HEALTHCARE REALTY TRUST INC
Form 10-K
February 15, 2017
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K
(Mark One)
ý 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
For the transition period to
Commission File Number: 001-11852

HEALTHCARE REALTY TRUST INCORPORATED
(Exact name of Registrant as specified in its charter)

Maryland	62-1507028
(State or other jurisdiction of Incorporation or organization)	(I.R.S. Employer Identification No.)

3310 West End Avenue
Suite 700
Nashville, Tennessee 37203
(Address of principal executive offices)
(615) 269-8175
(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 stock, $0.01 par value per share	New York Stock Exchange

Securities Registered Pursuant to Section 12(g) of the Act:
None
(Title of Class)

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) 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. o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b -2 of the Exchange Act. (Check one):

Large accelerated filer	ý	Accelerated filer	o
Non-accelerated filer (Do not check if a smaller reporting company)	o	Smaller reporting company	o

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act.) Yes o No ý

The aggregate market value of the shares of common stock of the Registrant (based upon the closing price of these shares on the New York Stock Exchange on June 30, 2016) held by non-affiliates on June 30, 2016 was $3,650,133,357.

As of January 27, 2017, there were 116,440,289 shares of the Registrant's common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's definitive Proxy Statement relating to the Annual Meeting of Stockholders to be held on May 9, 2017 are incorporated by reference into Part III of this Report.

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FORM 10-K
December 31, 2016

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PART I

Item 1. Business

Overview

Healthcare Realty Trust Incorporated ("Healthcare Realty" or the "Company") is a self-managed and self-administered real estate investment trust ("REIT") that owns, leases, manages, acquires, finances, develops and redevelops income-producing real estate properties associated primarily with the delivery of outpatient healthcare services throughout the United States. The Company was incorporated in Maryland in 1992 and listed on the New York Stock Exchange in 1993.

The Company operates so as to qualify as a REIT for federal income tax purposes. As a REIT, the Company is not subject to corporate federal income tax with respect to taxable income distributed to its stockholders. See "Risk Factors" in Item 1A for a discussion of risks associated with qualifying as a REIT.

Real Estate Properties

The Company had gross investments of approximately $3.6 billion in 202 real estate properties, construction in progress, land held for development and corporate property at December 31, 2016. The Company provided property management services for 146 healthcare-related properties nationwide, totaling approximately 10.3 million square feet as of December 31, 2016. The Company's real estate property investments by geographic area are detailed in Note 2 to the Consolidated Financial Statements. The following table details the Company's owned properties by facility type as of December 31, 2016:

(Dollars and square feet in thousands)	Number of Properties	Gross Investment	Square Feet	Percentage of Square Feet	Occupancy [1] December 31, 2016	December 31, 2015
Medical office/outpatient	182	$3,165,868	13,245	90.8 %	87.4 %	86.7 %
Inpatient	10	344,051	818	5.6 %	100.0 %	100.0 %
Other	10	80,941	518	3.6 %	83.1 %	85.9 %
Sub-Total	202	$3,590,860	14,581	100.0 %	87.9 %	87.6 %
Construction in progress	—	11,655				
Land held for development	—	20,123				
Corporate property	—	5,583				
Total	202	$3,628,221				

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(1) The occupancy columns represent the percentage of total rentable square feet leased (including month-to-month and holdover leases), excluding properties classified as held for sale (two properties as of December 31, 2016 and one property as of December 31, 2015). Properties under property operating or single-tenant net lease agreements are included at 100% occupancy. Upon expiration of these agreements, occupancy reflects underlying tenant leases in the building.

Revenue Concentrations

The Company's real estate portfolio is leased to a diverse tenant base. For the year ended December 31, 2016, the Company did not have any tenants that accounted for 10% or more of the Company's consolidated revenues, including revenues from discontinued operations. The largest revenue concentration is with Baylor Scott & White Health and its affiliates which accounted for 9.8% of the Company's consolidated revenues. These arrangements are spread over 166 leases and 20 buildings. The next largest concentration is with Mercy (St. Louis) at 4.4%.

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Expiring Leases

As of December 31, 2016, the weighted average remaining years to maturity pursuant to the Company's leases were approximately 4.4 years, with expirations through 2036. The table below details the Company's lease maturities as of December 31, 2016, excluding two properties classified as held for sale.

Expiration Year	Number of Leases	Square Feet	Percentage of Square Feet	
2017 (1)	604	2,325,443	18.2	%
2018	387	1,400,606	11.0	%
2019	463	2,344,770	18.3	%
2020	289	1,374,086	10.7	%
2021	278	1,089,943	8.5	%
2022	107	727,731	5.7	%
2023	128	738,186	5.8	%
2024	105	663,874	5.2	%
2025	60	552,119	4.3	%
2026	55	198,128	1.6	%
Thereafter	60	1,373,607	10.7	%

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(1) Includes 50 leases totaling 186,441 square feet that expired prior to December 31, 2016 and are currently on month-to-month terms.

See Trends and Matters Impacting Operating Results as part of Management's Discussion and Analysis of Financial Condition and Results of Operations for additional information regarding the Company's leases and leasing efforts.

Liquidity

The Company believes that its liquidity and sources of capital are adequate to satisfy its cash requirements. The Company expects to meet its liquidity needs through cash on hand, cash flows from operations, property dispositions, equity and debt issuances in the public or private markets and borrowings under commercial credit facilities.

Business Strategy

The Company owns and operates healthcare properties that facilitate the delivery of care in primarily outpatient settings. To execute its strategy, the Company engages in a broad spectrum of integrated services including leasing, management, acquisition, financing, development and redevelopment of such properties. The Company seeks to generate stable, growing income and lower the long-term risk profile of its portfolio of properties by focusing on facilities located on or near the campuses of large, acute care hospitals associated with leading health systems. The Company seeks to reduce financial and operational risk by owning properties in diverse geographic locations with a broad tenant mix that includes over 30 physician specialties, as well as surgery, imaging, cancer and diagnostic centers.

2016 Investment Activity

The Company acquired 10 medical office buildings during 2016 for a total purchase price of $241.9 million, including the assumption of mortgage notes payable of $13.2 million. The weighted average capitalization rate for the 10 medical office buildings was 5.6%. The Company calculates the capitalization rate for an acquisition as the forecasted first year net operating income divided by the purchase price plus acquisition costs and expected capital additions.

The Company disposed of six properties during 2016 for a total sales price of $94.7 million, including $68.0 million for three inpatient rehabilitation facilities. The weighted average capitalization rate for these properties was 8.2%.

In 2016, the Company funded $45.3 million toward development and redevelopment of properties, with two projects underway at December 31, 2016. The Company received a certificate of occupancy for one redevelopment project during the fourth quarter of 2016. This project added 49,089 square feet to one of the Company's existing medical office buildings. Funding of tenant improvements for this project will continue through the first half of 2017 as tenants take occupancy.

See the Company's discussion regarding the 2016 acquisitions and dispositions activity in Note 4 to the Consolidated Financial Statements and development activity in Note 15 to the Consolidated Financial Statements. Also, please refer to the Company's

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discussion in Trends and Matters Impacting Operating Results as part of Management's Discussion and Analysis of Financial Condition and Results of Operations.

Competition

The Company competes for the acquisition and development of real estate properties with private investors, healthcare providers, other REITs, real estate partnerships and financial institutions, among others. The business of acquiring and developing new healthcare facilities is highly competitive and is subject to price, construction and operating costs, and other competitive pressures. Some of the Company's competitors may have lower costs of capital.

The financial performance of all of the Company’s properties is subject to competition from similar properties. The extent to which the Company’s properties are utilized depends upon several factors, including the number of physicians using or referring patients to an associated healthcare facility, healthcare employment, competitive systems of healthcare delivery, and the area’s population, size and composition. Private, federal and state health insurance programs and other laws and regulations may also have an effect on the utilization of the properties. The Company’s properties operate in a competitive environment, and patients and referral sources, including physicians, may change their preferences for a healthcare facility from time to time.

Government Regulation

The facilities owned by the Company are utilized by medical tenants which are required to comply with extensive regulation at the federal, state and local levels, including the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 (collectively, the "Affordable Care Act") and laws intended to combat fraud and waste such as the Anti-Kickback Statute, Stark Law, False Claims Act and Health Insurance Portability and Accountability Act of 1996. These laws and regulations establish, among other things, requirements for state licensure and criteria for medical tenants to participate in government-sponsored reimbursement programs, such as the Medicare and Medicaid programs. The Company's leases generally require the tenant to comply with all applicable laws relating to the tenant's use and occupation of the leased premises. Although lease payments to the Company are not directly affected by these laws and regulations, changes in these programs or the loss by a tenant of its license or ability to participate in government-sponsored reimbursement programs could have a material adverse effect on the tenant's ability to make lease payments to the Company.

The Medicare and Medicaid programs are highly regulated and subject to frequent evaluation and change. Government healthcare spending has increased over time; however, changes from year to year in reimbursement methodology, rates and other regulatory requirements have resulted in a challenging operating environment for healthcare providers. Substantial changes to the Medicare and Medicaid programs may cause the profitability of providing care to Medicare and Medicaid patients to decline, which could adversely affect tenants' ability to make lease payments to the Company.

The Affordable Care Act was intended to provide for comprehensive reform of the United States' healthcare system and extend health insurance benefits to the uninsured population, with the potential to alleviate high uncompensated care expense to healthcare providers. However, the law also increased regulatory scrutiny of providers and insurers by federal and state administrative authorities; lowered annual increases in Medicare payment rates; and implemented cost-saving measures and shared risk-and-reward payment models to promote value and savings, rather than payment for volume of services. These initiatives may slow the growth of healthcare spending over time, but also require providers to expand access and quality of care, presenting the industry and its individual participants with uncertainty and greater financial risk.

The Affordable Care Act continues to be the subject of legal and legislative challenges, including its potential repeal in 2017 by the Republican-led Congress and President Trump’s administration. The repeal of the law, in whole or in part, along with potential health reform replacement legislation, could affect the market for individual health insurance and, indirectly, the economic performance of some or all of the Company's tenants and borrowers. The Company cannot predict the degree to which any changes may affect indirectly the economic performance of the Company, positively or negatively.

Section 603 of the Bipartisan Budget Act of 2015 lowered Medicare rates effective January 1, 2017 for services provided in off-campus, provider-based outpatient departments to the same level of rates for physician-office settings for those facilities not grandfathered-in under the current Medicare rates as of the law’s date of enactment, November

2, 2015. This legislation reflects the movement by the Center for Medicare and Medicaid Services toward reimbursement “site-neutrality,” or equalizing Medicare rates across different facility-type settings. While these changes are expected to lower overall Medicare spending, the Company’s medical office buildings that are located on hospital campuses could become more valuable as hospital tenants will keep their higher Medicare rates for on-campus outpatient services. However, the Company cannot predict the amount of benefit from these measures or if other federal health policy or regulation will ultimately require cuts to reimbursement rates for services provided in other facility-type settings. The Company cannot predict the degree to which these changes, or changes to federal healthcare programs in general, may affect the economic performance of some or all of the Company's tenants, positively or negatively.

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Legislative Developments

Each year, legislative proposals for health policy are introduced in Congress and state legislatures, and regulatory changes are enacted by government agencies. These proposals, individually or in the aggregate, could significantly change the delivery of healthcare services, either nationally or at the state level, if implemented. Examples of significant legislation recently enacted or in the process of implementation include:

- the repeal of the Affordable Care Act and related actions concerning the expansion of Medicaid benefits and the implementation of health insurance exchanges, whether run by the state or by the federal government, whereby individuals and small businesses purchase health insurance, including government-funded plans, many assisted by federal subsidies that are subject to ongoing legal and legislative challenges;
- quality control, cost containment, and payment system reforms for Medicaid and Medicare, such as expansion of pay-for-performance criteria, bundled provider payments, accountable care organizations, increased patient cost-sharing, geographic payment variations, comparative effectiveness research, and lower payments for hospital readmissions;
- implementation of the Medicare Access and CHIP Reauthorization Act of 2015 ("MACRA"), which, if not amended in future legislation, will eventually replace the traditional fee-for-service payment model for physicians with a new value-based payment initiative in which physicians can participate in one of two reimbursement tracks - a merit-based incentive payment system or an advanced alternative payment model; in its final rule for 2017 physician Medicare reimbursement rates, the Center for Medicare and Medicaid Services exempted approximately one-third of physician practices from MACRA compliance in 2017;
- equalization of Medicare payment rates across different facility-type settings; Section 603 of the Bipartisan Budget Act of 2015 lowered Medicare payment rates, effective January 1, 2017 for services provided in off-campus, provider-based outpatient departments to the same level of rates for physician-office settings for those facilities not grandfathered under the current Medicare rates as of the law's date of enactment, November 2, 2015;
- the continued adoption by providers of federal standards for the meaningful-use of electronic health records;
- anti-trust scrutiny of health insurance company mergers; and
- consideration of significant cost-saving overhauls of Medicare and Medicaid, including capped federal Medicaid payments to states, premium-support models to provide for a fixed amount of Medicare benefits per enrollee, and an increase in the eligibility age for Medicare.

The Company cannot predict whether any proposals will be fully implemented, adopted, repealed, or amended, or what effect, whether positive or negative, such proposals might have on the Company's business.

Environmental Matters

Under various federal, state and local environmental laws, ordinances and regulations, an owner of real property (such as the Company) may be liable for the costs of removal or remediation of certain hazardous or toxic substances at, under, or disposed of in connection with such property, as well as certain other potential costs (including government fines and injuries to persons and adjacent property) relating to hazardous or toxic substances. Most, if not all, of these laws, ordinances and regulations contain stringent enforcement provisions including, but not limited to, the authority to impose substantial administrative, civil, and criminal fines and penalties upon violators. Such laws often impose liability, without regard to whether the owner knew of, or was responsible for, the presence or disposal of such substances, and may be imposed on the owner in connection with the activities of a tenant or operator of the property. The cost of any required remediation, removal, fines or personal or property damages and the owner's liability therefore could exceed the value of the property and/or the aggregate assets of the owner. In addition, the presence of such substances, or the failure to properly dispose of or remediate such substances, may adversely affect the owner's ability to sell or lease such property or to borrow using such property as collateral. A property can also be negatively impacted either through physical contamination, or by virtue of an adverse effect on value, from contamination that has or may have emanated from other properties.

Operations of the properties owned, developed or managed by the Company are and will continue to be subject to numerous federal, state, and local environmental laws, ordinances and regulations, including those relating to the following: the generation, segregation, handling, packaging and disposal of medical wastes; air quality requirements related to operations of generators, incineration devices, or sterilization equipment; facility siting and construction;

disposal of non-medical wastes and ash from incinerators; and underground storage tanks. Certain properties owned, developed or managed by the Company contain, and others may contain or at one time may have contained, underground storage tanks that are or were used to store waste oils, petroleum products or other hazardous substances. Such underground storage tanks can be the source of releases of

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hazardous or toxic materials. Operations of nuclear medicine departments at some properties also involve the use and handling, and subsequent disposal of, radioactive isotopes and similar materials, activities which are closely regulated by the Nuclear Regulatory Commission and state regulatory agencies. In addition, several of the Company's properties were built during the period that asbestos was commonly used in building construction and other such facilities may be acquired by the Company in the future. The presence of such materials could result in significant costs in the event that any asbestos-containing materials requiring immediate removal and/or encapsulation are located in or on any facilities or in the event of any future renovation activities.

The Company has had environmental site assessments conducted on substantially all of the properties that it currently owns. These site assessments are limited in scope and provide only an evaluation of potential environmental conditions associated with the property, not compliance assessments of ongoing operations. While it is the Company's policy to seek indemnification from tenants relating to environmental liabilities or conditions, even where leases do contain such provisions, there can be no assurance that the tenant will be able to fulfill its indemnification obligations. In addition, the terms of the Company's leases or financial support agreements do not give the Company control over the operational activities of its tenants or healthcare operators, nor will the Company monitor the tenants or healthcare operators with respect to environmental matters.

Insurance

The Company carries comprehensive liability insurance and property insurance covering its owned and managed properties, including those held under long-term ground leases. In addition, tenants under long-term single-tenant net leases are required to carry property insurance covering the Company's interest in the buildings.

Employees

At December 31, 2016, the Company employed 261 people. The employees are not members of any labor union, and the Company considers its relations with its employees to be excellent.

Available Information

The Company makes available to the public free of charge through its Internet website the Company's Proxy Statement, Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, as soon as reasonably practicable after the Company electronically files such reports with, or furnishes such reports to, the Securities and Exchange Commission ("SEC"). The Company's Internet website address is www.healthcarerealty.com.

The public may read and copy any materials that the Company files with the SEC at the SEC's Public Reference Room located at 100 F Street, NE, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC also maintains electronic versions of the Company's reports on its website at www.sec.gov.

Corporate Governance Principles

The Company has adopted Corporate Governance Principles relating to the conduct and operations of the Board of Directors. The Corporate Governance Principles are posted on the Company's website (www.healthcarerealty.com) and are available in print to any stockholder who requests a copy.

Committee Charters

The Board of Directors has an Audit Committee, Compensation Committee, Corporate Governance Committee and Executive Committee. The Board of Directors has adopted written charters for each committee, except for the Executive Committee, which are posted on the Company's website (www.healthcarerealty.com) and are available in print to any stockholder who requests a copy.

Executive Officers

Information regarding the executive officers of the Company is set forth in Part III, Item 10 of this report and is incorporated herein by reference.

Item 1A. Risk Factors

The following are some of the risks and uncertainties that could negatively affect the Company's consolidated financial condition, results of operations, business and prospects. These risk factors are grouped into three categories: risks relating to the Company's business and operations; risks relating to the Company's capital structure and financings; and risks arising from the Company's status as a REIT and the regulatory environment in which it operates.

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These risks, as well as the risks described in Item 1 under the headings “Competition,” “Government Regulation,” “Legislative Developments,” and “Environmental Matters,” and in Item 7 under the heading “Disclosure Regarding Forward-Looking Statements” should be carefully considered before making an investment decision regarding the Company. The risks and uncertainties described below are not the only ones facing the Company, and there may be additional risks that the Company does not presently know of or that the Company currently considers not likely to have a significant impact. If any of the events underlying the following risks actually occurred, the Company’s business, consolidated financial condition, operating results and cash flows, including distributions to the Company's stockholders, could suffer, and the trading price of its common stock could decline.

Risk relating to our business and operations

The Company's expected results may not be achieved.

The Company's expected results may not be achieved, and actual results may differ materially from expectations. This may be the result of various factors, including, but not limited to: changes in the economy; the availability and cost of capital at favorable rates; increases in property taxes, changes to facility-related healthcare regulations; changes in interest rates; competition for quality assets; negative developments in the operating results or financial condition of the Company's tenants, including, but not limited to, their ability to pay rent and repay loans; the Company's ability to reposition or sell facilities with profitable results; the Company's ability to re-lease space at similar rates as vacancies occur; the Company's ability to timely reinvest proceeds from the sale of assets at similar yields; government regulations affecting tenants' Medicare and Medicaid reimbursement rates and operational requirements; unanticipated difficulties and/or expenditures relating to future acquisitions and developments; changes in rules or practices governing the Company's financial reporting; and other legal and operational matters.

The Company’s revenues depend on the ability of its tenants under its leases to generate sufficient income from their operations to make rent, loan and lease guaranty payments to the Company.

The Company’s revenues are subject to the financial strength of its tenants and associated health systems. The Company has no operational control over the business of these tenants and associated health systems who face a wide range of economic, competitive, government reimbursement and regulatory pressures and constraints. Any slowdown in the economy, decline in the availability of financing from the capital markets, and changes in healthcare regulations may adversely affect the businesses of the Company’s tenants to varying degrees. Such conditions may further impact such tenants’ abilities to meet their obligations to the Company and, in certain cases, could lead to restructurings, disruptions, or bankruptcies of such tenants. In turn, these conditions could adversely affect the Company’s revenues and could increase allowances for losses and result in impairment charges, which could decrease net income attributable to common stockholders and equity, and reduce cash flows from operations.

The Company may decide or may be required under purchase options to sell certain properties. The Company may not be able to reinvest the proceeds from sales at rates of return equal to the return received on the properties sold. Uncertain market conditions could result in the Company selling properties at unfavorable rates or at losses in the future.

The Company had approximately $173.7 million, or 4.8% of the Company’s real estate property investments, that were subject to purchase options held by lessees that were exercisable as of December 31, 2016 or could become exercisable in 2017. Other properties have purchase options that will become exercisable in future periods. Properties with options exercisable in 2017 produced aggregate net operating income (operating revenues, such as property operating revenue, single-tenant net lease revenue, and property lease guaranty revenue, less property operating expense) of approximately $17.8 million in 2016. The exercise of these purchase options exposes the Company to reinvestment risk and a reduction in investment return. Certain properties subject to purchase options are producing returns above the rates of return the Company expects to achieve with new investments. If the Company is unable to reinvest the sale proceeds at rates of return equal to the return received on the properties that are sold, it may experience a decline in lease revenues and profitability and a corresponding material adverse effect on the Company’s business and financial condition, the Company’s ability to make distributions to its stockholders, and the market price of its common stock. For more specific information concerning the Company’s purchase options, see “Purchase Options” in the “Trends and Matters Impacting Operating Results” section of this report.

Owning real estate and indirect interests in real estate is subject to inherent risks.

The Company's operating performance and the value of its real estate assets are subject to the risk that if its properties do not generate revenues sufficient to meet its operating expenses, including debt service, the Company's cash flow and ability to pay dividends to stockholders will be adversely affected.

The Company may incur impairment charges on its real estate properties or other assets.

The Company performs an impairment review on its real estate properties every year. In addition, the Company assesses the potential for impairment of identifiable intangible assets and long-lived assets, including real estate properties, whenever events occur or a change in circumstances indicates that the recorded value might not be fully recoverable. The decision to sell a property also requires the Company to assess the potential for impairment. At some future date, the Company may determine that an impairment has occurred in the value of one or more of its real estate properties or other assets. In such an event, the

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Company may be required to recognize an impairment which could have a material adverse effect on the Company's consolidated financial condition and results of operations.

If the Company is unable to promptly re-let its properties, if the rates upon such re-letting are significantly lower than the previous rates or if the Company is required to undertake significant expenditures to attract new tenants, then the Company's business, consolidated financial condition and results of operations would be adversely affected.

A portion of the Company's leases will expire over the course of any year. For more specific information concerning the Company's expiring leases, see "Multi-Tenant Leases" and "Single-Tenant Net Leases" in the Trends and Matters Impacting Operating Results as part of Management's Discussion and Analysis of Financial Condition and Results of Operations. The Company may not be able to re-let space on terms that are favorable to the Company or at all. Further, the Company may be required to make significant capital expenditures to renovate or reconfigure space to attract new tenants. If unable to promptly re-let its properties, if the rates upon such re-letting are significantly lower than the previous rates, or if the Company is required to undertake significant capital expenditures in connection with re-letting units, the Company's business, consolidated financial condition and results of operations, the Company's ability to make distributions to the Company's stockholders and the trading price of the Company's common stock may be materially and adversely affected.

Certain of the Company's properties are special purpose healthcare facilities and may not be easily adaptable to other uses.

Some of the Company's properties are specialized medical facilities. If the Company or the Company's tenants terminate the leases for these properties or the Company's tenants lose their regulatory authority to operate such properties, the Company may not be able to locate suitable replacement tenants to lease the properties for their specialized uses. Alternatively, the Company may be required to spend substantial amounts to adapt the properties to other uses. Any loss of revenues and/or additional capital expenditures occurring as a result may have a material adverse effect on the Company's business, financial condition and results of operations, the Company's ability to make distributions to its stockholders, and the market price of the Company's common stock.

The Company has, and in the future may have more, exposure to fixed rent escalators, which could lag behind inflation.

The Company receives a significant portion of its revenues by leasing assets subject to fixed rent escalations. Eighty percent of leases have increases that are based upon fixed percentages, fourteen percent of leases have increases based on the Consumer Price Index and six percent have no increase. If the fixed percentage increases begin to lag behind inflation, the Company's growth and profitability would be negatively impacted.

The Company's real estate investments are illiquid and the Company may not be able to sell properties strategically targeted for disposition.

Because real estate investments are relatively illiquid, the Company's ability to adjust its portfolio promptly in response to economic or other conditions is limited. Certain significant expenditures generally do not change in response to economic or other conditions, including debt service (if any), real estate taxes, and operating and maintenance costs. This combination of variable revenue and relatively fixed expenditures may result in reduced earnings and could have an adverse effect on the Company's financial condition. In addition, the Company may not be able to sell properties targeted for disposition, including properties held for sale, due to adverse market conditions. This may negatively affect, among other things, the Company's ability to sell properties on favorable terms, execute its operating strategy, repay debt, pay dividends or maintain its REIT status.

The Company is subject to risks associated with the development and redevelopment of properties.

The Company expects development and redevelopment of properties will continue to be a key component of its growth plans. The Company is subject to certain risks associated with the development and redevelopment of properties including the following:

- The construction of properties generally requires various government and other approvals that may not be received when expected, or at all, which could delay or preclude commencement of construction;
- Opportunities that the Company pursued but later abandoned could result in the expensing of pursuit costs, which could impact the Company's consolidated results of operations;

- Construction costs could exceed original estimates, which could impact the building's profitability to the Company;
- Operating expenses could be higher than forecasted;
- Time required to initiate and complete the construction of a property and to lease up a completed property may be greater than originally anticipated, thereby adversely affecting the Company's cash flow and liquidity;

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- Occupancy rates and rents of a completed development property may not be sufficient to make the property profitable to the Company; and

- Favorable capital sources to fund the Company's development and redevelopment activities may not be available when needed.

The Company may make material acquisitions and undertake developments and redevelopments that may involve the expenditure of significant funds and may not perform in accordance with management's expectations.

The Company regularly pursues potential transactions to acquire, develop or redevelop real estate assets. Future acquisitions could require the Company to issue equity securities, incur debt or other contingent liabilities or amortize expenses related to other intangible assets, any of which could adversely impact the Company's consolidated financial condition or results of operations. In addition, equity or debt financing required for such acquisitions may not be available at favorable times or rates.

The Company's acquired, developed and existing real estate properties may not perform in accordance with management's expectations because of many factors including the following:

- The Company's purchase price for acquired facilities may be based upon a series of market or building-specific judgments which may be incorrect;

- The costs of any maintenance or improvements for properties might exceed estimated costs;

- The Company may incur unexpected costs in the acquisition, construction or maintenance of real estate assets that could impact its expected returns on such assets; and

- Leasing may not occur at all, within expected time frames or at expected rental rates.

Further, the Company can give no assurance that acquisition, development and redevelopment opportunities that meet management's investment criteria will be available when needed or anticipated.

The Company is exposed to risks associated with geographic concentration.

As of December 31, 2016, the Company had investment concentrations of greater than 5% of its total investments in the Dallas, Texas (13.4%) and Seattle, Washington (11.2%) markets. These concentrations increase the exposure to adverse conditions that might affect these markets, including natural disasters, local economic conditions, local real estate market conditions, increased competition, state and local regulation, including property taxes, and other localized events or conditions.

Many of the Company's leases are dependent on the viability of associated health systems. Revenue concentrations relating to these leases expose the Company to risks related to the financial condition of the associated health systems.

The Company's revenue concentrations with tenants are diversified, with the largest revenue concentration relating to Baylor Scott & White Health and its affiliates, which accounted for 9.8% of the Company's consolidated revenues. The next largest concentration is with Mercy (St. Louis) at 4.4%.

Most of the Company's properties on or adjacent to hospital campuses are largely dependent on the viability of the health system's campus where they are located, whether or not the hospital or health system is a tenant in such properties. The viability of these health systems depends on factors such as the quality and mix of healthcare services provided, competition, demographic trends in the surrounding community, market position and growth potential. If one of these hospitals is unable to meet its financial obligations, is unable to compete successfully, or is forced to close or relocate, the Company's properties on or near such hospital campus could be adversely impacted.

Many of the Company's properties are held under ground leases. These ground leases contain provisions that may limit the Company's ability to lease, sell, or finance these properties.

As of December 31, 2016, the Company had 99 properties that were held under ground leases, including one property with construction in progress, representing an aggregate gross investment of approximately $1.8 billion. The weighted average remaining term of the Company's ground leases is approximately 69.4 years, including renewal options. The Company's ground lease agreements with hospitals and health systems typically contain restrictions that limit building occupancy to physicians on the medical staff of an affiliated hospital and prohibit tenants from providing services that compete with the services provided by the affiliated hospital. Ground leases may also contain consent requirements or other restrictions on sale or assignment of the Company's leasehold interest, including rights of first offer and first refusal in favor of the lessor. These ground lease provisions may limit the Company's ability to lease, sell, or obtain mortgage financing secured by such properties which, in turn, could adversely affect the income from operations or the proceeds received from a sale. As a ground lessee, the Company is also exposed to the risk of reversion of the property upon expiration of the ground lease term, or an earlier breach by the Company of the ground lease, which may have a material adverse effect on the Company's business, consolidated

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financial condition and results of operations, the Company’s ability to make distributions to the Company’s stockholders and the trading price of the Company’s common stock.

The Company may experience uninsured or underinsured losses related to casualty or liability.

The Company carries comprehensive liability insurance and property insurance covering its owned and managed properties. In addition, tenants under long-term single-tenant net leases are required to carry property insurance covering the Company’s interest in the buildings. Some types of losses may be uninsurable or too expensive to insure against. Should an uninsured loss or a loss in excess of insured limits occur, the Company could lose all or a portion of the capital it has invested in a property, as well as the anticipated future revenue from the property. In such an event, the Company might remain obligated for any mortgage debt or other financial obligation related to the property. The Company cannot give assurance that material losses in excess of insurance proceeds will not occur in the future.

The Company is subject to cyber security risks.

A cyber-attack that bypasses the Company's information technology (“IT”) security systems causing an IT security breach may lead to a material disruption of the Company's IT business systems and/or the loss of business information resulting in an adverse business impact. Risks may include:

- future results could be adversely affected due to the theft, destruction, loss, misappropriation or release of confidential data or intellectual property;
- operational or business delays resulting from the disruption of IT systems and subsequent clean-up and mitigation activities; and/or
- negative publicity resulting in reputation or brand damage with the Company's tenants, health systems or other operators.

Risks relating to our capital structure and financings

The Company has incurred significant debt obligations and may incur additional debt and increase leverage in the future.

As of December 31, 2016, the Company had approximately $1.3 billion of outstanding indebtedness and the Company’s leverage ratio [debt divided by (debt plus stockholders’ equity less intangible assets plus accumulated depreciation)] was 33.9%. Covenants under the Credit Agreement, dated as of October 14, 2011, among the Company and Wells Fargo Bank, National Association, as Administrative Agent, and the other lenders that are party thereto, as amended (“Unsecured Credit Facility”), the Term Loan Agreement, dated as of February 27, 2014, among the Company, Wells Fargo Bank, National Association, as Administrative Agent, and the other lenders that are party thereto, as amended (the “Unsecured Term Loan due 2019”) and the indentures governing the Company’s senior notes permit the Company to incur substantial, additional debt, and the Company may borrow additional funds, which may include secured borrowings. A high level of indebtedness would require the Company to dedicate a substantial portion of its cash flows from operations to service the debt, thereby reducing the funds available to implement the Company’s business strategy and to make distributions to stockholders. A high level of indebtedness could also:

- limit the Company’s ability to adjust rapidly to changing market conditions in the event of a downturn in general economic conditions or in the real estate and/or healthcare industries;
- impair the Company’s ability to obtain additional debt financing or require potentially dilutive equity to fund obligations and carry out its business strategy; and
- result in a downgrade of the rating of the Company’s debt securities by one or more rating agencies, which would increase the costs of borrowing under the Unsecured Credit Facility and the cost of issuance of new debt securities, among other things.

In addition, from time to time, the Company secures or assumes mortgages to partially fund its investments. If the Company is unable to meet its mortgage payments, then the encumbered properties could be foreclosed upon or transferred to the mortgagee with a consequent loss of income and asset value. A foreclosure on one or more of the Company's properties could have a material adverse effect on the Company’s consolidated financial condition and results of operations.

Covenants in the Company’s debt instruments limit its operational flexibility, and a breach of these covenants could materially affect the Company’s consolidated financial condition and results of operations.

The terms of the Unsecured Credit Facility, the Unsecured Term Loan due 2019, the indentures governing the Company’s outstanding senior notes and other debt instruments that the Company may enter into in the future are subject to customary financial and operational covenants. These provisions include, among other things: a limitation on the incurrence of additional indebtedness; limitations on mergers, investments, acquisitions, redemptions of capital stock, transactions with affiliates; and maintenance of specified financial ratios. The Company's continued ability to incur debt and operate its business is subject to compliance with these covenants, which limit operational flexibility. Breaches of these covenants could result in defaults under applicable debt instruments, even if payment obligations are satisfied. Financial and other covenants that limit the Company's operational flexibility, as well as defaults resulting from a breach of any of these covenants in its debt instruments, could have a material adverse effect on the Company's consolidated financial condition and results of operations.

A change to the Company's current dividend payment may have an adverse effect on the market price of the Company's common stock.

The ability of the Company to pay dividends is dependent upon its ability to maintain funds from operations and cash flow, to make accretive new investments and to access capital. There can be no assurance that the Company will continue to pay dividends at current amounts, or at all. A failure to maintain dividend payments at current levels could result in a reduction of the market price of the Company's common stock.

If lenders under the Unsecured Credit Facility fail to meet their funding commitments, the Company's operations and consolidated financial position would be negatively impacted.

Access to external capital on favorable terms is critical to the Company's success in growing and maintaining its portfolio. If financial institutions within the Unsecured Credit Facility were unwilling or unable to meet their respective funding commitments to the Company, any such failure would have a negative impact on the Company's operations, consolidated financial condition and ability to meet its obligations, including the payment of dividends to stockholders.

The unavailability of equity and debt capital, volatility in the credit markets, increases in interest rates, or changes in the Company's debt ratings could have an adverse effect on the Company's ability to meet its debt payments, make dividend payments to stockholders or engage in acquisition and development activity.

A REIT is required by the Internal Revenue Code of 1986, as amended (the "Internal Revenue Code"), to make dividend distributions, thereby retaining less of its capital for growth. As a result, a REIT typically requires new capital to invest in real estate assets. However, there may be times when the Company will have limited access to capital from the equity and/or debt markets. Changes in the Company's debt ratings could have a material adverse effect on its interest costs and financing sources. The Company's debt rating can be materially influenced by a number of factors including, but not limited to, acquisitions, investment decisions, and capital management activities. In recent years, the capital and credit markets have experienced volatility and at times have limited the availability of funds. The Company's ability to access the capital and credit markets may be limited by these or other factors, which could have an impact on its ability to refinance maturing debt, fund dividend payments and operations, acquire healthcare properties and complete development and redevelopment projects. If the Company is unable to refinance or extend principal payments due at maturity of its various debt instruments, its cash flow may not be sufficient to repay maturing debt and, consequently, make dividend payments to stockholders. If the Company defaults in paying any of its debts or satisfying its debt covenants, it could experience cross-defaults among debt instruments, the debts could be accelerated and the Company could be forced to liquidate assets for less than the values it would otherwise receive.

The Company is exposed to increases in interest rates, which could adversely impact its ability to refinance existing debt, sell assets or engage in acquisition and development activity.

The Company receives a significant portion of its revenues by leasing its assets under long-term leases in which the rental rate is generally fixed, subject to annual rent escalators. A significant portion of the Company's debt may be subject to floating rates, based on LIBOR or other indices. The generally fixed nature of revenues and the variable rate of certain debt obligations create interest rate risk for the Company. Increases in interest rates could make the financing of any acquisition or investment activity more costly. Rising interest rates could limit the Company's ability to refinance existing debt when it matures or cause the Company to pay higher rates upon refinancing. An increase in interest rates also could have the effect of reducing the amounts that third parties might be willing to pay for real estate assets, which could limit the Company's ability to sell assets at times when it might be advantageous to do so.

The Company may enter into swap agreements from time to time that may not effectively reduce its exposure to changes in interest rates.

The Company has entered into swap agreements in the past and may enter into such agreements to manage some of its exposure to interest rate volatility. These swap agreements involve risks, such as the risk that counterparties may fail to honor their obligations under these arrangements. In addition, these arrangements may not be effective in reducing the Company's exposure to changes in interest rates. When the Company uses forward-starting interest rate swaps, there is a risk that it will not complete the long-term borrowing against which the swap is intended to hedge. If such events occur, the Company's results of operations may be adversely affected.

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Risks relating to government regulations

If a healthcare tenant loses its licensure or certification, becomes unable to provide healthcare services, cannot meet its financial obligations to the Company or otherwise vacates a facility, the Company would have to obtain another tenant for the affected facility.

If the Company loses a tenant or sponsoring health system because such tenant loses its license or certification, becomes unable to provide healthcare services, cannot meet its financial obligations to the Company or otherwise vacates a facility, and the Company is unable to attract another healthcare provider on a timely basis and on acceptable terms, the Company's cash flows and results of operations could suffer. Transfers of operations of healthcare facilities are often subject to regulatory approvals not required for transfers of other types of commercial operations and real estate.

Adverse trends in the healthcare service industry may negatively affect the Company's lease revenues and the values of its investments.

The healthcare service industry may be affected by the following:

- trends in the method of delivery of healthcare services;
- competition among healthcare providers;
- consolidation of large health insurers;
- lower reimbursement rates from government and commercial payors, high uncompensated care expense, investment losses and limited admissions growth pressuring operating profit margins for healthcare providers;
- availability of capital;
- credit downgrades;
- liability insurance expense;
- regulatory and government reimbursement uncertainty resulting from the Affordable Care Act and other healthcare reform laws;
- efforts to repeal, replace or modify the Affordable Care Act in whole or in part;
- health reform initiatives to address healthcare costs through expanded value-based purchasing programs, bundled provider payments, health insurance exchanges, increased patient cost-sharing, geographic payment variations, comparative effectiveness research, lower payments for hospital readmissions, and shared risk-and-reward payment models such as accountable care organizations;
- federal court decisions on cases challenging the legality of certain aspects of the Affordable Care Act;
- federal and state government plans to reduce budget deficits and address debt ceiling limits by lowering healthcare provider Medicare and Medicaid payment rates, while requiring increased patient access to care;
- equalizing Medicare payment rates across different settings;
- heightened health information technology security standards and the meaningful use of electronic health records by healthcare providers; and

- potential tax law changes affecting non-profit providers.

These changes, among others, can adversely affect the economic performance of some or all of the tenants and sponsoring health systems who provide financial support to the Company's investments and, in turn, negatively affect the lease revenues and the value of the Company's property investments.

If the Company fails to remain qualified as a REIT, the Company will be subject to significant adverse consequences, including adversely affecting the value of its common stock.

The Company intends to operate in a manner that will allow it to continue to qualify as a REIT for federal income tax purposes. Although the Company believes that it qualifies as a REIT, it cannot provide any assurance that it will continue to qualify as a

REIT for federal income tax purposes. The Company's continued qualification as a REIT will depend on the satisfaction of certain asset, income, organizational, distribution, stockholder ownership and other requirements on a continuing basis. The Company's ability to satisfy the asset tests depends upon the characterization and fair market values of its assets. The Company's compliance with the REIT income and quarterly asset requirements also depends upon the Company's ability to successfully manage the composition of the Company's income and assets on an ongoing basis. Accordingly, there can be no assurance that the Internal Revenue Service ("IRS") will not contend that the Company has operated in a manner that violates any of the REIT requirements.

If the Company were to fail to qualify as a REIT in any taxable year, the Company would be subject to federal income tax, including any applicable alternative minimum tax, on its taxable income at regular corporate rates and possibly increased state and local taxes (and the Company might need to borrow money or sell assets in order to pay any such tax). Further, dividends paid to the Company's stockholders would not be deductible by the Company in computing its taxable income. Any resulting corporate tax liability could be substantial and would reduce the amount of cash available for distribution to the Company's stockholders, which in turn could have an adverse impact on the value of, and trading prices for, the Company's common stock. In addition, in such event the Company would no longer be required to pay dividends to maintain REIT status, which could adversely affect the value of the Company's common stock. Unless the Company were entitled to relief under certain provisions of the Internal Revenue Code, the Company also would continue to be disqualified from taxation as a REIT for the four taxable years following the year in which the Company failed to qualify as a REIT.

Even if the Company remains qualified for taxation as a REIT, the Company is subject to certain federal, state and local taxes on its income and assets, including taxes on any undistributed taxable income, and state or local income, franchise, property and transfer taxes. These tax liabilities would reduce the Company's cash flow and could adversely affect the value of the Company's common stock. For more specific information on state income taxes paid, see Note 16 to the Consolidated Financial Statements.

The Company's Articles of Incorporation contain limits and restrictions on transferability of the Company's common stock which may have adverse effects on the value of the Company's common stock.

In order to qualify as a REIT, no more than 50% of the value of the Company's outstanding shares may be owned, directly or indirectly, by five or fewer individuals (as defined in the Internal Revenue Code to include certain entities) during the last half of a taxable year. To assist in complying with this REIT requirement, the Company's Articles of Incorporation contain provisions restricting share transfers where the transferee (other than specified individuals involved in the formation of the Company, members of their families and certain affiliates, and certain other exceptions) would, after such transfer, own (a) more than 9.9% either in number or value of the outstanding common stock of the Company or (b) more than 9.9% either in number or value of any outstanding preferred stock of the Company. If, despite this prohibition, stock is acquired increasing a transferee's ownership to over 9.9% in value of either the outstanding common stock or any preferred stock of the Company, the stock in excess of this 9.9% in value is deemed to be held in trust for transfer at a price that does not exceed what the purported transferee paid for the stock, and, while held in trust, the stock is not entitled to receive dividends or to vote. In addition, under these circumstances, the Company has the right to redeem such stock. These restrictions on transfer of the Company's shares could have adverse effects on the value of the Company's common stock.

Dividends payable by REITs do not qualify for the reduced tax rates available for some dividends.

The federal tax rate applicable to income from "qualified dividends" payable to certain domestic stockholders that are individuals, trusts and estates is currently the preferential tax rate applicable to long-term capital gains. Dividends payable by REITs, however, are generally not qualified dividends and do not qualify for the preferential tax rate. The more favorable rates applicable to regular corporate qualified dividends could cause investors who are individuals, trusts and estates to perceive investments in REITs to be relatively less attractive than investments in the stocks of non-REIT corporations that pay dividends, which could adversely affect the value of the stock of REITs, including the Company's common stock.

Complying with the REIT requirements may cause the Company to forego otherwise attractive opportunities.

To qualify as a REIT for federal income tax purposes, the Company must continually satisfy tests concerning, among other things, the sources of its income, the nature of its assets, the amounts it distributes to its stockholders and the ownership of its stock. The Company may be unable to pursue investments that would be otherwise advantageous to the Company in order to satisfy the source-of-income or distribution requirements for qualifying as a REIT. Thus, compliance with the REIT requirements may hinder the Company's ability to make certain attractive investments.

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

Qualification as a REIT involves the application of highly technical and complex provisions of the Internal Revenue Code for which only limited judicial and administrative authorities exist. Even a technical or inadvertent violation could jeopardize the Company's REIT qualification. The Company's continued qualification as a REIT will depend on the Company's satisfaction of certain asset, income, organizational, distribution, stockholder ownership and other requirements on a continuing basis. In

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addition, the Company’s ability to satisfy the requirements to qualify as a REIT depends in part on the actions of third parties over which the Company has no control or only limited influence, including in cases where the Company owns an equity interest in an entity that is classified as a partnership for U.S. federal income tax purposes.

New legislation or administrative or judicial action, in each instance potentially with retroactive effect, could make it more difficult or impossible for the Company to qualify as a REIT.

The present federal income tax treatment of REITs may be modified, possibly with retroactive effect, by legislative, judicial or administrative action at any time, which could affect the federal income tax treatment of an investment in the Company. The federal income tax rules that affect REITs are constantly under review by persons involved in the legislative process, the IRS and the U.S. Treasury Department, which results in statutory changes as well as frequent revisions to regulations and interpretations. Revisions in federal tax laws and interpretations thereof could cause the Company to change its investments and commitments and affect the tax considerations of an investment in the Company. There can be no assurance that new legislation, regulations, administrative interpretations or court decisions will not change the tax laws significantly with respect to the Company’s qualification as a REIT or with respect to the federal income tax consequences of qualification.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

In addition to the properties described in Item 1, “Business,” in Note 2 to the Consolidated Financial Statements, and in Schedule III of Item 15 of this Annual Report on Form 10-K, the Company leases office space from an unrelated third party for its headquarters, which are located at 3310 West End Avenue in Nashville, Tennessee. The Company’s corporate office lease currently covers approximately 36,653 square feet of rented space and expires on October 31, 2020. Annual base rent on the corporate office lease increases approximately 3.25% annually. The Company’s base rent for 2016 was approximately $0.9 million.

Item 3. Legal Proceedings

The Company is not aware of any pending or threatened litigation that, if resolved against the Company, would have a material adverse effect on the Company's consolidated financial position, results of operations, or cash flows.

Item 4. Mine Safety Disclosures

Not applicable.

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PART II

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

Shares of the Company's common stock are traded on the New York Stock Exchange under the symbol "HR." At December 31, 2016, there were 1,076 stockholders of record. The following table sets forth the high and low sales prices per share of common stock, and the dividends declared and paid per share of common stock related to the periods indicated.

	High	Low	Dividends Declared and Paid per Share
2016			
First Quarter	$31.09	$27.50	$ 0.30
Second Quarter	35.00	29.42	0.30
Third Quarter	36.60	32.80	0.30
Fourth Quarter (Dividend payable on February 28, 2017)	34.28	26.66	0.30
2015			
First Quarter	$31.20	$26.03	$ 0.30
Second Quarter	28.39	23.10	0.30
Third Quarter	25.24	22.01	0.30
Fourth Quarter	28.51	24.64	0.30