured that we will be able to find attractive sale opportunities for assets we wish to dispose of in order to execute our repositioning strategy or that any sale will be completed in a timely manner, if at all. Our ability to continue to sell certain of our properties, and the prices we receive upon any such sales, may be negatively affected by many factors. In particular, these factors could arise from weakness in or the lack of an established market for a property, the illiquid nature of real estate assets, changes in the financial condition or prospects of prospective purchasers, a limited number of prospective purchasers in certain markets, increase in the cost of or lack of availability of debt, the number of competing properties on the market, a deterioration in current local, national or international economic conditions, and changes in laws, regulations or fiscal policies of jurisdictions in which the property is located. In addition, provisions of the Code relating to REITs may limit our ability to sell properties. See risk factor below “Risks Related to Our Taxation as a REIT—The tax on “prohibited transactions” may limit our ability to engage in transactions which would be treated as sales for U.S. federal income tax purposes.” For these reasons, we may be unable to sell certain of our properties for an extended period of time or at all, our business plan to sell certain of our properties may not succeed, and we may incur expenses and reputational harm.

We may be unable to identify and complete acquisitions consistent with our repositioning strategy on favorable terms or at all, which may inhibit our growth and have a material adverse effect on us.

We are evaluating the market of available properties and businesses and may acquire additional properties and businesses consistent with our office repositioning strategy. Our ability to acquire properties and businesses on favorable terms is subject to the following significant risks:

- we may be unable to identify attractive acquisition opportunities that satisfy the criteria of our repositioning strategy; we may be unable to acquire a desired property or business because of competition from other real estate investors
- with significant resources and/or access to capital, including both publicly traded REITs and institutional investment funds;
- we may experience conditions which delay or preclude the completion of acquisitions;
- even if we are able to acquire a desired property or business, competition from other potential acquirers may significantly increase the purchase price or result in other less favorable terms;
- even if we enter into agreements for the acquisition of a desired property or business, these agreements are subject to customary conditions to closing, including completion of due diligence investigations to our satisfaction, and we may incur significant expenses for properties or businesses we never actually acquire;
- we may be unable to finance acquisitions on favorable terms or at all; and
- we may acquire properties subject to liabilities and without any recourse, or with only limited recourse, with respect to unknown liabilities such as liabilities for clean-up of environmental contamination, claims by customers, vendors or other persons dealing with the former owners of the properties and claims for indemnification by general partners, directors, officers and others indemnified by the former owners of the properties.

Any inability to complete property or business acquisitions on favorable terms or at all may result in our inability to successfully implement our repositioning strategy, which could have a material adverse effect on us.

We may encounter unanticipated difficulties relating to acquired properties, which may inhibit our growth and have a material adverse effect on us.

Even if we are able to make acquisitions on favorable terms, we might encounter unanticipated difficulties and expenditures relating to any acquired properties. Newly acquired properties might require significant management attention that would otherwise be devoted to our ongoing business. We might never realize the anticipated benefits of our acquisitions. Notwithstanding pre-acquisition due diligence, we do not believe that it is possible to fully understand a property before it is owned and operated for an extended period of time. For example, we could acquire a property that contains undisclosed defects in design or construction. In addition, after our acquisition of a property, the market in which the acquired property is located may experience unexpected changes that adversely affect the property's value. The occupancy of properties that we acquire may decline during our ownership, and rents that are in effect at the time a property is acquired may decline thereafter. Also, our property operating costs for acquisitions may be higher than we anticipate and acquisitions of properties may not yield the

returns we expect and, if financed using debt or new equity issuances, may result in shareholder dilution. For these reasons, among others, our business plan to acquire additional properties may not succeed or may cause us losses. If we are unable to identify attractive opportunities to redeploy the capital received from the dispositions that occurred in recent years and any future dispositions, we may sell all of our remaining assets and wind down, liquidate or dissolve our Company, which may be a lengthy process, yield unexpected results and diminish or delay any potential distributions to our shareholders.

We are seeking opportunities to reinvest capital received from dispositions, but we cannot provide any assurances that we will be successful in making such investments. We are actively evaluating various strategies and one possibility is to decide to sell all or substantially all of our remaining assets and liquidate or sell the Company. No such decision has been made as of the date of this filing and we cannot predict the timing of making any such decision. In the event of a wind down, liquidation or dissolution of the Company, holders of our common shares may not realize the return on investment expected at the time they purchased our common shares.

Our reliance upon CBRE, Inc., or CBRE, for third party property management may have a negative effect on our financial condition and results of operations.

We have engaged CBRE to provide property management services for substantially all of our properties pursuant to a master property management agreement. The successful operation and management of our properties requires significant coordination between us and CBRE. Additionally, since the expiration of the initial term of our agreement with CBRE in September 2016, CBRE can terminate the property management agreement, as a whole or as to any one or more of our properties, without cause upon providing three months' notice, and we are permitted to terminate the property management agreement, as a whole or as to any one or more of our properties, without cause upon 60 days' notice. If we are unable to successfully coordinate with CBRE with respect to property management or the property management agreement with CBRE is terminated, in whole or in part, our operations could be disrupted, which may have a negative effect on our financial condition and results of operations.

We are currently dependent upon economic conditions relating to the commercial office real estate market, and adverse economic or regulatory developments in this market could materially and adversely affect our results of operations.

Our business is influenced by the economic and regulatory environment (such as business layoffs or downsizing, industry slowdowns, relocations of businesses, increases in real estate and other taxes, costs of complying with governmental regulations or increased regulation). Such adverse developments could materially reduce the value of our real estate portfolio and our rental revenues, and thus materially and adversely affect our ability to service current debt and to pay distributions to shareholders. If economic conditions in our market worsen or fail to grow at a sufficient pace, we may experience reduced demand from tenants for our properties. A significant economic downturn in our market could adversely affect our results of operations.

Future impairment charges could have a material adverse effect on our results of operations in the period for which the charge occurs.

We periodically evaluate the recoverability of the carrying values of each of the real estate assets that comprise our portfolio. In undertaking our portfolio reviews, we comprehensively review our portfolio to evaluate whether there are any indicators, including property operating performance and general market conditions, that the value of the real estate properties (including any related amortizable intangible assets or liabilities) may not be recoverable. In 2014, we determined that due to the shortening of the expected periods of ownership of a number of our assets, as a result of the disposition plan, it was necessary to reduce the net book value of a portion of the real estate assets in our portfolio to their estimated fair values. As a result, we recorded a loss on asset impairment for 34 properties of \$167.1 million

in 2014, to reflect the estimated fair values of those real estate assets in our portfolio that failed the recoverability test because their net book values exceeded their fair values. We reduced the aggregate carrying value of these properties from \$581.7 million to their estimated fair value of \$414.6 million. We recorded impairment charges of \$58.5 million and \$17.2 million during the years ended December 31, 2016 and 2015, respectively, based upon updated market information in accordance with our impairment analysis procedures. There can be no assurance that we will not take additional charges in the future related to the impairment of our assets.

As part of the evaluation of our portfolio, we compare the current carrying value of the asset to the estimated undiscounted cash flows that are directly associated with the use and ultimate disposition of the asset. Our estimated cash flows are based on several key assumptions, including rental rates, costs of tenant improvements, leasing commissions, anticipated hold periods, and assumptions regarding the residual value upon disposition, including the exit capitalization rate. These key assumptions are subjective in nature and could differ materially from actual results. Additionally, changes in our disposition



strategy or changes in the marketplace may alter the hold period of an asset or asset group, which may result in an impairment loss and such loss could be material to the Company's financial condition or operating performance. To the extent that the carrying value of the asset exceeds the estimated undiscounted cash flows, an impairment loss is recognized equal to the excess of carrying value over fair value. Any future impairment could have a material adverse effect on our results of operations in the period in which the charge is taken.

Additionally, the fair value of real estate assets is highly subjective and is determined through comparable sales information and other market data if available, or through use of an income approach such as the direct capitalization method or the discounted cash flow approach. Such cash flow projections consider factors, including expected future operating income, trends and prospects, as well as the effects of demand, competition and other factors, and therefore are subject to a significant degree of management judgment. In estimating the fair value of undeveloped land, we generally use market data and comparable sales information. These subjective assessments have a direct impact on our net income because recording an impairment charge results in an immediate negative adjustment to net income. Thus, our results of operations may be significantly affected by the subjective judgments of our management team as to the fair value of our properties.

If global market and economic conditions worsen or do not fully recover, our business, financial condition and results of operations could be adversely affected.

In the United States, market and economic conditions continue to be uncertain and challenging with modest growth. We are unable to predict with any certainty whether economic conditions will decline, remain stable or improve. If current economic conditions deteriorate, business layoffs, downsizing, industry slowdowns and other similar factors that affect our tenants could negatively impact commercial real estate fundamentals and result in lower occupancy, lower rental rates and declining values in our real estate portfolio. Additionally, the cost and availability of credit and the commercial real estate market generally may be adversely affected by persistent high levels of unemployment, insufficient consumer demand or confidence, the impacts of changes in the U.S. federal budgetary process, changes in regulatory environments and other macro-economic factors. Deteriorating economic conditions could also have an impact on our lenders or tenants, causing them to fail to meet their obligations to us. No assurances can be given that the current economic conditions will remain stable or improve, and if market and economic conditions weaken, our ability to lease our properties and increase or maintain rental rates may be affected, which would have a material adverse effect on our business, financial condition and results of operations.

We rely on the ability of our tenants to pay rent and would be harmed by their inability to do so.

Our performance depends on the ability of our tenants to fulfill their lease obligations by paying their rental payments in a timely manner. As a result, we would be harmed if one or more of our major tenants, or a number of our smaller tenants, were to experience financial difficulties, including bankruptcy, insolvency, or general downturn of business.

Significant competition for tenants and acquisition opportunities may reduce rents and increase acquisition costs which could materially and adversely affect our company.

All of our properties face competition for tenants. Some competing properties may be newer, better located or more attractive to tenants. Competing owners may offer available space at lower rents than we offer at our properties. This competition may affect our ability to attract and retain tenants and may reduce the rents we are able to charge.

In addition, we face significant competition for acquisition opportunities from other investors, including publicly traded and private REITs, numerous financial institutions, individuals and public and private companies. Because of competition, we may be unable to, or may pay a significantly increased purchase price to, acquire a desired property. Some of our competitors may have greater financial and management resources than we do.

When we renew leases or lease to new tenants our rents may decline and our expenses may increase and changes in tenants' requirements for leased space may adversely affect us.

When we renew leases or lease to new tenants we may receive less rent than we currently receive. Market conditions may require us to lower our rents to retain tenants. When we lease to new tenants or renew leases we may have to spend substantial amounts for leasing commissions, tenant improvements or tenant inducements. Many of our leases are for properties that are specially suited to the particular business of our tenants. Because these properties have been designed or physically modified for a particular tenant, if the current lease is terminated or not renewed, we may be required to renovate the property at substantial costs, decrease the rent we charge or provide other concessions in order to lease the property to another tenant. In general, tenants have been seeking to increase their space utilization under their leases, including reducing the amount of square footage per employee at leased properties, which may reduce the demand for leased space. If a significant number of such

events occur, our income and cash flow may materially decline and our ability to make regular distributions to our shareholders may be jeopardized.

We have substantial debt obligations which could materially and adversely affect our cost of operations.

As of December 31, 2016, we had \$1.1 billion in debt outstanding, which was 25.2% of our total book capitalization.

As a result, we are and expect to be subject to the risks normally associated with debt financing, including:

- that interest rates may rise;

- that our cash flow will be insufficient to make required payments of principal and interest;

- that any refinancing will not be on terms as favorable as those of our existing debt;

- that required payments on mortgages and on our other debt are not reduced if the economic performance of any property declines;

- that debt service obligations will reduce funds available for distribution to our shareholders;

- that any default on our debt, due to noncompliance with financial covenants or otherwise, could result in acceleration of those obligations;

- that we may be unable to refinance or repay the debt as it becomes due, and

- that if our degree of leverage is viewed unfavorably by lenders or potential joint venture partners, it could affect our ability to obtain additional financing.

If we default in paying any of our debts or honoring our debt covenants, it may create one or more cross defaults, our debts may be accelerated and we could be forced to liquidate our assets for less than the values we would receive in a more orderly process. Additionally, we may not be able to refinance or repay debt as it becomes due which may force us to refinance or to incur additional indebtedness at higher rates and additional cost or, in the extreme case, to sell assets or seek protection from our creditors under applicable law.

Mortgage debt obligations expose us to the possibility of foreclosure, which could result in the loss of our investment in a property or group of properties subject to mortgage debt.

Incurring mortgage and other secured debt obligations increases our risk of property losses because defaults on indebtedness secured by properties may result in foreclosure actions initiated by lenders and ultimately our loss of the property securing any loans for which we are in default. Any foreclosure on a mortgaged property or group of properties could adversely affect the overall value of our portfolio of properties. For tax purposes, a foreclosure of any of our properties that is subject to a nonrecourse mortgage loan would be treated as a sale of the property for a purchase price equal to the outstanding balance of the debt secured by the mortgage. If the outstanding balance of the debt secured by the mortgage exceeds our tax basis in the property, we would recognize taxable income on foreclosure, but would not receive any cash proceeds.

Our failure or inability to meet certain terms of our credit agreement, which includes our unsecured revolving credit facility and term loans, may prevent us from making distributions to our shareholders.

Our credit agreement includes various conditions to borrowings and various financial and other covenants, including covenants requiring us to maintain certain minimum debt service coverage and maximum leverage ratios, and events of default. We may not be able to satisfy all of these conditions or may default on some of these covenants for various reasons, including matters which are beyond our control. If we are unable to borrow under our revolving credit facility, we may be unable to meet our business obligations or to grow by buying additional properties, or we may be required to sell some of our properties. If we default under our credit agreement, the lenders may demand immediate payment or elect not to make further borrowings available. Additionally, during the continuance of any event of default under our credit agreement, we will be limited or in some cases prohibited from making distributions on our shares. Any default under our credit agreement would likely have serious and adverse consequences to us and would likely cause the market price of our shares to materially decline.

## Edgar Filing: Equity Commonwealth - Form 10-K

In the future, we may obtain additional debt financing, and the covenants and conditions which apply to any such additional indebtedness may be more restrictive than the covenants and conditions contained in our current credit agreement.

Changes in capital markets may adversely affect the value of an investment in our shares.

Although interest rates remain below historical long term averages, interest rates have recently risen. Increases in interest rates may adversely affect us and the value of an investment in our shares, including in the following ways:

8

---

Amounts outstanding under our credit agreement bear interest at variable interest rates. When interest rates increase, so will our interest costs, which could adversely affect our cash flow, ability to pay principal and interest on debt, cost of refinancing debt when it becomes due and ability to make or sustain distributions to our shareholders. Additionally, if we choose to hedge our interest rate risk, we cannot assure that the hedge will be effective or that our hedging counterparty will meet its obligations to us.

An increase in interest rates could decrease the amount buyers may be willing to pay for our properties, thereby reducing the market value of our properties and limiting our ability to sell properties or to obtain mortgage financing secured by our properties. Increased interest rates may increase the cost of financing properties we acquire to the extent we utilize leverage for those acquisitions and may result in a reduction in our acquisitions to the extent we reduce the amount we offer to pay for properties, due to the effect of increased interest rates, to a price that sellers may not accept.

A lack of any limitation on our debt could result in our becoming more highly leveraged.

Our governing documents do not limit the amount of indebtedness we may incur. Furthermore, our note indenture and credit agreement permit us and our subsidiaries to incur additional debt, including secured debt. Accordingly, we may incur additional debt. We might become more highly leveraged as a result, and our financial condition, results of operations and cash available for distribution to shareholders might be negatively affected, and the risk of default on our indebtedness could increase.

If we fail to maintain an effective system of integrated internal controls, we may not be able to accurately report our financial results.

Effective internal and disclosure controls are necessary for us to provide reliable financial reports and effectively prevent fraud and to operate successfully as a public company. If we cannot provide reliable financial reports or prevent fraud, our reputation and operating results would be harmed. As part of our ongoing monitoring of internal controls we may discover material weaknesses or significant deficiencies in our internal controls. As a result of weaknesses that may be identified in our internal controls, we may also identify certain deficiencies in some of our disclosure controls and procedures that we believe require remediation. If we discover weaknesses, we will make efforts to improve our internal and disclosure controls. However, there is no assurance that we will be successful. Any failure to maintain effective controls or timely effect any necessary improvement of our internal and disclosure controls could harm operating results or cause us to fail to meet our reporting obligations, which could affect our ability to remain listed with the NYSE. Ineffective internal and disclosure controls could also cause investors to lose confidence in our reported financial information, which would likely have a negative effect on the per share trading price of our securities.

We could become a party to legal proceedings, which could adversely affect our financial results and/or distract our Board of Trustees and management.

Claims may be filed against us in connection with any action we may or may not take in the ordinary course of business or otherwise, including any equity or debt financing we may undertake, any sales or purchases of assets, past and future changes to our corporate governance and other past or future actions taken by or on behalf of the Company. The results of litigation are difficult to predict and we can provide no assurance that our legal conclusions or positions will be upheld. Moreover, legal claims present a risk of protracted litigation, incurrence of significant attorneys' fees, costs and expenses, and diversion of management's attention from the operation of our business. In addition, we have agreed to indemnify our present and former Trustees and officers who are made or threatened to be made parties to a legal proceeding by reason of their service in that capacity, which may be costly. Adverse rulings in any such legal proceedings could have a material adverse effect on our financial results and condition and cause substantial reputational harm and/or a decline in the market price of our shares.

We could incur significant costs and liabilities with respect to environmental matters.

## Edgar Filing: Equity Commonwealth - Form 10-K

Under various federal, state and local laws and regulations, as the current or former owners or operators of real estate, we may be liable for costs and damages resulting from the presence or release of hazardous substances, including waste or petroleum products, at, on, in, under or from such property, including costs for investigation, removal or remediation of such contamination and for natural resource damages arising from such contamination. Such laws often impose liability without regard to whether the owner or operator knew of, or was responsible for, the presence of such contamination, and the liability may be joint and several. In addition, the presence of contamination or the failure to remediate contamination at our properties may expose us to third-party liability for costs of remediation and/or personal or property damage, adversely affect our ability to lease, sell or rent such property, or adversely affect our ability to borrow using such property as collateral. Environmental laws may create liens on contaminated sites in favor of the government for damages and costs it incurs to address such

contamination. If contamination is discovered on our properties, environmental laws also may impose restrictions on the manner in which those properties may be used or businesses may be operated, and these restrictions may require significant expenditures. Additionally, we may remain responsible for costs and liabilities arising from environmental issues related to representations and warranties we make in sales agreements for properties of which we have disposed. We also may be liable for the costs of removal or remediation of hazardous substances or waste at disposal or treatment facilities if we arranged for disposal or treatment of hazardous substances at such facilities, whether or not we own or operate such facility.

Some of our properties have been or may be impacted by releases of hazardous substances or petroleum products. Such contamination may arise from a variety of sources, including historic uses of our properties for commercial or industrial purposes, spills of such materials at adjacent properties, or releases from tanks used on our properties to store petroleum or hazardous substances. In addition, certain of our properties are on sites upon which or are adjacent to or near other properties upon which others, including former owners or tenants, have engaged, or may in the future engage, in activities that may release petroleum products or other hazardous or toxic substances.

We, our tenants, and our properties are subject to various federal, state and local regulatory requirements related to environmental, health and safety matters, such as environmental laws, state and local fire and safety requirements, building codes and land use regulations. Failure to comply with these requirements could subject us or our tenants to governmental fines or private litigant damage awards. In addition, compliance with these requirements, including new requirements or stricter interpretation of existing requirements, may require us or our tenants to incur significant expenditures. We do not know whether existing requirements will change or whether future requirements, including any requirements that may emerge from pending or future climate change laws or regulations, will develop. Environmental noncompliance liability also could impact a tenant's ability to make rental payments to us, and our reputation could be negatively affected if we or our tenant's violate environmental laws or regulations.

Buildings and other structures on properties that we currently or formerly own or operate or those we acquire or operate in the future contain, may contain, or may have contained, asbestos-containing material (or ACM). Environmental, health and safety laws require that ACM be properly managed and maintained, and include requirements to undertake special precautions, such as removal or abatement, if ACM would be disturbed during maintenance, renovation, or demolition of a building, potentially resulting in substantial costs. Moreover, laws regarding ACM may impose fines and penalties on owners, employers and operators, and we may be subject to liability for releases of ACM into the air and third parties may seek recovery from owners or operators of real property for personal injury associated with ACM.

When excessive moisture accumulates in buildings or on building materials, mold growth may occur, particularly if the moisture problem remains undiscovered or is not addressed over a period of time. Some molds may produce airborne toxins or irritants. Indoor air quality issues also can stem from inadequate ventilation, chemical contamination from indoor or outdoor sources, and other biological contaminants such as pollen, viruses and bacteria. Indoor exposure to airborne toxins or irritants above certain levels can be alleged to cause a variety of adverse health effects and symptoms, including allergic or other reactions. The presence of mold or other airborne contaminants in our buildings could expose us to costs and liabilities to address these issues, including from third parties if property damage or personal injury occurs.

We may be adversely affected by laws, regulations or other issues related to climate change.

If we become subject to laws or regulations related to climate change, our business, results of operations and financial condition could be impacted adversely. The federal government has enacted, and some of the states and localities in which we operate may enact certain climate change laws and regulations or have begun regulating carbon footprints and greenhouse gas emissions. Although these laws and regulations have not had any known material adverse effects on our business to date, they could result in substantial costs, including compliance costs, increased energy costs, retrofit costs and construction costs, including monitoring and reporting costs, and capital expenditures for

environmental control facilities and other new equipment. Furthermore, our reputation could be negatively affected if we violate climate change laws or regulations. We cannot predict how future laws and regulations, or future interpretations of current laws and regulations, related to climate change will affect our business, results of operations and financial condition. Lastly, the potential physical impacts of climate change on our operations are highly uncertain, and would be particular to the geographic circumstances in areas in which we operate. These may include changes in rainfall and storm patterns and intensities, water shortages, changing sea levels and changing temperatures. These impacts may adversely affect our business, financial condition and results of operations.

We rely on information technology in our operations, and any material failure, inadequacy, interruption or security failure of that technology could harm our business.

We rely on information technology networks and systems, including the Internet, to process, transmit and store electronic information and to manage or support a variety of our business processes, including financial transactions and maintenance of



records, which may include personal identifying information of tenants and lease data. We rely on commercially available systems, software, tools and monitoring to provide security for processing, transmitting and storing confidential tenant information, such as individually identifiable information relating to financial accounts. As our reliance on technology has increased, so have the risks posed to our systems, both internal and those we have outsourced to third party service providers. In addition, information security risks have generally increased in recent years due to the rise in new technologies and the increased sophistication and activities of perpetrators of cyber attacks. Although we have taken steps to protect the security of the data maintained in our information systems, it is possible that our security measures will not be able to prevent the systems' improper functioning, or the improper disclosure of personally identifiable information such as in the event of cyber attacks. Security breaches, including physical or electronic break-ins, computer viruses, attacks by hackers and similar breaches, can create system disruptions, shutdowns or unauthorized disclosure of confidential information. Any failure to maintain proper function, security and availability of our information systems could interrupt our operations, damage our reputation, subject us to liability claims or regulatory penalties and could materially and adversely affect us. We are dependent on key personnel and the loss of such personnel could adversely affect our results of operations and financial condition.

The execution of our repositioning strategy and management of our operations, depend to a significant degree on our senior management team. Our senior management team has extensive experience and a strong reputation in the real estate industry, which aid us in identifying opportunities, having opportunities brought to us, and negotiating with tenants. If we are unable to attract and retain skilled executives, our results of operations and financial condition could be adversely affected.

We may co-invest in joint ventures with third parties. Any future joint venture investments could be adversely affected by the capital markets, lack of sole decision-making authority, reliance on joint venture partners' financial condition and any disputes that may arise between us and our joint venture partners.

We may co-invest with third parties through partnerships, joint ventures or other structures in which we acquire noncontrolling interests in, or share responsibility for, managing the affairs of a property, partnership, co-tenancy or other entity. If we enter into any such joint venture or similar ownership structure, we may not be in a position to exercise sole decision-making authority regarding the properties owned through such joint ventures or similar ownership structure. In addition, investments in joint ventures may, under certain circumstances, involve risks not present when a third party is not involved, including potential deadlocks in making major decisions, restrictions on our ability to exit the joint venture, reliance on joint venture partners and the possibility that a joint venture partner might become bankrupt or fail to fund its share of required capital contributions, thus exposing us to liabilities in excess of our share of the joint venture or jeopardizing our REIT status. The funding of our capital contributions to such joint ventures may be dependent on proceeds from asset sales, credit facility advances or sales of equity securities. Joint venture partners may have business interests or goals that are inconsistent with our business interests or goals, and may be in a position to take actions contrary to its policies or objectives. We may, in specific circumstances, be liable for the actions of its joint venture partners. In addition, any disputes that may arise between us and joint venture partners may result in litigation or arbitration that would increase its expenses. Any of the foregoing may have a material adverse effect on our business, financial condition and results of operations.

#### Risks Related to the Real Estate Industry

Real estate ownership creates risks and liabilities that could have a material adverse effect on us, including our results of operations and financial condition.

Our economic performance and the value of our real estate assets, and consequently the value of our securities, are subject to risks inherently associated with real estate ownership, including:

- changes in supply of or demand for properties in areas in which we own buildings;
- the illiquid nature of real estate markets, which limits our ability to sell our assets rapidly or to respond to changing market conditions;
- the subjectivity of real estate valuations and changes in such valuations over time;

• property and casualty losses;

• the ongoing need for property maintenance and repair, and the need to make expenditures due to changes in governmental regulations, including the Americans with Disabilities Act;

• the inability of tenants to pay rent;

competition from the development of new properties in the markets in which we own property and the quality

- of such competition, such as the attractiveness of our properties as compared to our competitors' properties based on considerations such as convenience of location, rental rates, amenities and safety record;

• civil unrest, acts of war, acts of God, including earthquakes, hurricanes and other natural disasters (which may result in uninsured losses), and other factors beyond our control;

legislative, tax and regulatory developments that may occur at the federal, state and local levels that have direct or indirect impact on the ownership, leasing and operation of our properties; and litigation incidental to our business.

If any of the foregoing events occur, our properties may not generate revenues sufficient to meet our operating expenses, including debt service and capital expenditures, and our cash flow and ability to pay distributions to our shareholders will be adversely affected.

Potential losses may not be covered by insurance exposing us to potential risk of loss.

We do not carry insurance for generally uninsurable losses such as loss from riots, war or acts of God, and, in some cases, flooding. Some of our policies, such as those covering losses due to terrorism, hurricanes, earthquakes and floods, are insured subject to limitations involving large deductibles or co-payments and policy limits that may not be sufficient to cover all losses. If we experience a loss that is uninsured or that exceeds policy limits, we could lose the capital invested in the damaged properties as well as the anticipated future cash flows from those properties. Inflation, changes in building codes and ordinances, environmental considerations, and other factors also might make it impractical or undesirable to use insurance proceeds to replace a property after it has been damaged or destroyed. In addition, if the damaged properties are subject to recourse indebtedness, we would continue to be liable for the indebtedness, even if these properties were irreparably damaged.

Insurance coverage on our properties may be expensive or difficult to obtain, exposing us to potential risk of loss.

In the future, we may be unable to renew or duplicate our current insurance coverage at adequate levels or at reasonable prices. In addition, insurance companies may no longer offer coverage against certain types of losses, such as losses due to terrorist acts, environmental liabilities, or other catastrophic events including hurricanes and floods, or, if offered, the expense of obtaining these types of insurance may not be justified. We therefore may cease to have insurance coverage against certain types of losses and/or there may be decreases in the limits of insurance available. If an uninsured loss or a loss in excess of our insured limits occurs, we could lose all or a portion of the capital we have invested in a property, as well as the anticipated future revenue from the property after a covered period of time, but still remain obligated for any mortgage debt or other financial obligations related to the property. We cannot guarantee that material losses in excess of insurance proceeds will not occur in the future. If any of our properties were to experience a catastrophic loss, it could seriously disrupt our operations, delay revenue and result in large expenses to repair or rebuild the property. Events such as these could adversely affect our results of operations and our ability to meet our obligations.

Actual or threatened terrorist attacks may adversely affect our ability to generate revenues and the value of our properties.

We have significant investments in large metropolitan markets that have been or may be in the future the targets of actual or threatened terrorism attacks. As a result, some tenants in these markets may choose to relocate their businesses to other markets or to lower-profile office buildings within these markets that may be perceived to be less likely targets of future terrorist activity. This could result in an overall decrease in the demand for office space in these markets generally or in our properties in particular, which could increase vacancies in our properties or necessitate that we lease our properties on less favorable terms or both. In addition, future terrorist attacks in these markets could directly or indirectly damage our properties, both physically and financially, or cause losses that materially exceed our insurance coverage. As a result of the foregoing, our ability to generate revenues and the value of our properties could decline materially.

Changes in accounting pronouncements may materially and adversely affect our financial statements, our tenants' credit quality and our ability to secure long-term leases and renewal options.

Accounting policies and methods are fundamental to how we record and report our financial condition and results of operations. Uncertainties posed by various initiatives of accounting standard-setting by the Financial Accounting Standards Board and the Securities and Exchange Commission, which create and interpret applicable accounting standards for U.S. companies, may change the financial accounting and reporting standards or their interpretation and application of these standards that govern the preparation of our financial statements. These changes could have a material impact on our reported financial condition and results of operations. In some cases, we could be required to apply a new or revised standard retroactively, resulting in potentially material restatements of prior period financial statements. Similarly, these changes could have a material impact on our tenants' reported financial condition or results of operations or could affect our tenants' preferences regarding leasing real estate.

The Financial Accounting Standards Board issued an accounting standard, effective January 1, 2019 for public business entities, that requires companies to capitalize all leases on their balance sheets by recognizing a lessee's rights and obligations. Many companies that account for certain leases on an "off balance sheet" basis will be required to account for such leases "on balance sheet." This change will remove many of the differences in the way companies account for owned property and leased property, and could have a material effect on various aspects of our tenants' businesses, including their credit quality and the factors they consider in deciding whether to own or lease properties. The new standard could cause companies that lease properties to prefer shorter lease terms, in an effort to reduce the leasing liability required to be recorded on their balance sheets. The new standard could also make lease renewal options less attractive, as, under certain circumstances, the rule would require a tenant to assume that a renewal right will be exercised and accrue a liability relating to the longer lease term.

#### Risks Related to Our Securities

We cannot assure that we will make distributions to our shareholders, and distributions we may make may include a return of capital.

Any distributions will be made at the discretion of our Board of Trustees and will depend upon various factors that our Board of Trustees deems relevant, including, but not limited to, our results of operations, our financial condition, debt and equity capital available to us, our expectations of our future capital requirements and operating performance, including our funds from operations, or FFO, our normalized funds from operations, or Normalized FFO, and our cash available for distribution, restrictive covenants in our financial or other contractual arrangements (including those in our credit agreement and senior notes indenture), tax law requirements to maintain our status as a REIT, restrictions under Maryland law and our expected needs and availability of cash to pay our obligations or to fund our acquisitions strategy. Our making of distributions is subject to compliance with restrictions contained in our credit agreement and our debt indenture. Additionally, our ability to make distributions will be adversely affected if any of the risks described herein, or other significant adverse events, occur. For these reasons, among others, our distribution rate may decline or we may cease making distributions. Also, our distributions may include a return of capital. As a result of the net operating loss carryforward from prior years, a distribution to common shareholders will not be required for 2016. There can be no assurance that we will pay distributions in the future.

Changes in market conditions could adversely affect the market price of our common shares.

As with other publicly traded equity securities, the value of our common shares depends on various market conditions that may change from time-to-time. Among the market conditions that may affect the value of our common shares are the following:

- the extent of investor interest in our securities;
- the general reputation of REITs and the attractiveness of our equity securities in comparison to other equity securities, including securities issued by other real estate-based companies;
- our underlying asset value;
- national and global economic conditions;
- changes in tax laws;
- our financial performance;
- changes in our credit ratings; and
- general stock and bond market conditions.

The market value of our common shares is based primarily upon the market's perception of our growth potential and our current and potential future earnings and cash dividends. Consequently, our common shares may trade at prices that are greater or less than our net asset value per share of common shares. If our future earnings or cash dividends are less than expected, it is likely that the market price of our common shares will diminish.

Any notes we may issue will be effectively subordinated to the debts of our subsidiaries and our secured debt.

We conduct substantially all of our business through, and substantially all of our properties are owned by, our subsidiaries. Consequently, our ability to pay debt service on our outstanding notes and any notes we issue in the future will be dependent upon the cash flow of our subsidiaries and payments by those subsidiaries to us as dividends

or otherwise. Our subsidiaries are separate legal entities and have their own liabilities. Payments due on our outstanding notes, and any notes we may issue, are, or will be, effectively subordinated to liabilities of our subsidiaries, including guaranty liabilities. As of December 31, 2016, our subsidiaries had \$77.7 million of debt (including net unamortized premiums and net unamortized

deferred financing costs). Our outstanding notes are, and any notes we may issue will be, effectively subordinated to any secured debt with regard to our assets pledged to secure those debts.

Our notes may permit redemption before maturity, and our noteholders may be unable to reinvest proceeds at the same or a higher rate.

The terms of our notes may permit us to redeem all or a portion of our outstanding notes after a certain amount of time, or up to a certain percentage of the notes prior to certain dates. Generally, the redemption price will equal the principal amount being redeemed, plus accrued interest to the redemption date, plus any applicable premium. If a redemption occurs, our noteholders may be unable to reinvest the money they receive in the redemption at a rate that is equal to or higher than the rate of return on the applicable notes.

There may be no public market for notes we may issue and one may not develop.

Generally, any notes we may issue will be a new issue for which no trading market currently exists. We may not list our notes on any securities exchange or seek approval for price quotations to be made available through any automated quotation system. We cannot assure that an active trading market for any of our notes will exist in the future. Even if a market develops, the liquidity of the trading market for any of our notes and the market price quoted for any such notes may be adversely affected by changes in the overall market for fixed income securities, by changes in our financial performance or prospects, or by changes in the prospects for REITs or for the real estate industry generally.

The number of our common shares available for future issuance or sale could adversely affect the per share trading price of our common shares and may be dilutive to current shareholders.

Our declaration of trust authorizes our Board of Trustees to, among other things, issue additional shares of capital stock without stockholder approval. We cannot predict whether future issuances or sales of our common shares or the availability of shares for resale in the open market will decrease the per share trading price per share of our common shares. The issuance of substantial numbers of our common shares in the public market, or upon conversion of our Series D preferred shares, or the perception that such issuances might occur, could adversely affect the per share trading price of our common shares. In addition, we may issue our common shares or restricted share units under the Equity Commonwealth 2015 Omnibus Incentive Plan. Any such future issuances of our common shares may be dilutive to existing shareholders.

Rating agency downgrades or rising interest rates may increase our cost of capital.

Our senior notes and our preferred shares are rated by two rating agencies. These rating agencies may elect to downgrade their ratings on our senior notes and our preferred shares at any time. Such downgrades may negatively affect our access to the capital markets and increase our cost of capital, including the interest rate and fees payable under our credit agreement. In addition, rising interest rates may adversely impact our ability to access the capital markets.

Conversion of our series D preferred shares may dilute the ownership interests of existing shareholders.

The conversion of some or all of our series D preferred shares may dilute the ownership interests of existing shareholders.

#### Risks Related to Our Organization and Structure

Ownership limitations and certain provisions in our declaration of trust and bylaws, as well as certain provisions of Maryland law, may deter, delay or prevent a change in our control or unsolicited acquisition proposals.

Our declaration of trust and bylaws prohibit any shareholder other than certain persons who have been exempted by our Board of Trustees from owning (directly and by attribution) more than 9.8% of the number or value of shares of any class or series of our outstanding shares of beneficial interest, including our common shares. These provisions are intended to assist with our REIT compliance under the Code and otherwise promote our orderly governance.

However, these provisions also inhibit acquisitions of a significant stake in us and may deter, delay or prevent a change in our control or unsolicited acquisition proposals that a shareholder may consider favorable.

Additionally, provisions contained in our declaration of trust and bylaws or under Maryland law may have a similar impact, including, for example, provisions relating to: the authority of our Board of Trustees, and not our

shareholders, to adopt, amend and repeal our bylaws and to fill most vacancies on our Board of Trustees; the fact that only the Chairman of the Board of Trustees, our Chief Executive Officer, our President, a majority of our Trustees or the holders of 10% of our common shares may call a special meeting of shareholders; and advance notice requirements for shareholder proposals.

Furthermore, our Board of Trustees has the authority to create and issue new classes or series of shares (including shares with voting rights and other rights and privileges that may deter a change in control) and issue additional common shares. The



authorization and issuance of a new class of capital stock or additional common shares could have the effect of delaying or preventing someone from taking control of us, even if a change in control were in our shareholders' best interests.

Certain provisions of Maryland law could inhibit changes in control.

Certain provisions of Maryland law may have the effect of inhibiting a third party from making a proposal to acquire us or of impeding a change of control under circumstances that otherwise could provide the holders of our common shares with the opportunity to realize a premium over the then-prevailing market price of such shares, including: “business combination moratorium/fair price” provisions that, subject to limitations, prohibit certain business combinations between us and an “interested shareholder” (defined generally as any person who beneficially owns 10% or more of the voting power of our shares or an affiliate thereof) for five years after the most recent date on which the shareholder becomes an interested shareholder, and thereafter imposes stringent fair price and super-majority shareholder voting requirements on these combinations; and “control share” provisions that provide that “control shares” of our company (defined as shares which, when aggregated with other shares controlled by the shareholder, entitle the shareholder to exercise one of three increasing ranges of voting power in electing trustees) acquired in a “control share acquisition” (defined as the direct or indirect acquisition of ownership or control of “control shares” from a party other than the issuer) have no voting rights except to the extent approved by our shareholders by the affirmative vote of at least two thirds of all the votes entitled to be cast on the matter, excluding all interested shares, and are subject to redemption in certain circumstances. We have opted out of these provisions of Maryland law. However, our Board of Trustees may opt to make these provisions applicable to us at any time without obtaining shareholder approval.

Certain provisions in the organizational documents of the Operating Trust may delay, defer or prevent unsolicited acquisitions of us or changes in our control.

Provisions in the organizational documents of the Operating Trust may delay, defer or prevent a transaction or a change of control that might involve a premium price for the Company’s common shares. These provisions include, among others:

- redemption rights of qualifying parties;
- a provision that we may not be removed as the trustee of the Operating Trust with or without cause;
- transfer restrictions on the OP Units held directly or indirectly by us;
- our ability as trustee in some cases to amend the organizational documents of the Operating Partnership without the consent of the other holders of OP Units;
- the right of the holders of OP Units to consent to mergers involving us under specified circumstances; and
- the right of the holders of OP Units to consent to our withdrawal as the sole trustee of the Operating Trust.

These provisions could discourage third parties from making proposals involving an unsolicited acquisition of us or change of our control, although some shareholders might consider such proposals, if made, desirable.

As an UPREIT, we are a holding company with no direct operations and will rely on distributions received from the Operating Trust to make distributions to our shareholders.

We are a holding company and conduct all of our operations through the Operating Trust. We do not have, apart from our ownership of the OP Units, any independent operations. As a result, we will rely on distributions from the Operating Trust to make any distributions to our shareholders we might declare on our common shares and to meet any of our obligations, including tax liability on taxable income allocated to us from the Operating Trust (which might not make distributions to our company equal to the tax on such allocated taxable income). The ability of subsidiaries of the Operating Trust to make distributions to the Operating Trust, and the ability of the Operating Trust to make distributions to us in turn, will depend on their operating results and on the terms of any financing arrangements into which they have entered. Such financing arrangements may contain lockbox arrangements, reserve requirements, covenants and other provisions that prohibit or otherwise restrict the distribution of funds, including upon default

thereunder. In addition, because we are a holding company, the claims of our shareholders as common shareholders of our company will be structurally subordinated to all existing and future liabilities and other obligations (whether or not for borrowed money) and any preferred equity of the Operating Trust and its subsidiaries. Therefore, in the event of our bankruptcy, liquidation or reorganization, our assets and those of the Operating Trust and its subsidiaries will be able to satisfy the claims of our common shareholders only after all of our and the Operating Trust's and its subsidiaries' liabilities and other obligations and any preferred equity have been paid in full.

We may acquire properties or portfolios of properties through tax-deferred contribution transactions, which could result in shareholder dilution and limit our ability to sell such assets.

In the future, we may acquire properties or portfolios of properties through tax-deferred contribution transactions in exchange for OP Units in the Operating Trust, which may result in shareholder dilution. This acquisition structure may have the effect of, among other things, reducing the amount of tax depreciation we could deduct over the tax lives of the acquired properties, and may require that we agree to protect the contributors' abilities to defer recognition of taxable gain through restrictions on our ability to dispose of the acquired properties and/or the allocation of partnership debt to the contributors to maintain their tax bases. These restrictions could limit our ability to sell or finance an asset at a time, or on terms, that would be favorable absent such restrictions.

Future issuances of OP Units would reduce our ownership interest in the Operating Trust and may result in shareholder dilution.

As of December 31, 2016, we beneficially owned 100.0% of the outstanding OP Units. Our Operating Trust may, in connection with our acquisition of additional properties or otherwise, issue OP Units to third parties. Additionally, we have and may in the future issue long-term equity awards convertible into OP Units (LTIP Units) to trustees, officers, employees or other agents. Such issuances of OP Units, or the conversion of LTIP Units into OP Units, would reduce our ownership in the Operating Trust and, consequently, our share of distributions from the Operating Trust. Because OP Units may be redeemed (sometimes subject to vesting or performance achievements) for, at our election, cash or common shares, additional common shares may be issued in respect of any such redeemed OP Units, which would dilute existing shareholders. Our shareholders do not have any voting rights with respect to any such issuances, redemptions or other operational activities of the Operating Trust.

Our recourse against Trustees and officers may be limited by the limited rights granted to our shareholders in our declaration of trust.

Our declaration of trust limits the liability of our Trustees and officers to us and our shareholders for money damages to the maximum extent permitted under Maryland law. Under current Maryland law, our Trustees and officers will not have any liability to us and our shareholders for money damages other than liability resulting from:

- actual receipt of an improper benefit or profit in money, property or services; or
- active and deliberate dishonesty by the Trustee or officer that was established by a final judgment as being material to the cause of action adjudicated.

Our declaration of trust and bylaws require us to indemnify any present or former Trustee or officer, to the maximum extent permitted by Maryland law, who is made or threatened to be made a party to a proceeding by reason of his or her service in that capacity. In addition, we may be obligated to pay or reimburse the expenses incurred by our present and former Trustees and officers without requiring a preliminary determination of their ultimate entitlement to indemnification. As a result, we and our shareholders may have more limited rights against our present and former Trustees and officers than might otherwise exist absent the provisions in our declaration of trust and bylaws or that might exist with other companies, which could limit your recourse in the event of actions not in your best interest.

Conflicts of interest could arise in the future between the interests of the Company's shareholders and the interests of other holders of OP Units, which may impede business decisions that could benefit our shareholders.

Conflicts of interest may exist or could arise in the future as a result of the relationships between the Company and its affiliates, on the one hand, and the Operating Trust or holders of OP Units, on the other. Our trustees and officers have duties to the Company and its shareholders under applicable Maryland law in connection with their management of the Company. At the same time, we, as trustee, have fiduciary duties to the Operating Trust and to the holders of all OP Units under Maryland law in connection with the management of the Operating Trust. The Company's duties as trustee to the Operating Trust and its Unitholders may come into conflict with the duties of our trustees and officers to the Company and our shareholders.

Additionally, the organizational documents of the Operating Trust expressly limit our liability by providing that the Company will not be liable for monetary or other damages or otherwise for losses sustained, liabilities incurred or benefits not derived in connection with such decisions unless the Company acted with willful misfeasance, bad faith,

gross negligence or reckless disregard of duty, and the act or omission was material to the matter giving rise to the loss, liability or benefit not derived. Moreover, the organizational documents of the Operating Trust provide that the Operating Trust may indemnify, and pay or reimburse reasonable expenses to, the Company and the Company's and the Operating Trust's present or former unitholders, trustees, officers or agents and any other persons acting on behalf of the Company that the Company may designate from and against all claims and liabilities by reason of his, her or its service in such capacity. The Operating Trust has the power, with the approval of the Company, to provide such indemnification and advancement of expenses. The provisions of

Maryland law that allow the fiduciary duties of a trustee to be modified by such organizational documents have not been resolved in a court of law, and we have not obtained an opinion of counsel covering the provisions set forth in the organizational documents of the Operating Trust that purport to waive or restrict our fiduciary duties that would be in effect were it not for such organizational documents.

Shareholder litigation against us or our Trustees and officers may be referred to binding arbitration proceedings which may increase our risk of default.

Our bylaws provide that actions by our shareholders against us or against our Trustees and officers, including derivative and class actions, may be referred to binding arbitration proceedings. As a result, our shareholders would not be able to pursue litigation for these disputes in courts against us or our Trustees and officers if the disputes were referred to arbitration. In addition, the ability to collect attorneys' fees or other damages may be limited, which may discourage attorneys from agreeing to represent parties wishing to commence such a proceeding.

We may change our operational, financing and investment policies without shareholder approval and we may become more highly leveraged, which may increase our risk of default under our debt obligations.

Our Board of Trustees determines our operational, financing and investment policies and may amend or revise our policies, including our policies with respect to our intention to qualify for taxation as a REIT, acquisitions, dispositions, growth, operations, indebtedness, capitalization and distributions, or approve transactions that deviate from these policies, without a vote of, or notice to, our shareholders. Policy changes could adversely affect the market value of our common shares and our ability to make distributions to our shareholders. Further, our organizational documents do not limit the amount or percentage of indebtedness, funded or otherwise, that we may incur. Our Board of Trustees may alter or eliminate our current policy on borrowing at any time without shareholder approval. If this policy changed, we could become more highly leveraged, which could result in an increase in our debt service costs. Higher leverage also increases the risk of default on our obligations. In addition, a change in our investment policies, including the manner in which we allocate our resources across our portfolio or the types of assets in which we seek to invest, may increase our exposure to interest rate risk, real estate market fluctuations and liquidity risk.

#### Risks Related to Our Taxation as a REIT

Qualifying as a REIT involves highly technical and complex provisions of the Code.

Qualification as a REIT involves the application of highly technical and complex Code provisions for which only limited judicial and administrative authorities exist. Even a technical or inadvertent violation could jeopardize our REIT qualification. Our qualification as a REIT depends on our satisfaction of certain asset, income, organizational, distribution, stockholder ownership and other requirements on a continuing basis. We have owned direct or indirect interests in one or more REITs (each, a "Subsidiary REIT") that have elected to be taxed as REITs under the U.S. federal income tax laws. Each Subsidiary REIT is subject to the various REIT qualification requirements and other limitations described herein that are applicable to us. If a Subsidiary REIT were to fail to qualify as a REIT, then (i) that Subsidiary REIT would become subject to U.S. federal income tax, (ii) our ownership of shares in such Subsidiary REIT would cease to be a qualifying asset for purposes of the asset tests applicable to REITs, and (iii) it is possible that we would fail certain of the asset tests applicable to REITs, in which event we would fail to qualify as a REIT unless we could avail ourselves of certain relief provisions. While we believe that the Subsidiary REITs have qualified as REITs under the Code, we have joined each Subsidiary REIT in filing a protective taxable REIT subsidiary election under Section 856(l) of the Code for each taxable year in which we have owned an interest in the Subsidiary REIT. Pursuant to the protective taxable REIT subsidiary election, we believe that even if a Subsidiary REIT was not a REIT for some reason, then it would instead have been considered one of our taxable REIT subsidiaries. As one of our taxable REIT subsidiaries, we believe that a Subsidiary REIT's failure to qualify as a REIT would not jeopardize our own qualification as a REIT, even if we owned more than 10% of the Subsidiary REIT.

New legislation, court decisions or administrative guidance, in each case possibly with retroactive effect, may make it more difficult or impossible for us to qualify as a REIT. Certain rules applicable to REITs are particularly difficult to interpret or to apply in the case of REITs investing in real estate mortgage loans that are acquired at a discount,

subject to work-outs or modifications, or reasonably expected to be in default at the time of acquisition. In addition, our ability to satisfy the requirements to qualify as a REIT depends in part on the actions of third parties over which we have no control or only limited influence, including in cases where we own an equity interest in an entity that is classified as a partnership for U.S. federal income tax purposes.

If we do not qualify as a REIT or fail to remain qualified as a REIT, we will be subject to U.S. federal income tax and potentially to additional state and local taxes which would reduce the amount of cash available for distribution to our shareholders.

We believe that we have been organized and have operated, and will continue to be organized and to operate, in a manner to allow us to qualify us to be taxed under the Code as a REIT. However, we cannot be certain that, upon review or audit, the IRS will agree with this conclusion. Furthermore, Congress and the IRS might make changes to the tax laws and regulations, and the courts might issue new rulings, that make it more difficult, or impossible, for us to remain qualified as a REIT. We do not intend to request a ruling from the IRS as to our REIT qualification. As a REIT, we generally do not pay U.S. federal income tax on our net income that we distribute currently to our shareholders. However, actual qualification as a REIT under the Code depends on satisfying complex statutory requirements, for which there are only limited judicial and administrative interpretations. Many of the REIT requirements, however, are highly technical and complex. The determination that we are a REIT requires an analysis of various factual matters and circumstances that may not be totally within our control. For example, to qualify as a REIT, at least 95% of our gross income must come from specific passive sources, such as rent, that are itemized in the REIT tax laws. In addition, to qualify as a REIT, we cannot own specified amounts of debt and equity securities of some issuers. We also are required to distribute to our shareholders with respect to each year at least 90% of our "REIT taxable income" (determined before the deduction for dividends paid and excluding net capital gains). Even a technical or inadvertent mistake could jeopardize our REIT status and, given the highly complex nature of the rules governing REITs and the ongoing importance of factual determinations, we cannot provide any assurance that we will continue to qualify as a REIT.

If we fail to qualify as a REIT for U.S. federal income tax purposes, and are unable to avail ourselves of certain savings provisions set forth in the IRC, we likely would be subject to U.S. federal income tax at regular corporate rates. As a taxable corporation, we would not be allowed to take a deduction for distributions to shareholders in computing our taxable income or pass through long term capital gains to individual shareholders at favorable rates. We also could be subject to the U.S. federal alternative minimum tax and possibly increased state and local taxes. We would not be able to elect to be taxed as a REIT for four years following the year we first failed to qualify unless the IRS were to grant us relief under certain statutory provisions. If we failed to qualify as a REIT, we likely would have to pay significant income taxes, which likely would reduce our net earnings available for investment or distribution to our shareholders. If we fail to qualify as a REIT, such failure would cause us to be in breach under our credit agreement, and may adversely affect our ability to raise capital and to service our debt. This likely would have a significant adverse effect on our earnings and the value of our securities. In addition, we would no longer be required to pay any distributions to shareholders. If we fail to qualify as a REIT for U.S. federal income tax purposes and are able to avail ourselves of one or more of the statutory savings provisions in order to maintain our REIT status, we would nevertheless be required to pay penalty taxes of \$50,000 or more for each such failure.

Distributions to shareholders generally do not qualify for the preferential tax rates available for some dividends. Dividends payable by U.S. corporations to noncorporate shareholders, such as individuals, trusts and estates, are generally eligible for reduced tax rates. Distributions paid by REITs, however, generally are not eligible for these reduced rates. Although this does not adversely affect the taxation of REITs or dividends payable by REITs, to the extent that the preferential rates continue to apply to regular corporate qualified dividends, the more favorable rates for corporate dividends may cause investors who are individuals, trusts and estates to perceive that an investment in a REIT is less attractive than an investment in a non-REIT entity that pays dividends, thereby reducing the demand and market price of our shares.

REIT distribution requirements could adversely affect our ability to execute our business plan.

We generally must distribute annually at least 90% of our "REIT taxable income" (determined before the deduction for dividends paid and excluding net capital gains) in order for U.S. federal corporate income tax not to apply to earnings that we distribute. To the extent that we satisfy this distribution requirement, but distribute less than 100% of our taxable income, we will be subject to U.S. federal corporate income tax on our undistributed taxable income. We intend to make distributions to our shareholders to comply with the REIT requirements of the IRC. In addition, we

## Edgar Filing: Equity Commonwealth - Form 10-K

will be subject to a 4% nondeductible excise tax if the actual amount that we pay out to our shareholders in a calendar year is less than a minimum amount specified under U.S. federal tax laws. We intend to make distributions to our shareholders to comply with the REIT requirements of the Code.

From time to time, we may generate taxable income greater than our income for financial reporting purposes prepared in accordance with U.S. generally accepted accounting principles, or GAAP, or differences in timing between the recognition of taxable income and the actual receipt of cash may occur. If we do not have other funds available in these situations we could be required to (i) borrow funds on unfavorable terms, (ii) sell investments at disadvantageous prices, (iii) distribute amounts that would otherwise be invested in future acquisitions, or (iv) make a taxable distribution of our common shares as part of a distribution in which shareholders may elect to receive our common shares or (subject to a limit measured as a percentage of



the total distribution) cash to make distributions sufficient to enable us to pay out enough of our taxable income to satisfy the REIT distribution requirement. These alternatives could increase our costs or reduce our shareholders' equity. Thus, compliance with the REIT requirements may hinder our ability to grow, which could adversely affect the value of our shares.

Even if we qualify and remain qualified as a REIT, we may face other tax liabilities that reduce our cash flow.

Even if we qualify and remain qualified for taxation as a REIT, we may be subject to certain U.S. federal, state and local taxes on our income and assets, including taxes on any undistributed income, excise taxes, state or local income, property and transfer taxes, such as mortgage recording taxes, and other taxes. We are subject to U.S. federal and state income tax (and any applicable non-U.S. taxes) on the net income earned by our taxable REIT subsidiaries. Moreover, if we have net income from "prohibited transactions," that income will be subject to a 100% tax. Finally, some state and local jurisdictions may tax some of our income even though as a REIT we are not subject to U.S. federal income tax on that income because not all states and localities treat REITs the same way they are treated for federal U.S. income tax purposes. To the extent that we and our affiliates are required to pay federal, state and local taxes, we will have less cash available for distributions to our shareholders.

Complying with REIT requirements may force us to forgo and/or liquidate otherwise attractive investment opportunities.

To qualify as a REIT, we must ensure that we meet the REIT gross income tests annually and that at the end of each calendar quarter, at least 75% of the value of our assets consists of cash, cash items, government securities and qualified REIT real estate assets. The remainder of our investment in securities (other than government securities and qualified real estate assets) generally cannot include more than 10% of the outstanding voting securities of any one issuer or more than 10% of the total value of the outstanding securities of any one issuer. In addition, in general, no more than 5% of the value of our assets (other than government securities and qualified real estate assets) can consist of the securities of any one issuer, no more than 25% (20% for taxable years beginning after December 31, 2017) of the value of our total securities can be represented by securities of one or more TRSs and, effective for our taxable year that began on January 1, 2016 and all future taxable years, no more than 25% of the value of our assets can be represented by debt instruments issued by "publicly offered REITs." If we fail to comply with these requirements at the end of any calendar quarter, we must correct the failure within 30 days after the end of the calendar quarter or qualify for certain statutory relief provisions to avoid losing our REIT qualification and suffering adverse tax consequences. As a result, we may be required to liquidate from our portfolio, or contribute to a TRS, otherwise attractive investments in order to maintain our qualification as a REIT. These actions could have the effect of reducing our income, increasing our income tax liability, and reducing amounts available for distribution to our stockholders. In addition, we may be required to make distributions to shareholders at disadvantageous times or when we do not have funds readily available for distribution, and may be unable to pursue investments (or, in some cases, forego the sale of such investments) that would be otherwise advantageous to us in order to satisfy the source-of-income or asset-diversification requirements for qualifying as a REIT. Thus, compliance with the REIT requirements may hinder our ability to make, and, in certain cases, maintain ownership of certain attractive investments.

The tax on "prohibited transactions" may limit our ability to engage in transactions which would be treated as sales for U.S. federal income tax purposes.

A REIT's net income from prohibited transactions is subject to a 100% tax. In general, prohibited transactions are sales or other dispositions of property, other than foreclosure property, held primarily for sale to customers in the ordinary course of business. Our Trustees have adopted a strategy to own and acquire at a discount to replacement cost high-quality, multi-tenant office assets in markets and sub-markets with favorable long-term supply and demand fundamentals. Our efforts will primarily be focused on larger office buildings in central business districts and major urban areas that offer an attractive quality of life, including opportunities for tenants to live and play in close proximity to where they work, with a preference for markets that have above average limitations on new supply. We

believe that the dispositions related to the repositioning of our portfolio along with other dispositions that we have made or that we might make in the future will not be subject to the 100% penalty tax; however, because application of the prohibited transactions tax could be based on an analysis of all of the facts and circumstances, there can be no assurance that the gains on our prior real estate sales have not, or any future real estate sales will not, be subject to the 100% prohibited transaction tax.

Our ownership of TRSs has been and will continue to be limited and our transactions with our TRSs will cause us to be subject to a 100% penalty tax on certain income or deductions if those transactions are not conducted on arm's length terms.

A REIT may own up to 100% of the stock of one or more TRSs. A TRS may hold assets and earn income that would not be qualifying assets or income if held or earned directly by a REIT. Both the subsidiary and the REIT must jointly elect to treat

the subsidiary as a TRS. A corporation of which a TRS directly or indirectly owns more than 35% of the voting power or value of the stock will automatically be treated as a TRS. Overall, no more than 25% (20% for taxable years beginning after December 31, 2017) of the value of a REIT's assets may consist of stock or securities of one or more TRSs. In addition, the TRS rules limit the deductibility of interest paid or accrued by a TRS to its parent REIT to assure that the TRS is subject to an appropriate level of corporate taxation. The rules also impose a 100% excise tax on certain transactions between a TRS and its parent REIT that are not conducted on an arm's length basis.

TRSs that we have formed have paid and will continue to pay U.S. federal, state and local income tax on their taxable income, and their after-tax net income is available for distribution to us but is not required to be distributed by such domestic TRSs to us. We believe that the aggregate value of the stock and securities of our TRSs has been and we anticipate that the aggregate value will continue to be less than 25% (20% for taxable years beginning after December 31, 2017) of the value of our total assets (including our TRS stock and securities). Furthermore, we have monitored and will continue to monitor the value of our respective investments in our TRSs for the purpose of ensuring compliance with TRS ownership limitations. In addition, we have scrutinized and will continue to scrutinize all of our transactions with TRSs to ensure that they are entered into on arm's length terms to avoid incurring the 100% excise tax described above. There can be no assurance, however, that we will be able to comply with the TRS limitation discussed above or to avoid application of the 100% excise tax discussed above.

Complying with REIT requirements may limit our ability to hedge effectively and may cause us to incur tax liabilities.

The REIT provisions of the Code limit our ability to hedge our liabilities. Generally, income from a hedging transaction we enter into to manage risk of interest rate fluctuations with respect to borrowings, including gain from the disposition of such hedging transactions, to the extent the hedging transactions hedge indebtedness incurred, or to be incurred, by us to acquire or carry real estate assets does not constitute "gross income" for purposes of the 75% or 95% gross income tests, provided we properly identify the hedge pursuant to the applicable sections of the Code and Treasury regulations. To the extent that we enter into other types of hedging transactions, the income from those transactions is likely to be treated as non-qualifying income for purposes of both gross income tests. As a result of these rules, we may need to limit our use of advantageous hedging techniques or implement those hedges through a taxable REIT subsidiary. This could increase the cost of our hedging activities because our taxable REIT subsidiary would be subject to tax on income or gains resulting from hedges entered into by it or expose us to greater risks associated with changes in interest rates than we would otherwise want to bear. In addition, losses in our taxable REIT subsidiary will generally not provide any tax benefit, except for being carried forward for use against future taxable income in our taxable REIT subsidiary.

There is a risk of changes in the tax law applicable to REITs.

The IRS, the United States Treasury Department and Congress frequently review U.S. federal income tax legislation, regulations and other guidance. Legislative and regulatory changes, including comprehensive tax reform, may be more likely in the 115<sup>th</sup> Congress, which convened in January 2017, because the new President and both Houses of Congress will be controlled by the same political party. We cannot predict whether, when or to what extent new federal tax laws, regulations, interpretations or rulings will be adopted. Any legislative action may prospectively or retroactively modify our tax treatment and, therefore, may adversely affect taxation of us and/or our shareholders.

Item 1B. Unresolved Staff Comments.

None.



Edgar Filing: Equity Commonwealth - Form 10-K

Item 2. Properties.

General. At December 31, 2016, we had real estate investments totaling approximately \$2.9 billion in 33 properties (64 buildings), one land parcel and one property taken out of service which is now classified as a land parcel, that were leased to approximately 600 tenants. We account for the operations of all our properties in one reporting segment. At December 31, 2016, we owned the following real estate (dollars in thousands):

Property	State	Number of Buildings	Undepreciated Carrying Value(1)	Depreciated Carrying Value(1)	Annualized Rental Revenue(2)
Parkshore Plaza	CA	4	\$ 45,439	\$38,744	\$ 4,190
1225 Seventeenth Street	CO	1	156,803	130,813	23,822
5073, 5075, & 5085 S. Syracuse Street	CO	1	63,610	53,795	7,379
1601 Dry Creek Drive	CO	1	34,550	24,538	8,865
97 Newberry Road	CT	1	15,350	12,175	1,816
33 Stiles Lane	CT	1	9,793	7,440	639
1250 H Street, NW	DC	1	72,608	44,224	8,016
Georgetown-Green and Harris Buildings	DC	2	60,023	53,423	6,514
802 Delaware Avenue	DE	1	43,496	19,279	4,280
6600 North Military Trail	FL	3	145,808	126,337	16,990
600 West Chicago Avenue	IL	2	395,444	349,605	49,406
8750 Bryn Mawr Avenue	IL	2	93,605	79,194	16,164
109 Brookline Avenue	MA	1	47,536	27,340	10,826
111 Market Place	MD	1	71,555	44,199	12,583
25 S. Charles Street	MD	1	38,504	24,864	8,717
820 W. Diamond	MD	1	33,660	20,883	2,948
Danac Stiles Business Park	MD	3	65,718	44,799	7,078
East Eisenhower Parkway	MI	2	56,376	48,187	10,569
2250 Pilot Knob Road	MN	1	6,530	3,634	867
411 Farwell Avenue	MN	1	16,357	12,301	1,909
4700 Belleview Avenue	MO	1	7,225	5,939	1,064
Cherrington Corporate Center	PA	7	71,964	49,470	6,019
1500 Market Street	PA	1	304,546	215,829	39,245
1600 Market Street	PA	1	135,851	76,416	20,744
1735 Market Street	PA	1	302,533	184,128	27,106
Foster Plaza	PA	8	76,256	54,703	11,869
206 East 9th Street	TX	1	49,197	44,318	6,356
4515 Seton Center Parkway	TX	1	23,130	13,381	3,650
4516 Seton Center Parkway	TX	1	24,257	13,760	2,645
Bridgepoint Square	TX	5	91,332	51,624	12,385
Research Park	TX	4	93,444	61,149	11,709
333 108th Avenue NE	WA	1	153,219	127,431	20,455
600 108th Avenue NE	WA	1	50,596	37,138	7,725
Properties		64	\$ 2,856,315	\$2,101,060	\$ 374,550
625 Crane Street	IL	—	\$ —	\$ —	\$ —
Cabot Business Park Land	MA	—	575	575	—
Land Parcels		—	\$ 575	\$575	\$ —
Total		64	\$ 2,856,890	\$2,101,635	\$ 374,550



(1) Excludes purchase price allocations for acquired real estate leases.

Annualized rental revenue is annualized contractual rents from our tenants pursuant to leases which have commenced as of December 31, 2016, plus estimated recurring expense reimbursements; includes triple net lease rents and excludes lease value amortization, straight line rent adjustments, abated ("free") rent periods and parking revenue. We calculate annualized rental revenue by aggregating the recurring billings outlined above for the most recent month during the quarter reported, adding abated rent, and multiplying the sum by 12 to provide an estimation of near-term potentially-recurring revenues. Annualized rental revenue is a forward-looking non-GAAP measure. Annualized rental revenue cannot be reconciled to a comparable GAAP measure without unreasonable efforts, primarily due to the fact that it is calculated from the billings of tenants in the most recent month at the most recent rental rates during the quarter reported, whereas historical GAAP measures include billings from a potentially different group of tenants over multiple months at potentially different rental rates.

(2) At December 31, 2016, four properties (7 buildings) were encumbered by mortgage notes payable totaling \$77.7 million (including net unamortized premiums and discounts and net unamortized deferred financing costs). For more information regarding these mortgage notes, see Note 8 of the Notes to Consolidated Financial Statements included in Part IV, Item 15 of this Annual Report on Form 10-K.

### Item 3. Legal Proceedings.

We are or may be a party to various legal proceedings that arise in the ordinary course of business. We are not currently involved in any litigation nor, to our knowledge, is any litigation threatened against us where the outcome would, in our judgment based on information currently available to us, have a material adverse effect on our consolidated financial position or consolidated results of operations.

### Item 4. Mine Safety Disclosures.

Not applicable.

## PART II

## Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Our common shares are traded on the NYSE (symbol: EQC). The following table sets forth for the periods indicated the high and low sale prices for our common shares, as reported by the NYSE:

	High	Low
2016		
First Quarter	\$28.58	\$25.23
Second Quarter	29.74	26.92
Third Quarter	31.91	29.13
Fourth Quarter	30.98	28.04
2015		
First Quarter	\$27.24	\$24.97
Second Quarter	27.64	24.91
Third Quarter	27.70	25.17
Fourth Quarter	29.75	26.34

As of February 13, 2017, there were 1,317 shareholders of record of our common shares. However, because many of our common shares are held by brokers and other institutions on behalf of shareholders, we believe that there are considerably more beneficial holders of our common shares than record holders.

## Distributions

Under our governing documents and Maryland law, distributions to our shareholders are to be authorized and declared by our Board of Trustees.

We did not pay any cash distributions to our common shareholders in 2016 and 2015.

As a result of the net operating loss carryforward from prior years, a distribution to common shareholders was not required for 2016. The timing and amount of future distributions is determined at the discretion of our Board of Trustees and will depend upon various factors that our Board of Trustees deems relevant, including, but not limited to, our results of operations, our financial condition, debt and equity capital available to us, our expectations of our future capital requirements and operating performance, including our FFO, our Normalized FFO, and our cash available for distribution, restrictive covenants in our financial or other contractual arrangements (including those in our credit agreement and senior notes indenture), tax law requirements to qualify for taxation as and remain a REIT, restrictions under Maryland law and our expected needs and availability of cash to pay our obligations and fund acquisitions. Therefore, there can be no assurance that we will pay distributions in the future.

## Issuer Repurchases

## Common Share Repurchase Program

On August 24, 2015, our Board of Trustees approved a common share repurchase plan, which authorized the repurchase of up to \$100.0 million of our outstanding common shares over the twelve month period following the date of authorization. On September 14, 2015, our Board of Trustees authorized the repurchase of up to an additional \$100.0 million of our outstanding common shares over the twelve month period following the date of authorization. On March 17, 2016, our Board of Trustees authorized the repurchase of up to an additional \$150.0 million of our outstanding common shares over the twelve month period following the date of authorization.



During the year ended December 31, 2016, we purchased and retired 2,491,675 of our common shares at a weighted average price of \$27.68 per share for a total investment of \$69.0 million. The following table provides information with respect to the common share repurchases made by the Company during the year ended December 31, 2016:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number or Approximate Dollar Value of Shares that May Yet be Purchased Under the Plans or Programs
January 2016	361,162	\$ 25.97	361,162	\$ 102,772,995
February 2016	622,627	\$ 25.93	622,627	\$ 86,630,373
March 2016	—	\$ —	—	\$ 236,630,373
April 2016	—	\$ —	—	\$ 236,630,373
May 2016	—	\$ —	—	\$ 236,630,373
June 2016	—	\$ —	—	\$ 236,630,373
July 2016	—	\$ —	—	\$ 236,630,373
August 2016	—	\$ —	—	\$ 236,630,373
September 2016	—	\$ —	—	\$ 150,000,000
October 2016	—	\$ —	—	\$ 150,000,000
November 2016	255,000	\$ 28.98	255,000	\$ 142,610,648
December 2016	1,252,886	\$ 28.78	1,252,886	\$ 106,550,323
Total	2,491,675	\$ 27.68	2,491,675	\$ 106,550,323

Since the inception of the common share repurchase plan through December 31, 2016, we have purchased and retired a total of 5,901,975 of our common shares at a weighted average price of \$26.57 per share, for a total of \$156.8 million. In August and September 2016, the first two share repurchase authorizations, of which \$86.6 million was not utilized, expired. The \$106.6 million of remaining authorization available under our share repurchase program as of December 31, 2016 is scheduled to expire in March 2017.

## Surrender of Common Shares for Tax Withholding

During the year ended December 31, 2016, certain of our employees surrendered common shares owned by them to satisfy their statutory tax withholding obligations in connection with the vesting of restricted common shares under the Equity Commonwealth 2015 Omnibus Incentive Plan (the 2015 Incentive Plan).

The following table summarizes all of these repurchases during the year ended December 31, 2016:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number or Approximate Dollar Value of Shares that May Yet be Purchased Under the Plans or Programs
January 2016	—	N/A	N/A	N/A
February 2016	—	N/A	N/A	N/A
March 2016	—	N/A	N/A	N/A
April 2016	—	N/A	N/A	N/A
May 2016	—	N/A	N/A	N/A
June 2016	—	N/A	N/A	N/A
July 2016	—	N/A	N/A	N/A
August 2016	—	N/A	N/A	N/A
September 2016	853	(1)\$ 30.71	N/A	N/A
October 2016	—	N/A	N/A	N/A
November 2016	30,172	(1)\$ 29.41	N/A	N/A
December 2016	—	N/A	N/A	N/A
Total	31,025	(1)\$ 29.45		

(1) The number of shares purchased represents common shares surrendered by certain of our employees to satisfy their statutory minimum federal and state tax obligations associated with the vesting of restricted common shares of beneficial interest under the 2015 Incentive Plan. With respect to these shares, the price paid per share is based on the closing price of our common shares as of the date of the determination of the statutory minimum federal and state tax obligations.

## Unregistered Sales of Securities

There were no unregistered sales of equity securities during the year ended December 31, 2016.

## Performance Graph

Notwithstanding anything to the contrary set forth in any of our filings under the Securities Act or the Exchange Act that might incorporate SEC filings, in whole or in part, the following performance graph will not be incorporated by reference into any such filings.

The following graph compares the cumulative total shareholder return of our common shares for the period from December 31, 2011 to December 31, 2016, to the NAREIT All REITs, Standard & Poor's 500 Index, or the S&P 500, and to the NAREIT Equity Office Index over the same period. The graph assumes an investment of \$100.00 in our common shares and each index and the reinvestment of all distributions. The shareholder return shown on the graph below is not indicative of future performance.

Index	Period Ending					
	12/31/2011	12/31/2012	12/31/2013	12/31/2014	12/31/2015	12/31/2016
Equity Commonwealth	\$100.00	\$ 104.94	\$ 161.93	\$ 180.31	\$ 194.78	\$ 212.41
NAREIT All REITs	\$100.00	\$ 120.14	\$ 124.00	\$ 157.66	\$ 161.27	\$ 176.24
S&P 500	\$100.00	\$ 116.00	\$ 153.57	\$ 174.60	\$ 177.01	\$ 198.18
NAREIT Equity Office Index	\$100.00	\$ 114.15	\$ 120.52	\$ 151.68	\$ 152.11	\$ 172.14

Source: SNL Financial LC

## Item 6. Selected Financial Data.

The following table sets forth selected financial data for the periods and dates indicated. This data should be read in conjunction with, and is qualified in its entirety by reference to, "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Part II, Item 7 and the consolidated financial statements and accompanying notes included in "Exhibits and Financial Statement Schedules" in Part IV, Item 15 of this Annual Report on Form 10-K. Reclassifications have been made to the prior years' financial statements to conform to the current year's presentation. Amounts are in thousands, except per share

data.

	Year Ended December 31,			
Operating Data 2016	2015	2014	2013	2012
Total revenues	\$ 500,680			